

# MEMBER PROPOSALS FOR TAX REFORM

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HEARING  
BEFORE THE  
SUBCOMMITTEE ON SELECT REVENUE MEASURES  
OF THE  
COMMITTEE ON WAYS AND MEANS  
U.S. HOUSE OF REPRESENTATIVES  
ONE HUNDRED NINTH CONGRESS  
FIRST SESSION

JULY 28, 2005

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## **MEMBER PROPOSALS FOR TAX REFORM**

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**THURSDAY, JULY 28, 2005**

U.S. HOUSE OF REPRESENTATIVES,  
COMMITTEE ON WAYS AND MEANS,  
SUBCOMMITTEE ON SELECT REVENUE MEASURES,  
*Washington, DC.*

The Subcommittee met, pursuant to notice, at 10:00 a.m., in room 1100, Longworth House Office Building, Hon. Dave Camp (Chairman of the Subcommittee) presiding.

[The advisory announcing the hearing follows:]

# ADVISORY

FROM THE COMMITTEE ON WAYS AND MEANS

## SUBCOMMITTEE ON SELECT REVENUE MEASURES

FOR IMMEDIATE RELEASE  
July 13, 2005  
SRM-4

CONTACT: (202) 225-1721

### **Camp Announces Hearing on Member Proposals for Tax Reform**

Congressman Dave Camp (R-MI), Chairman, Subcommittee on Select Revenue Measures of the Committee on Ways and Means, today announced that the Subcommittee will hold a hearing on various tax reform proposals by Members of the U.S. House of Representatives. **The hearing will take place on Thursday, July 28, 2005, in the main Committee hearing room, 1100 Longworth House Office Building, beginning at 10:00 a.m.**

Testimony will be received from Members of Congress alone during the hearing. However, any individual or organization not scheduled for an oral appearance may submit a written statement for consideration by the Subcommittee and for inclusion in the printed record of the hearing.

#### **BACKGROUND:**

On January 7, 2005, President Bush established the Advisory Panel on Federal Tax Reform. The Panel has been holding hearings throughout the country to solicit the opinions of leading experts, academics, and practitioners on reforming the Tax Code. Recognizing the burden imposed by the current Federal Tax Code in terms of compliance and growth incentives, the President's stated goal is to explore options to reform the Tax Code to make it simpler, fairer, and more pro-growth. The Panel is expected to report to the Secretary of the U.S. Department of the Treasury by September 30, 2005.

More than 14,000 changes have been made to the Tax Code since the last major reform effort in 1986. The Tax Code imposes economic distortions that cost the U.S. economy as much as 50 cents for every additional dollar raised, and causes taxpayers to waste 3.2 billion hours and as much as \$100 billion complying with an increasingly complex system.

On June 8, 2005, the full Committee held the first in a series of hearings on tax reform. That hearing focused on the broad overview of the principle economic objectives of tax reform, including fairness, simplicity, and impacts on growth.

In announcing the hearing, Chairman Camp stated, "As the Committee begins to review the formal recommendations of the President's Advisory Panel on Federal Tax Reform, the Subcommittee will examine how reform proposals made by Members of Congress may satisfy the President's objectives of fair, simple, and growth-oriented tax reform."

#### **FOCUS OF THE HEARING:**

The focus of the hearing will be to examine proposals made by Members of the U.S. House of Representatives that satisfy the President's objectives of fair, simple, and growth-oriented tax reform.

#### **DETAILS FOR SUBMISSIONS OF REQUESTS TO BE HEARD:**

Requests to be heard at the hearing must be made by telephone to Michael Morrow or Kevin Herms at (202) 225-1721 no later than the close of business on Friday, July 22, 2005. The telephone request should be followed by a formal written request

faxed to Allison Giles, Chief of Staff, Committee on Ways and Means, U.S. House of Representatives, 1102 Longworth House Office Building, Washington, D.C. 20515, at (202) 225-0942. The staff of the Subcommittee will notify by telephone those scheduled to appear as soon as possible after the filing deadline. Any questions concerning a scheduled appearance should be directed to the Subcommittee staff at (202) 226-5911.

Members scheduled to present oral testimony are required to summarize briefly their written statements in no more than five minutes. The five-minute rule will be strictly enforced. The full written statement of each Member will be included in the printed record, in accordance with House Rules.

In order to assure the most productive use of the limited amount of time available to question witnesses, all Members scheduled to appear before the Subcommittee are required to submit 200 copies, along with an *IBM compatible 3.5-inch diskette in WordPerfect or MS Word format*, of their prepared statement for review by Members prior to the hearing. **Testimony should arrive at the Subcommittee office, 1135 Longworth House Office Building, no later than Tuesday, July 26, 2005.**

#### **WRITTEN STATEMENTS IN LIEU OF PERSONAL APPEARANCE:**

**Please Note:** Any person(s) and/or organization(s) wishing to submit for the hearing record must follow the appropriate link on the hearing page of the Committee website and complete the informational forms. From the Committee homepage, <http://waysandmeans.house.gov>, select "109th Congress" from the menu entitled, "Hearing Archives" (<http://waysandmeans.house.gov/Hearings.asp?congress=17>). Select the hearing for which you would like to submit, and click on the link entitled, "Click here to provide a submission for the record." Once you have followed the on-line instructions, completing all informational forms and clicking "submit" on the final page, an email will be sent to the address which you supply confirming your interest in providing a submission for the record. You **MUST REPLY** to the email and **ATTACH** your submission as a Word or WordPerfect document, in compliance with the formatting requirements listed below, by close of business on Wednesday, August 31, 2005. **Finally**, please note that due to the change in House mail policy, the U.S. Capitol Police will refuse sealed-package deliveries to all House Office Buildings. Those filing written statements who wish to have their statements distributed to the press and interested public at the hearing can follow the same procedure listed above for those who are testifying and making an oral presentation. For questions, or if you encounter technical problems, please call (202) 225-1721.

#### **FORMATTING REQUIREMENTS:**

The Committee relies on electronic submissions for printing the official hearing record. As always, submissions will be included in the record according to the discretion of the Committee. The Committee will not alter the content of your submission, but we reserve the right to format it according to our guidelines. Any submission provided to the Committee by a witness, any supplementary materials submitted for the printed record, and any written comments in response to a request for written comments must conform to the guidelines listed below. Any submission or supplementary item not in compliance with these guidelines will not be printed, but will be maintained in the Committee files for review and use by the Committee.

1. All submissions and supplementary materials must be provided in Word or WordPerfect format and MUST NOT exceed a total of 10 pages, including attachments. Witnesses and submitters are advised that the Committee relies on electronic submissions for printing the official hearing record.

2. Copies of whole documents submitted as exhibit material will not be accepted for printing. Instead, exhibit material should be referenced and quoted or paraphrased. All exhibit material not meeting these specifications will be maintained in the Committee files for review and use by the Committee.

3. All submissions must include a list of all clients, persons, and/or organizations on whose behalf the witness appears. A supplemental sheet must accompany each submission listing the name, company, address, telephone and fax numbers of each witness.

Note: All Committee advisories and news releases are available on the World Wide Web at <http://waysandmeans.house.gov>.

The Committee seeks to make its facilities accessible to persons with disabilities. If you are in need of special accommodations, please call 202-225-1721 or 202-226-3411 TTD/TTY in advance of the event (four business days notice is requested). Questions with regard to special accommodation needs in general (including availability of Committee materials in alternative formats) may be directed to the Committee as noted above.

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Chairman CAMP. The hearing of the Subcommittee on Select Revenue Measures will come to order. On January 7, 2005, President Bush established the President's Advisory Panel on Federal Tax Reform. The panel has held ten hearings throughout the country to solicit the opinions of leading experts, academics, and practitioners on reforming the Tax Code. The President's goal is for the panel to explore options to reform the Tax Code, to make it simpler, fairer, and more pro-growth. The panel is expected to provide recommendations to the Secretary of the Treasury by September 30, 2005. The bipartisan panel is chaired by former Senators Connie Mack and John Breaux, both distinguished former Members of the United States Senate Committee on Finance. The panel also includes distinguished former members of the government, academia, and the business community, including a distinguished former Member of the House Committee on Ways and Means, Mr. Bill Frenzel.

Similar to the bipartisan nature of the President's panel, we have a bipartisan panel of Members of the U.S. House of Representatives testifying before us today. The composition of our witnesses serves as testimony to the fact that both parties recognize that the current U.S. tax system is broken and needs to be fixed for the benefit of working families. In anticipation of the formal recommendations of the President's panel in September, the goal of this hearing is to examine how tax reform proposals made by Members of the U.S. House of Representatives satisfy the President's objectives of simple, fair, and growth-oriented tax reform. These topics are among the most serious issues Members of the Ways and Means Committee will face. I want to welcome our witnesses' and colleagues' views as to how we might address them. I now yield to the Ranking Member, Mr. McNulty, for a statement.

Mr. MCNULTY. Thank you, Mr. Chairman. Today's hearing is a follow-up to last month's full Committee hearing on the economic aspects of tax reform legislation. I welcome each Member of the House appearing before the Subcommittee this morning. I thank you all for your contributions to the ongoing debate on tax reform and look forward to the discussion of your proposals. Bipartisan hearings, such as our hearing today, provide Members of the Subcommittee with valuable insight into the merits of various approaches for improving our tax system. The Congress, in a bipartisan manner, needs to press for tax simplification as a goal and as a priority. Having said that, I would caution against establishing a totally new system of assessing and collecting Federal taxes, which raises serious questions about fairness and effective tax administration. Whether a flat tax, a retail sales tax, or a value-added tax (VAT), I suggest that the Subcommittee and the Committee accept the offer of the IRS Commissioner to brief the Committee on problems his European and other international coun-



terparts have shared with him about the serious noncompliance problems they face in administering their tax system. In short, Mr. Chairman, we should fix any problems that may exist in our Tax Code, not throw it out in its entirety. I thank you, Mr. Chairman, and yield back the balance of my time.

Chairman CAMP. Thank you very much. Our panel today includes the Honorable Richard Neal, a Member of the Committee, and a Member from the State of Massachusetts; the Honorable Phil English, a Member of the Ways and Means Committee, from the State of Pennsylvania; the Honorable John Linder, also a Member of the Committee, from the State of Georgia; the Honorable Rahm Emanuel, a Member of the full Committee, from the State of Illinois; the Honorable Dennis Kucinich, a Representative in Congress from the State of Ohio; the Honorable Timothy Bishop, a Representative from the State of New York; and the Honorable Michael Burgess, a Representative from the State of Texas. As you know, in this Committee, you will each have 5 minutes, and we will begin with the Honorable Richard E. Neal. We have your written testimony, and if you could summarize your testimony for us, we would appreciate it. We thank all of you for taking the time to come today, in a very busy week, to share your views on fundamental tax reform. Mr. Neal?

**STATEMENT OF THE HONORABLE RICHARD E. NEAL, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MASSACHUSETTS**

Mr. NEAL. Thank you very much, Mr. Chairman. I just had an interesting moment. I have been a constant critic of the Alternative Minimum Tax (AMT), and I have just had three of my former staffers that are here, as well as my current staff—and I have been very fortunate. I have had very competent tax advisers who have worked for me. It also tells the story of my woe. Three former members of my staff, who are still toiling on the Hill, have all worked on this issue, and we are no closer to fixing it than we were when they began. Mr. Camp, Mr. McNulty, and fellow Ways and Means Members, I want to thank you for giving me this opportunity to testify before you today on H.R. 2950, the Individual Tax Simplification Act, which I introduced last month. As the title implies, my bill is designed to attack the overwhelming complexity embedded in our Nation's Tax Code.

Today's Internal Revenue Code contains 1.5 million words, hundreds of thousands of which have been added in the last 10 years alone. As you might guess, those massive additions to the Tax Code have not made it easier to fill out a 1040 form. Americans now spend more time than ever handling their taxes: 3.5 billion hours per year, for an average of about 25 hours per return. That is more than half of a work week. As a result, record numbers of Americans—60 percent—are giving up filling out their own tax forms and are instead paying tax preparers, at an average cost of between \$100 and \$150. For many families, that represents a full day's wages. Other taxpayers receive assistance from volunteer services or from the IRS, leaving only a third of taxpayers to file their taxes with no help whatsoever. It does not have to be this way. For the past four Congresses, I have authored a bill that would streamline

the Tax Code, and make it more transparent and understandable. Crucially, the bill is revenue neutral. My legislation would attack three hefty sources of complexity in the Tax Code. First, it would enact a paid-for repeal of the AMT. Second, it would untangle the mess that we have made of nonrefundable personal credits, by instituting uniform phase-outs of credits for adoption, children, and education. Third, it would streamline the jumble of rates and forms that govern long-term capital gains, and replace it, instead, with a simple 38-percent exclusion.

Altogether, my bill would wipe out about 200 lines from tax reforms, schedules, and work sheets, drastically reducing the amount of time needed to file. The AMT alone is estimated to add 12 hours to the filing process, and under my bill it would disappear. As all of you know, the AMT is not problematic only because of its complexity, but because it is a revenue monster steadily swallowing up the rest of our Tax Code and shifting an ever increasing burden onto the backs of middle-income families. At one time, the AMT was a “class tax,” levied on the wealthiest Americans to ensure that they did not overuse certain tax breaks to avoid paying any taxes. Now, it is a “mass tax,” which CRS projects would reach 41 million Americans by 2013. By the end of this decade, the majority of taxpayers with income between \$75,000 and \$100,000 will be forced to pay the AMT, as will almost all married couples with two or more children in that income range. Up to now, Congress has employed various stop-gap measures to patch the AMT temporarily, but these will not work forever. The problem will get worse the longer we allow it to fester, and retaining the status quo is really not an option. At the same time, repeal of the AMT is expected to cost between \$700 billion and \$1.1 trillion over the next 10 years, so repealing the AMT without a pay-for would be a fiscally reckless policy.

My legislation would counterbalance AMT repeal, by placing an additional income tax on adjusted gross income exceeding \$120,000 for joint filers and \$90,000 for single taxpayers. The rate of that tax would be doubled for income above \$150,000 for joint filers and \$112,000 for single taxpayers. All of these thresholds would be indexed to inflation, and the bill requires the Secretary of the Treasury to set a rate that makes the bill revenue neutral over the first 10 years of its enactment. The goal of my bill is to simplify the Tax Code, not to provide a tax increase or cut, nor to redistribute wealth. There is no responsible way to repeal the AMT and offer a free lunch, and I cannot underscore that message more clearly. The numbers simply do not add up. We must tackle the AMT repeal, and that requires us to make hard choices. My bill attempts to achieve these objectives, while balancing fiscal responsibility with equity and fairness. Mr. Chairman, Mr. McNulty, simplifying the Tax Code is a goal that we all share and we all frequently talk about, but it certainly is easier to talk about it than to achieve it. I am glad that we are beginning to dialogue once again on how we get from here to there. It is going to require a lot of cooperation, a lot of bipartisanship, and I am eager to join all of you in pursuing these goals. This is the first step today. I am glad you are doing this, Mr. Chairman, and I hope that this will be a process that we can engage in through the coming year as well. Seldom have I been

aligned with an issue that has drawn more favorable attention to my position and less action. Thank you for your time.

[The prepared statement of Mr. Neal follows:]

**Statement of The Honorable Richard E. Neal, a Representative in Congress from the State of Massachusetts**

Chairman Camp and Ranking Member McNulty, and fellow Ways and Means Members, I want to thank you for giving me the opportunity to testify before you today on H.R. 2950, the Individual Tax Simplification Act, which I introduced last month. As its title implies, my bill is designed to attack the overwhelming complexity embedded in our nation's tax code.

Today's Internal Revenue Code contains 1.5 million words, hundreds of thousands of which have been added in the last ten years alone. As you might guess, those massive additions to the tax code haven't made it easier to fill out a 1040 form. Americans now spend more time than ever before handling their taxes: 3.5 billion hours per year, for an average of about 25 hours per return. That's more than half of a work week.

As a result, record numbers of Americans—sixty percent—are giving up on filling out their own tax forms and are instead hiring paid tax preparers, at an average cost of between \$100 and \$150. For many families, that represents a full day's wages. Other taxpayers receive assistance from volunteer services or from the IRS, leaving only a third of taxpayers to file their taxes with no help whatsoever.

But it just doesn't have to be this way. For the past four Congresses, I have authored a bill that would streamline the tax code and make it more transparent and understandable. And, crucially, the bill is *revenue neutral*. My legislation would attack three hefty sources of complexity in the tax code.

- First, it would enact a paid-for repeal of the Alternative Minimum Tax.
- Second, it would untangle the mess that we've made of nonrefundable personal credits, by instituting uniform phaseouts of credits for adoption, children, and education.
- Third, it would streamline the jumble of rates and forms that govern long term capital gains and replace it instead with a simple 38 percent exclusion.

Altogether, my bill would wipe out 200 lines from tax forms, schedules, and worksheets, drastically reducing the amount of time needed to file. The AMT alone is estimated to add 12 hours to the filing process, and under my bill it would disappear.

As all of you know, the AMT isn't problematic only because of its complexity but because it is a revenue monster steadily swallowing up the rest of our tax code and shifting an ever-increasing burden onto the backs of middle income families. At one time, the AMT was a "class tax," levied on the wealthiest Americans to ensure that they did not overuse certain tax breaks to avoid paying any taxes. Now it's a "mass tax," which CRS projects would reach 41 million Americans by 2013. By the end of this decade, the majority of taxpayers with income between \$75,000 and \$100,000 will be forced to pay the AMT, as will almost all married couples with two or more children in that income range.

Up to now, Congress has employed various stopgap measures to patch the AMT temporarily, but these won't work forever. The problem will get worse the longer we allow it to fester, and retaining the status quo is not an option. At the same time, total repeal of the AMT is expected to cost between \$700 billion and \$1.1 trillion over the next ten years, so repealing the AMT without a pay-for would be a fiscally reckless policy.

My bill would counterbalance AMT repeal by placing an additional income tax on adjusted gross income exceeding \$120,000 for joint filers and \$90,000 for single taxpayers. That rate of that tax would be doubled for income above \$150,000 for joint filers and \$112,000 for single taxpayers. All of the thresholds would be indexed to inflation, and the bill requires the Secretary of the Treasury to set a rate that makes the bill revenue neutral over the first ten years of its enactment.

The goal of my bill is to simplify the tax code, not to provide a tax increase or cut, nor to redistribute wealth. There is no responsible way to repeal the AMT and offer a free lunch; the numbers just don't add up. We must tackle AMT repeal, and it will require hard choices. My bill attempts to achieve these objectives while balancing fiscal responsibility with equity and fairness.

Mr. Chairman and Mr. McNulty, simplifying the tax code is a goal that we all share, but it has always been easier to talk about it than to achieve it. I'm glad that we're beginning the dialogue about how to get from here to there. It will re-

quire a lot of cooperation and a lot of work, and I am eager to join my colleagues in pursuing these goals. Today's hearing is an excellent first step, and I thank you for the opportunity to participate.

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Chairman CAMP. Thank you very much, Mr. Neal. The Honorable Phil English, a distinguished Member of the full Ways and Means Committee, you have 5 minutes. Welcome.

**STATEMENT OF THE HONORABLE PHIL ENGLISH, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF PENNSYLVANIA**

Mr. ENGLISH. Thank you, Chairman Camp, Members of the Committee, for the opportunity to appear before you today. If I could, I would like to submit my full testimony for the record and summarize, as is customary in this setting.

Chairman CAMP. Without objection.

Mr. ENGLISH. In my view, the American tax system is too complicated and riddled with obvious inequities. It punishes savings and investment, while reducing economic growth and burdening domestic industry, struggling to remain competitive. To address these inequities, and because I want to reform the American tax system in a way that makes sense to the average citizen, I am advocating the Simplified USA Tax Act (SUSAT), which I have introduced in previous Congresses and I will be reintroducing this coming fall. I am currently in the midst of updating several provisions, which have been impacted significantly by the many positive tax changes this Committee and the Congress have made in recent years. The principles which are the pillars of the Simplified USA Tax will remain fully intact. Not only do we need a Tax Code that is fair and sensible, we need one that is stable. As bad as the current Tax Code is—and I am certainly one of its critics—the last thing we need to enact is a reform that is so radical and experimental that we have to redo it all over again a few years hence.

The new Tax Code I have developed—the Simplified USA Tax, or SUSAT—is based on sound and familiar doctrines that are easy to understand. It also meets all of the criteria President Bush laid out when he created an advisory panel to make recommendations to fundamentally change the Code. First, SUSAT significantly simplifies the Tax Code and does so by a factor by some estimates of about 75 percent. Second, it is progressive while it preserves the importance of homeownership and charitable giving. Finally—and in my view, most importantly—it provides the right incentives for the U.S. economy to thrive globally. Although the Joint Committee on Taxation (JCT) has never completed a revenue score of SUSAT, it was written to be revenue neutral. The USA Tax for individuals is simplicity itself, a true minimalist approach that achieves a great deal without a lot of complex rules.

First, the Tax Code must give Americans a fair opportunity to save part of their earnings. In my tax reform proposal, USA stands for “unlimited savings allowance.” Everyone is allowed an unlimited Roth IRA in which they can put the portion of each year's income they save after paying taxes and living expenses. After 5 years, all money in the account can be withdrawn for any purposes,

and all withdrawals—including accumulated interest and other earnings or principal—are tax free. The Tax Code must also give everyone the opportunity to keep what they save and, if they wish, to pass it along to succeeding generations. To that end, my tax reform proposal repeals permanently the Federal estate and gift taxes.

Under the new Tax Code, tax rates must remain low, especially for wage earners who now pay both an income tax and a FICA payroll tax on the same wage base. The Simplified USA Tax starts out with low tax rates—three progressive rates in the range of 10 to 25 percent. Then the rates are reduced further by allowing wage earners a full tax credit for the 7.65 percent Social Security and Medicare payroll tax that is withheld from their paychecks under current law. I do not propose to repeal the payroll tax, but I do allow a credit for it. When the credit is taken into account, the rates of tax on workers' wages are low indeed. This proposal provides tax relief for all Americans, especially those who own their home, give to their church, educate their children, and set aside some savings for a better future. Under my proposal, everyone gets a deduction for the mortgage interest on their home and for charitable contributions they make. My proposal also contained a new and better way of taxing corporations and other businesses that will allow them to compete and win in global markets in a way that exports American-made products, not American jobs.

All businesses, corporate and non-corporate, are taxed alike at an 8-percent rate on the first \$150,000 of profit and at 12 percent on all amounts above that small business level. All businesses will be allowed a credit for the payroll tax they pay under current law. All costs for plant, equipment, and inventory will be expended into the year of purchase. If they are to survive and prosper, American manufacturers must make big-dollar purchases of capital goods, but they need the lower cost and financing help that first-year expensing provides. Another key element on the business side is the way income earned outside of our borders is taxed. What we need to move toward—and what SUSAT embodies—is a system that does not tax foreign-source income on a worldwide basis or export sales of American-made products and services. The absence of some type of border tax adjustments for exports of American-made goods to correspond to the export rebates under foreign countries' value-added tax systems puts our businesses—manufacturers and eventually service providers—at a serious disadvantage.

Under SUSAT, all export sales income is exempt, as is all other foreign-source income, and all profits earned abroad can be brought back for reinvestment in America without penalty. In conclusion, the Simplified USA Tax is a hybrid of the others we often hear about. The plan combined the great strengths of other mainstream tax proposals and, most importantly, it does not contain their individual weaknesses. For too long the Tax Code has been a needless drag on the economy. This is unproductive as a national policy. More importantly, it is unfair to those Americans whose living standards are lower because of it. I thank you, Mr. Chairman and Members of the Subcommittee, for the opportunity to testify.

[The prepared statement of Mr. English follows:]

**Statement of The Honorable Phil English, a Representative in Congress  
from the State of Pennsylvania**

Thank you Chairman Camp, Members of the Committee, for the opportunity to appear before you today. The American tax system is a Frankenstein's monster that haunts individual taxpayers while casting a cold shadow over the productive sectors of the U.S. economy. It is too complicated, and riddled with obvious inequities. It punishes savings and investment, while reducing economic growth and burdening domestic industry struggling to remain competitive.

To address these inequities and because I want to reform the American tax system in a way that makes sense to average citizens, I am advocating the *Simplified USA Tax Act*, which I have introduced in previous Congresses. I will be reintroducing the proposal this coming fall; I am currently in the midst of updating several provisions which have been impacted by the many positive tax changes this Committee and the Congress have made in recent years. But the principles which are the pillars of the *Simplified USA Tax* will remain fully intact. Not only do we need a tax code that is fair and sensible, we need one that is stable. As bad as the current tax code is—and I am certainly one of its critics—the last thing we need is to enact some reform that is so radical and experimental that we have to redo it all over again a few years later.

The new tax code I have developed—the *Simplified USA Tax Act* or “SUSAT”—is based on sound and familiar doctrines that are easy to understand. It also meets all of the criteria President Bush laid out when he created an advisory panel to make recommendations to fundamentally change the tax code. First, SUSAT significantly simplifies the tax code—and does so by a factor of 75 percent; second, it is progressive while it preserves the importance of homeownership and charitable giving; and finally—and in my view, most importantly—provides the right incentives for the U.S. economy to thrive globally. Although the Joint Committee on Taxation had never completed a revenue score of SUSAT, it was written to be revenue neutral.

***Taxing Individuals***

The USA Tax for individuals is simplicity itself; a true minimalist approach that achieves a great deal without a lot of complex rules. In addition to providing a simple way to calculate taxes, the USA Tax brings several key reforms to the table.

First, the tax code must give Americans a fair opportunity to save part of their earnings. Thrift has helped provide Americans the security and independence that is the foundation of freedom. Savings buys the tools to make Americans more productive. Productivity raises our living standards to the highest in the world.

In my tax reform proposal, “USA” stands for unlimited savings allowance. Everyone is allowed an unlimited Roth IRA in which they can put the portion of each year's income they save after paying taxes and living expenses. After five years, all money in the account can be withdrawn for any purpose and all withdrawals—including accumulated interest and other earnings or principal—are tax free. Nothing could give the people a better opportunity to save; especially young people. Because only new income earned after enactment of the *Simplified USA Tax* can be put in the USA Roth IRA, young people starting to move into their higher-earning years are the ones who will benefit the most for the longest time.

The tax code must also give everyone the opportunity to keep what they save and, if they wish, to pass it along to succeeding generations. To that end, my tax reform proposal repeals the federal estate and gift taxes.

Under the new tax code, tax rates must be low; especially for wage earners who now pay both an income tax and a FICA payroll tax on the same amount of wages. The *Simplified USA Tax* starts out with low tax rates—three progressive rates in the range of 10 percent to 25 percent. Then, the rates are reduced even further by allowing wage earners a full tax credit for the 7.65 percent Social Security and Medicare payroll tax that is withheld from their paychecks under current law. I do not propose to repeal the payroll tax, but I do allow a credit for it and when the credit is taken into account, the rates of tax on workers' wages are very low indeed.

The *Simplified USA Tax* provides tax relief for all Americans, especially those who own their home, give to their church, educate their children and set aside some savings for a better tomorrow. Under my proposal, everyone gets a deduction for the mortgage interest on their home and for charitable contributions they make. In addition—and this is brand new and long overdue in my opinion—the USA plan allows a deduction for tuition paid for college and post-secondary vocational education. The annual limit is \$4,000 per person and \$12,000 for a family. Generous personal and family exemptions are also allowed under my proposal.

The *Simplified USA Tax* is simplicity itself. The tax return will be short, only a page or two for most of us, but more to the point, the tax return will be *understandable*. For the first time in a very long time, America's tax system will make sense to the citizens who file the tax returns and pay the taxes. Since inception of the federal income tax, Americans will have a full and fair opportunity to save whatever portion of their income they wish and for whatever purpose they wish. For the first time, working people will be allowed a credit for the payroll tax they pay, and also for the first time, families will have generous tax-free allowance for the education of their children.

#### ***Taxing Businesses***

My proposal also contains a new and better way of taxing corporations and other businesses that will allow them to compete and *win* in global markets in a way that exports American-made products, not American jobs. I have studied this issue and believe that, if enacted in America, this approach to business taxation will soon become the worldwide standard to which other countries aspire.

All businesses—corporate and non-corporate—are taxed alike at an 8 percent rate on the first \$150,000 of profit and at 12 percent on all amounts above that small business level. All businesses will be allowed a credit for the payroll tax they pay under current law.

All costs for plant, equipment and inventory will be expended into the year of purchase. This is a major departure from our current, and frankly archaic, depreciation system, but a crucial element of the *Simplified USA Tax*. If they are to survive and prosper, American manufacturers must make big-dollar purchases of capital goods, but they need the lower cost and financing help that first-year expensing provides. If American manufacturers have state-of-the-art machinery and equipment, they will not only create high-paying jobs, they will be able to compete effectively with low-cost producers outside of the U.S.

In the year 2002, Congress enacted a 30% expensing allowance followed by a 50% allowance stopped which reversed a two-year decline in capital spending that was one of the worst in history. Every economic principle and every piece of data tells us that first-year expensing must be a major component of fundamental tax reform because it directly translates into high-paying manufacturing jobs and decreases the cost-of-capital.

Another key element of the business side of the *Simplified USA Tax* is the way income earned outside of our borders is taxed. What we need to move towards—and what SUSAT embodies—is a system that does not tax foreign-source income on a worldwide basis or export sales of American-made products and services. The absence of some type of border tax adjustments for exports of American-made goods to correspond to the export rebates under foreign countries' Value Added Tax systems puts our businesses—manufacturers and eventually service providers—at a severe disadvantage. If anyone doubts the disadvantage American exporters are faced with, they ought to look at our trade deficit of astronomical proportions.

Under SUSAT, all export sales income is exempt, as is all other foreign-source income, and all profits earned abroad can be brought back home for reinvestment in America without penalty. Because of a 12 percent import adjustment, all companies that produce abroad and sell back into U.S. markets will be required to bear the same tax as companies that both produce and sell in the U.S.

#### ***Conclusion***

The *Simplified USA Tax* is a hybrid of the others we often hear about. This plan combines the biggest strengths of other mainstream tax proposals and most importantly, it does not contain their weaknesses. For too long the tax code has been a needless drag on the economy. This is unproductive as a national policy and more importantly, is unfair to those Americans whose living standards are lower because of it. For years, its complex inanities have been the object of ridicule. It is also the ultimate source of bureaucratic excess that is inconsistent with a free society. It is high time that we restore people's faith in the integrity and competence of their tax system and, in the process, take a major step toward restoring people's confidence in the good character of their government.

Thank you Chairman Camp, and Members of the Committee for the opportunity to testify.

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Chairman CAMP. Thank you, Mr. English. Now, the Honorable John Linder of Georgia, who is also a Member of the Select Revenue Measures Subcommittee, you have 5 minutes.

**STATEMENT OF THE HONORABLE JOHN LINDER, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF GEORGIA**

Mr. LINDER. Thank you, Mr. Chairman, and Members of the Committee. My bill, H.R. 25, the FairTax, would abolish all taxes on income of any source, and tax only personal consumption at the retail checkout. It gets rid of the corporate income tax, the personal income tax, the payroll tax, which is the largest tax, three-fourths of us pay. It gets rid of the AMT on a revenue neutral basis, the gift tax, the estate tax, for the retail sales tax. It is simple, replaces 60,000 pages with 132 pages. It is fair. It untaxes everyone up to the poverty level spending, totally—as the Tax Commission said, it is the only proposal that totally untaxes the poor. It is voluntary. You pay taxes when you choose, as much as you choose, by how you choose to spend. It is transparent. Instead of having a 22 percent hidden tax on everything, we pay for now—that is the Harvard study, 22 percent of the price system represents the tax component—you will see on your receipt for that loaf of bread exactly how much you paid the government. It is border neutral. It treats imports exactly the same as our domestic competition. Imports coming from China would be taxed 23 cents in a General Agreement on Tariffs and Trade (GATT)-compliant, World Trade Organization (WTO)-compliant way. It is industry neutral. We should not be charging the guy down the street—or putting the guy down the street who sells books at a disadvantage to amazon.com. That is a huge problem for States losing collections to Internet catalogue sales. It strengthens Social Security by going from 158 million payers to 296 million citizens and 51 million visitors to our shores every time they buy something.

Mr. Chairman, there are several economic forces that are driving us toward this. The 22 percent tax component of the price system makes us less than competitive. We spend \$400 to \$500 billion a year complying with this Code. That is like paying for a dead horse. That produces no jobs, produces no wealth. We have driven into the underground economy, not participating in our tax system, between \$1.5 and \$3 trillion, and the more complex we get, the easier it is to go underground, and the more difficult it is to be found. We have driven in dollar-denominated deposits in offshore financial centers \$10 trillion. Ten trillion dollars not in our markets. If we are to get rid of the IRS and all taxes on income, all of those would be fixed. There is simply no way to fix any of them by nibbling around the edges of the current system. Why do we want \$10 trillion back in our economy, in our markets? If it were to come, we would eliminate all of the pension problems every major corporation has because the markets would be driven up. We have two market managers, whose names you would recognize, who have looked at this and said, “I don’t know what the Dow Jones would be at when this becomes effective, but in 2 years, it will have doubled.”

Now, let me tell you something that this does that no one ever thinks about. We have never taxed wealth in this country. We tax wages, and people who are living on their wages have no latitude to adjust the way they live. People living on wealth can do it. If you recall, Mrs. Heinz Kerry had to disclose how much revenue she had in 2003 during the campaign. It was \$6.1 million. She paid a



12 percent tax, and likely paid nothing into Social Security or Medicare because she had no earned income. Ross Perot put \$3.5 billion from the sale of his company into municipal bonds, paid nothing in taxes and had no earned income, paid nothing into Social Security. It is likely that Bill Gates spends \$10 million a year personally. He probably pays nothing into Social Security because he has no earned income. Under our system, he would pay \$800,000 into Social Security and Medicare, 8 percent of that would go into Social Security and Medicare.

We need to get off the system of taxing wages, and start thinking about taxing wealth. We believe that people who earn more spend more, and people who spend more will contribute more to the tax system. We will have many contributions to charities even if it is not deductible. The American people gave \$43 billion to charities in 1980, when the value of a charitable contribution at the margin was 70 percent. In 1988, when the value was 28 percent, they gave \$88 billion. The great fortunes that have been given away in this country, the Goulds, the Fricks, the Carnegies and Mellons, were given away before 1913. People with lots of money give lots of money away. Under our system, the average income earner is going to have a 50-percent increase in take-home pay. They will have money in their pockets, and they will be able to afford to give to charity. Mr. Chairman, thanks for this opportunity. I stand ready to take any questions you might have.

[The prepared statement of Mr. Linder follows:]

**Statement of The Honorable John Linder, a Representative in Congress  
from the State of Georgia**

Mr. Chairman, Ranking Democratic Member McNulty, and Members of the Subcommittee, I appreciate having the opportunity to testify today.

IRS bashing has become a sport in this country. Whenever I mention the possibility of abolishing the IRS at a town hall meeting, I'm greeted with thunderous applause. And while I know that we can all recite the horror stories of overzealous IRS agents or unhelpful and unknowledgeable IRS staff, I think that it is important that we as Members of Congress accept our role in making the IRS frightening and the tax code loathsome.

There are numbers that we can all quote by heart—more than 14,000 changes since 1986, 10 million words of code and regulation, 6.6 billion hours each year to comply, 60% of Americans forced to use professional tax preparers—and these are not the fault of the IRS bureaucracy. Rather, responsibility for these numbers—numbers that would be laughable if not so painful—lies squarely with you and me. I congratulate the Chairman for holding this hearing as an important step in accepting responsibility for our errant past and charting a new course for the future.

I think that there is a real debate in Congress about what taking responsibility for this tax morass means. There are those who believe that the responsible thing is to leave in place our current system—a system literally tried and tested over 90-plus years of frustration, arbitration, litigation and incarceration—and to limit it to impacting as few people as possible. This is a very easy and very doable path, and while the monster that is the income tax code will remain in place, we could limit it to feeding on as few citizens as possible. Simply raising the floor of the AMT and eliminating tax returns for most Americans would address constituent ire. Going one step further and eliminating all personal income taxes in favor of higher taxes on big business and capital might be even more popular. Again, these are relatively easy changes.

Mr. Chairman, the point that I would like to make today is that “easy” is not necessarily “better.” I would argue that if we take this historic opportunity to reform our system of taxation and we do something “easy” then we are not accepting the mantle of responsibility for our past failings and in fact we are simply passing the buck and failing once again.

I certainly believe that one of our goals should be to make paying taxes easy, but it is but one of our goals. We must lift the foot of our tax system off of the neck of our economy and free the American worker and the American consumer.

To be competitive in international markets, we must have a border-adjustable tax system. How long has the Ways and Means Committee worked to provide some measure of relief from this burden for American companies doing business abroad? DISC . . . FSC . . . ETI . . . the list of acronyms that have tried and failed to address this issue is long. For more than 30 years we have tried these band-aid solutions to a problem that we know is real. The FairTax—for the first time—will heal this economic wound fully and permanently.

The FairTax is the only Congressional proposal that abolishes corporate taxes. For too long, the costs and complexities of the tax code have been levied on business, which simply hides the burden in higher prices for American consumers. Not only do these hidden taxes burden American goods as we try to compete in international markets but they also hide the true cost of government from American consumers here at home.

The FairTax also removes the highly regressive and hidden payroll tax from both workers' paychecks and the price of goods. Not only is the payroll tax doomed to failure as a funding mechanism for Social Security and Medicare, but it stands as the largest tax that Americans pay. How can we claim to tackle the burdens and complexities of the American tax code if we fail to address the largest tax that Americans pay? The answer is that we cannot, and yet the FairTax is the only major piece of legislation that takes on this challenge.

Just last week, the President's Advisory Panel on Tax Reform, with the help of the Treasury Department, concluded that the FairTax is the only reform proposal that completely untaxes the poor. I want to say that again: The FairTax is the only reform proposal that completely untaxes the poor. Today, we use exemptions and deductions, we use cash payments in the form of the fraud-riddled earned income tax credit, and we still fail to provide the opportunity society that we've promised to low-income Americans. For the first time, the FairTax fulfills this promise. Even more, it ends the punishment of American workers as they struggle to climb the ladder of success.

The CBO reported in March—as it does every March—about where the burden of Federal taxation falls. The CBO found, as it has every year since it began tracking these numbers in 1979, that while the effective income tax rate on the poor is actually negative the effective payroll tax on those same Americans is incredibly high. In fact, we have so manipulated the income tax code in this country that it is only those Americans with the highest quintile of incomes—those at \$175,000 and higher—who pay more in income taxes than payroll taxes. For the other four quintiles—80% of all Americans—the payroll tax burden is higher and larger than the income tax burden. It is simply folly to discuss tax reform without discussing this burden, and yet the FairTax is the only major reform proposal that does.

The reports above make it clear that a personal consumption tax of 23% is more favorable to working Americans than the current 10% or 15% income tax that is filled with credits and exemptions designed by Washington to make their lives better. The demagogues are always available to exacerbate the confusion. I expect that we might even hear some of that today. While the motive of some might be to confuse, others simply are confused, and who can blame them? The current system with its cascading taxes hidden at every level of income and consumption denies Americans that opportunity to understand exactly what their tax burden is. The FairTax by design ends the deception.

An interesting part of my experience promoting this bill has been responding to myriad calculations of what the rate of the FairTax would need to be. All sorts of outlandish numbers have been calculated including one of nearly 60% by the Joint Tax Committee some number of years ago. I confess that these erroneous guesstimates used to be very frustrating to me, but now I simply use them to make my point. You see, I don't care what the rate has to be for revenue neutrality. The math is what it is. I value the transparency and the efficiency of removing all of the hidden taxes and having the complete tax figure available for all Americans to see. With a near zero percent savings rate in this country, consumption and income by definition are the same thing . . . so if a detractor calculates that a revenue neutral FairTax rate would actually be 60%, by definition the current tax rate on all of America—when you pull all the hidden taxes together into one place—must also be 60%. If I spend everything that I earn, and the tax man needs 60 cents out of every dollar that I spend, in the alternative he would also need 60 cents out of every dollar that I earn. I ask that you take this point to heart as this Committee continues this process.

Transparency, border-adjustability, simplicity, and progressivity are all found in the FairTax. With a 600,000 member (and growing) grassroots organization on the ground in every state in America, the FairTax has amassed more cosponsors—both this Congress and last—than any other piece of fundamental tax reform legislation. It has been the subject of Committee hearings and has been poked and prodded by economists from the left and the right. I appreciate the opportunity to testify about the FairTax again today, and I look forward to working with the Subcommittee to make this bill a reality.

Thank you, Mr. Chairman.

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Chairman CAMP. Thank you, Mr. Linder. Now, the Honorable Rahm Emanuel, a distinguished Member of the full Committee, from Illinois.

**STATEMENT OF THE HONORABLE RAHM EMANUEL, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF ILLINOIS**

Mr. EMANUEL. Thank you, Mr. Chairman. I have introduced the Middle-Class Tax Fairness Act. Now, in my district office, I run—between January 1st to April—tax clinics, helping folks fill out the tax forms that we have. We have a tax assistance program for them, and over 1,000 families have benefited from it. What the problem is, because of the complexity of the Code, related specifically to achieve the American dream, we have to literally help people get, whether it is the earned income tax credit, the education deduction, the type of dollars that we have said are important to achieve in their life. So, what I have tried to do here is take the buying of a home, education of a child, raising a child, and saving for retirement, the basic pillars of a middle-class life, and simplify the Code as it relates to that part of the Code, as it penalizes, I think, middle-class families accomplishing the American dream. Just in the last 4 years, we have added 10,000 pages to the Code. One would think that the complexity is done by design in that effort. So, let's take it and try to knock these off real quickly. I know you have questions, and I know we have other Members here who want to speak.

The college tax credit. In that area we have five different types of deductions that exist in the Code, and depending on how you want to look at it, some think it is as high as nine. We would simplify that and take it down—and, actually, it takes 85 pages of notes and a booklet on how to fill out the IRS tax portions as it relates to higher education, going to a college, or a community school—85 pages to analyze what you have to do to fill it out just to get one deduction, whether it is a lifetime learning, the HOPE scholarship, et cetera. So, we would simplify it with a \$3,000 credit for 4 years of college or 2 years of graduate school, and it cuts the instruction book in half and simplifies the paperwork.

The home mortgage deduction. Presently, about 31 million Americans get the home mortgage deduction, those people who itemize. There are 10 million Americans who pay a mortgage, who make \$50,000 or less, who do not get the deduction. Allow every American who owns a home to get the mortgage deduction, regardless of whether you itemize or not. So, simplify the home mortgage deduction by making it universal.

Taking the raising of a child, we have the earned income tax credit, we have the per-child deduction, and we have the dependent care. Make it the simplified family credit. It takes 200 pages of the Code down to 12 questions. The portion of raising a child and what you would have to do to fill out all of those different forms, with different definitions of what a child is, reduce that down to 12 questions and help the families who are making somewhere between \$14,000 a year and \$30,000 a year, not having a dependency and not living on welfare, chose work, simplify the Code as it relates to raising a child. Then, lastly, retirement, and although we are dealing with this issue in the Social Security debate and in the non-Social Security retirement area. In the last 30 years, the Congresses have added 16 separate provisions to help people save for retirement, and yet, America's saving in the same time has gone from 10 percent down to less than 1 percent. Clearly, what we are doing as it relates to the Tax Code is not working. We have given everybody different definitions from IRA to super IRA to Roth IRAs, and so forth, and it is not adding to America's saving or people participating. Doing more of the same and expecting a different result will only waste dollars.

So, it takes all the different forms of saving for your retirement and makes it a universal pension for all Americans. What you would do is basically reduce the alphabet soup. Every taxpaying American would be able to open up a universal pension at the age of 21. Contribution limits would track those of the IRA, \$4,000 in 2005. For 80 percent of all the small business employees who don't have either a 401(k), they would be able to contribute an extra \$10,000 annually. There is one other key advantage to the universal pension. When people switch jobs, usually because of the complexity of the 401(k), a lot of people who have saved some money end up cashing out and taking their money out of their retirement. This automatically transfers, if you move jobs, your 401(k) into the universal pension, so you don't lose anything. It eliminates the paperwork and the chance that they will cash out their retirement.

Finally, the universal pension would work seamlessly with an expanded and a refundable saver's credit that we have also proposed, some of us, in the debate on retirement security. Individuals earning up to \$30,000 and married couples up to \$60,000, would get a flat 50 percent credit for contributions up to the first \$2,000. So, from retirement, buying a home, raising a child, or sending that child to college, all pillars that make the American dream possible, we would simplify the Tax Code and bring economic opportunity to more and more Americans. Last, I would say as a Democratic principle—and I know I have 20 seconds here left—the President, when he outlined his tax reform commission, he said he wanted this to be revenue neutral. That was his principle. I think for myself, I can speak for myself. My principle is this should be revenue neutral for the middle class. Any tax reform should not raise taxes on the middle class. That is our goal, not what it does to the government but what it does to the middle class families. This would help people not only achieve the American dream, but it would also help us grow the economy. Thank you.

[The prepared statement of Mr. Emanuel follows:]

**Statement of The Honorable Rahm Emanuel, a Representative in Congress  
from the State of Illinois**

Mr. Chairman,

Thank you for the opportunity to testify before the Select Revenue Measures Subcommittee on my tax reform proposal, the Middle-Class Tax Fairness Act.

This proposal will help middle-class families realize the American Dream by making the tax code simpler and fairer in four distinct areas: buying a home, raising children, sending them to college and saving for retirement.

In the last four years, 10,000 new pages have been added to the tax code, most of them adding new tax breaks for special interests. Our tax system is needlessly complicated and burdensome to the middle class. It is long past time for fundamental tax reform that restores equity to the tax code for middle-class families.

When President Bush announced his Advisory Panel on Tax Reform earlier this year, he said his core principle was that it should be revenue-neutral.

I believe the core principle of tax reform should be that it does not increase taxes on the middle class and makes the code simpler and fairer.

Part of the Middle-Class Tax Fairness Act combines all the higher education tax credits into one simple and progressive Simplified College Tax Credit. Nowhere is the need for tax reform more urgent than in the area of education incentives. As *USA Today* wrote, "Want to save for education? Fantastic, but you had better be on good terms with your accountant."

Part of this legislation will make it much easier—and much less expensive—for middle class parents to send their kids to college. The Simplified College Tax Credit combines each of the overlapping and confusing higher education tax credits that exist today into one simple and progressive credit.

Education tax incentives are designed to help families, yet the forms and the instructions that accompany them prevent families from taking full advantage of these incentives. For instance the IRS instruction booklet for the various current education incentives is 85 pages long. The Simplified College Tax Credit would cut that booklet in half.

The second piece of my proposal is the Simplified Family Credit. The Simplified Family Credit will provide meaningful tax relief to middle-income families, stimulate the economy and simplify the tax code, while delivering these benefits in a fiscally responsible way.

It does so by condensing the earned income tax credit, child tax credit, and additional child credit into one expanded credit. In the process, it shrinks 200 pages of tax code down to 12 easy questions.

The third element of this proposal is a Universal Mortgage Deduction that is available to every homeowner, not just to those who can afford to itemize deductions. This provision will enable 10 million more Americans, most of whom earn \$50,000 or less, to deduct the interest payments on their mortgages.

This simple step will help to level the playing field with the 31 million homeowners who currently take the mortgage interest deduction.

The fourth and final provision would create a Universal Pension for all Americans. During the past thirty years, Congress has created sixteen different tax-advantaged retirement savings accounts, each with its own contribution limits, income requirements and definitions.

At the same time, the savings rate has dropped from ten percent in 1980 to just one percent last year. The vast array of accounts creates confusion and acts as a deterrent to those who want to save for retirement but cannot afford to hire an accountant to navigate the sea of options. The Universal Pension would replace the 'alphabet soup' of retirement savings options with one simple account that is portable from job-to-job.

Mr. Chairman, the Middle Class Tax Fairness Act will add simplicity and fairness to the tax code while making it more equitable for America's families.

Thank you again for the opportunity to testify before this Subcommittee. I look forward to answering your questions.

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Chairman CAMP. All right. Thank you, Mr. Emanuel. The Honorable Dennis Kucinich from Ohio, you have 5 minutes, and your written statement will be a part of the record.

**STATEMENT OF THE HONORABLE DENNIS J. KUCINICH, A  
REPRESENTATIVE IN CONGRESS FROM THE STATE OF OHIO**

Mr. KUCINICH. I want to thank the Chairman, Mr. Camp, and the Ranking Member, Mr. McNulty, for the opportunity to testify. Thank you for holding this hearing. I would like to bring to your attention a proposal I introduced in the last Congress, H.R. 3655, the Progressive Tax Act of 2003, which will have a positive impact on millions of taxpayers. I think it is fair to say that all Members of Congress believe we need to strive for a fair, simple, and adequate tax system. We may disagree on how this has been accomplished, but we have the same goals. However, I think we can also agree on the need for transparency. Transparency in the tax system is necessary to achieve fairness. Transparency permits the taxpayer to understand how fairness is arrived in the Tax Code. A simplified Tax Code can provide this transparency, which in turn provides a sense of trust in the government.

This Committee should enact my proposal to create a \$2,000 simplified family credit, a refundable tax credit that simplifies the Tax Code by consolidating the earned income tax credit, the child tax credit, additional child credit, and dependent exemption for children into one streamlined simplified family credit. This tax credit will simplify the Tax Code, provide greater transparency, provide extra work incentives, and provide a stimulus effect. Families should not have to struggle to understand the eligibility requirements for each of the various family tax breaks in current law. All families should follow the same set of rules.

The simplified family credit is structured to provide progressive tax benefits and a work incentive. The families with lower income will get more benefit, but they are also rewarded for work. The credit would be steeply phased in at the lowest income levels providing the incentive to work and a substantial benefit. As income rises a slow phaseout would be necessary to ensure that we maintain a progressive tax system. The cost of this proposal would fall in the range of \$20 billion a year. Given our current deficit problems, I believe that Congress should only create the simplified family tax credit if it is paid for. In my legislation, H.R. 3655, there are several options to pay for this proposal, including rolling back parts of the tax cuts enacted in the last 5 years. Those tax cuts only added to the complexity of the Tax Code and removed any remaining transparency. Again, I want to thank the Chair for the opportunity to testify and thank the Ranking Member, for helping to make it possible.

[The prepared statement of Mr. Kucinich follows:]

**Statement of The Honorable Dennis J. Kucinich, a Representative in  
Congress from the State of Ohio**

Thank you Chairman Camp and Ranking Member McNulty for holding this important hearing. I would like to bring to your attention a proposal I introduced last Congress, H.R. 3655, the Progressive Tax Act of 2003, which will have a positive impact on millions of taxpayers.

I think it is fair to say that all Members of Congress believe we need to strive for a fair, simple, and adequate tax system. We may disagree on how this has been accomplished, but we have the same goals.

However, I think we can agree on the need for transparency. Transparency in the tax system is necessary to achieve fairness. Transparency permits the taxpayer to

understand how fairness is arrived in the tax code. A simplified tax code can provide this transparency, which in turn provides a sense of trust in the government.

This Committee should enact my proposal to create a \$2,000 Simplified Family Credit, a refundable tax credit that simplifies the tax code by consolidating the Earned Income tax Credit (EITC), Child Tax Credit, Additional Child Credit, and dependent exemption for children into one streamlined Simplified Family Credit. This tax credit will simplify the tax code, provide greater transparency, provide extra work incentives, and provide a stimulus effect.

Families should not have to struggle to understand the eligibility requirements for each of the various family tax breaks in current law. All families should follow the same set of rules.

The Simplified Family Credit is structured to provide progressive tax benefits and a work incentive. The families with lower income will get more benefit, but they are also rewarded for work. The credit would be steeply phased in at the lowest income levels providing the incentive to work and a substantial benefit. As income rises a slow phase out would be necessary to ensure we maintain a progressive tax system.

The cost of this proposal would fall in the range of \$20 billion a year. Given our current deficit problems, I believe that Congress should only create the Simplified Family Tax Credit if it is paid for. In my legislation H.R. 3655, there are several options to pay for this proposal including rolling back parts of the tax cuts enacted in the last 5 years. Those tax cuts only added to the complexity of the tax code and removed any remaining transparency.

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Chairman CAMP. Thank you, Mr. Kucinich. The Honorable Timothy Bishop from the State of New York, you have 5 minutes. Thank you.

**STATEMENT OF THE HONORABLE TIMOTHY H. BISHOP, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NEW YORK**

Mr. BISHOP. Thank you, Mr. Chairman, and Ranking Member McNulty. I have two very specific proposals to reform the Tax Code that I would like to share with you this morning, and they are both tailored to what I consider to be the single greatest environmental imperative in the district I represent, and that is the preservation of open space. The first of the two proposals is a piece of legislation I will file today called the Open Space Preservation Promotion Act. This legislation would allow Americans who sell development rights to their land on an installment sale basis to pay the capital gains taxes due in installments rather than all at once in the first year of the sale. The New York State Constitution requires that municipalities pay for land purchases through the use of a sinking fund. This requirement exists in 15 other States as well. This process has led willing sellers to believe that they cannot sell the development rights under an installment agreement, and it is complicated by a technical problem in the Tax Code that treats the sale of development rights the same as if a farmer sold the land to a private buyer.

Consequently, tax attorneys and estate planners advise their clients not to sell development rights if they do not have the cash payments on hand to pay the taxes immediately. My bill simply clarifies the IRS Code that sinking funds should receive installment sale treatment, and thus it removes the cash flow disincentive that currently exists for the seller. This will ensure that farmers who protect their land are not forced to pay taxes before they actually receive payment of the principal. The second bill that I will also file today is a bill that would allow survivors of farmers

to defer estate taxes on the farmland they inherit as long as the land remains in agricultural use or is otherwise undeveloped. The tax would only come due at the time when the farmer chooses to develop the land. As the value of farmland continues to skyrocket on Long Island and elsewhere, so also does the estate tax. Where new zoning legislation and preservation efforts have failed, my bill would help preserve as much as 80,000 acres of farmland in Suffolk County, New York, alone, which as I say is the area I represent. Thank you, Mr. Chairman. I look forward to your questions.

[The prepared statement of Mr. Bishop follows:]

**Statement of The Honorable Timothy H. Bishop, a Representative in  
Congress from the State of New York**

Thank you Mr. Chairman, Ranking Member McNulty, and distinguished Members of this Subcommittee for this opportunity to discuss two tax reform bills I am introducing this week to provide tax fairness for all Americans by rewarding conservation of farmland and open spaces.

My legislation fulfills a dual objective of achieving the kind of reform necessary to make the tax code more user-friendly for families while also addressing one of my home state's most critically important environmental issues—rapidly disappearing open space, a process that could be slowed considerably if we removed disincentives from the tax code which discourage conservation.

Urban sprawl will consume 95 million acres of farmland in the next 20 years, according to the Department of Agriculture; 75 million more acres of cropland, rangeland, pasture and forest are threatened. Farmland and open space preservation is an important goal for New York State and many other states actively working to accomplish this objective.

However, highly appreciated real estate values in my district, which encompasses the eastern half of Long Island, as well as other high-cost areas—combined with the complexities of estate tax policy and estate planning for families who are landowners—are disincentives for conservation of farmland and open space.

In response to these trends, I will reintroduce two tax bills this week that I initially introduced in the previous Congress. The first bill I wish to call to the Subcommittee's attention is titled *The Open Spaces Preservation Promotion Act*. As this title implies, my legislation is intended to protect open space and encourage environmental preservation.

A growing number of municipalities across the nation have demonstrated a strong commitment to preserving the natural beauty of our communities by purchasing the development rights of land from willing sellers. Some communities are investing tens of millions of dollars every year for this purpose. My legislation would help achieve this objective by ensuring that families who sell the development rights to a municipality can pay the capital gains taxes as they receive the payments for those development rights.

The Open Space Preservation Promotion Act of 2005 would encourage land conservation by clarifying a technical problem in the IRS Code. This problem effectively restricts the purchase of conservation easements and development rights in New York and fifteen other states when landowners desire to receive payment for the sale of their development rights in installment payments over multiple years rather than receiving a lump sum payment at once.

As Ranking Member McNulty may be aware, the New York State constitution requires the establishment of a sinking fund for purchases by municipalities—mandating payment of principal and interest over the life of the debt instrument. Under current law, it is believed that farmers and landowners have been reluctant to sell their land or the development rights of their land to municipalities under an installment agreement because sufficient uncertainty surrounds the treatment of sinking funds under the Internal Revenue Code.

As a matter of policy, this installment option is advantageous to both the seller and the buyer, but landowners wishing to structure deals this way have been discouraged because of the cloud of uncertain IRS treatment. Specifically, the concern is that transactions conducted in the form of a sinking fund would force farmers to pay their capital gains taxes immediately, rather than upon future receipt of the actual payment.

My bill would clarify that sinking funds should receive installment sales treatment, in an effort to ensure that farmers who opt to protect their land are not forced to pay premature taxes before they actually receive payment of principal. In other



words, the net effect of this provision is to have the tax obligation of the seller come due commensurate with the periodic receipt of proceeds from the sale.

Working now to remedy this minor technical problem will help to facilitate efforts by municipalities to purchase the development rights of land. Landowners and farmers committed to land conservation will be prepared to reap the financial benefits of their decision to protect their land without fear of owing taxes before they are able to pay the Internal Revenue Service. I hope you agree that this simple fix will go a long way toward encouraging land preservation and protecting our nation's natural landscape for future generations to enjoy.

The second bill I would like to discuss is the *Estate Tax Deferral for Working Farms and Land Conservation Act of 2005*. My legislation would modify the current federal estate tax by allowing a deferment to survivors of farm owners who choose to keep working their inherited land. The tax would only come due at the time a farmer chose to sell or develop the land.

As you know, upon the death of a farmer, the farm is considered part of the estate left to the heirs and subject to estate taxes. The tax can be very large, even though the deduction for the value of the gross estate in calculating inheritance taxes was recently increased to \$1.5 million for tax year 2005.

Under my legislation, federal estate taxes on farmland and open space could be deferred as long as the land remains in open space. Only land that qualifies for conservation easements under IRS Code Section 170(h) would be eligible for such deferral. The tax would only come due at the time when the farmer chooses to develop the land.

As long as families keep land as either a working farm or open space, they would have no tax liability on that portion of the estate. As the family chooses to sell portions or all of the land for development, tax liability would then become due. I am confident this legislation would go a long way to offset the effect of the estate tax where spiraling real estate values have made it too expensive for many families to pay the estate tax and not sell to developers.

When I introduced *The Open Spaces Preservation Promotion and The Estate Tax Deferral for Working Farms and Land Conservation Acts* during the last Congress, both measures received bipartisan support and bipartisan cosponsors in addition to endorsements from my local and state farm bureaus and environmental advocacy organizations. I welcome the support of taxpayer advocates, who should find the tax relief contained in both will go a long way toward helping farmers and their families keep more of the hard-earned money as well as keeping farmland in their family for future generations.

Mr. Chairman, thank you again for this opportunity to discuss both measures. I am confident you will find my legislation provides the kind of simplification and reform that you are seeking in order to make the tax code more user-friendly for American families. I applaud your initiative for calling this hearing, and I look forward to working with you to achieve meaningful and lasting tax reform.

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Chairman CAMP. Thank you very much, Mr. Bishop. Now the Honorable Michael Bishop from the State of Texas. Thank you. Did I say "Bishop"? I meant "Burgess." Thank you, Mr. Bishop. Mr. Burgess, welcome to the Committee.

**STATEMENT OF THE HONORABLE MICHAEL C. BURGESS, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TEXAS**

Mr. BURGESS. Thank you, Chairman Camp and Ranking Member McNulty. I really appreciate you holding this hearing today. I appreciate you keeping the issue of fundamental tax reform before this Congress and before the American people. The President, on a quiet summer's evening, last summer, in New York, or I guess it was in September in New York, mentioned one evening that he wanted tax reform to be a centerpiece of his second term Administration. I was so encouraged to hear that. The President laid out the principles that he would like to see embodied in that fundamental tax reform. He wanted it to be fair, he wanted it to be sim-

ple, and he did not want it to impede growth—economic growth—in this country.

Well, Mr. Chairman, I would submit to you that H.R. 1040, which has been introduced in this Congress and I believe has been referred to this Committee, would do exactly that, and almost immediately. It would eliminate the marriage penalty. It would repeal the death tax. It would abolish the punitive alternative minimum tax. It would eliminate multiple taxation of investment income and allow for immediate expensing of business capital equipment—all issues that we have heard today on this table. This proposal, H.R. 1040, is a flat tax. It is a flat tax that is a little bit different from the flat taxes that were introduced in earlier Congresses in that it is voluntary; that is, it gives the business or the individual the option to opt into a pro-growth system that will tax income one time, and if someone likes the life that they have under the IRS Code, they can stay under the IRS Code. Now, I come from Texas, and this Congress passed a fairly substantial tax reform back in 1986. We had a significant recession in Texas in 1988. A lot of people back home felt that one of the reasons we had that recession was because changes in the Tax Code hit the real estate and the energy sector pretty hard. Those are things that we depend upon back home. So, the question in my mind was always: Why does the government get to make these decisions? Why don't we let people make those decisions for themselves? That is why, when I introduced the flat tax, I thought it was important that it be a voluntary program.

Now, you may ask yourself, what in the world is a doctor doing here at sort of the tail end of this long line of economic experts? I ask myself the same question. The fact is, back in 1995, Mr. Chairman, I got religion. I bought a book that was published by former Majority Leader Dick Armey about the flat tax. I read this book and I said, it is so simple, it is so beautiful, why won't they do that? Then the good news is here on the 10-year anniversary of Mr. Armey's book, Mr. Forbes has a new book out about the flat tax that details many of the principles that I have outlined in my bill and many of the principles that I am bringing to you this morning. The flat tax is voluntary. It is a single rate 19 percent for the first 2 years, falling to 17 percent thereafter. A person or a business would not have the option to move in and out of the flat tax once making the election. They would have to stay within the flat tax. I believe it is reasonable to give people another option that would reduce complexity. A simple Tax Code would allow us to close the tax gap, the \$300 billion that is out there that is just not collected because it is not filed. Some people do not file because, "It is too hard, I can't do that." So, no one comes and picks them up, and over time they just stop filling out a tax form. What Dr. Linder refers to as people—the untaxed, the underground economy, perhaps we would bring more of these people into the system if it were not so difficult for them to fill out their forms and pay their taxes.

I would point out to you the \$300 billion that is taxed but not collected, owed but not collected, is essentially what our deficit is at the end of this fiscal year. This system would be fundamentally fair. We all talk about progressivity in our income tax, but how about an income tax that is fair horizontally as well? Myself and

President Clinton earned the same amount of money when he passed his tax increase back in 1993, and yet I paid a functional tax rate of 33 percent, he paid at 19 percent. Where is the fairness in that? Why the difference simply because one person is more clever about assigning deductions? This tax is simple and that is its beauty. It gives time back to families. Yes, families need more money, but families also need more time. Here is an opportunity for this Congress to step up to the plate and give time back to families.

On the issue of home mortgage deduction, which has always been one of the criticisms of the flat tax, remember that home mortgage deduction means different things in different parts of the country. In my area of Fort Worth, Texas, a home mortgage deduction may equal about \$1,000 in real dollars over a 3-year time. However, in Santa Barbara, California, if you bought your starter castle, a home mortgage deduction may be a pretty big deal. Why not give the person in Santa Barbara, California, a chance to stay in the Code and us in Fort Worth, Texas, a chance to opt into a flat tax? Mr. Chairman, in closing, I believe it is time to trust the American people. Let's give them the choice for a voluntary pro-growth system that is built on the concept of a flat tax, and I will yield back.

[The prepared statement of Mr. Burgess follows:]

**Statement of The Honorable Michael C. Burgess, a Representative in  
Congress from the State of Texas**

First, I want to thank Chairman Camp for holding this important hearing today. As a long-time supporter of fundamental tax reform, I believe that this is one of the most important issues that Congress will face in the next few years. I would also like to thank the Chairman for the opportunity to testify before you to explain my voluntary flat tax proposal. I believe that the flat tax meets the criteria set forth by the President to evaluate tax reform proposals—it is fair, simple, and pro-growth. I will discuss how the flat tax meets each of these important criteria, but first I would like to explain how the Freedom Flat Tax works.

**The Freedom Flat Tax Act**

In March 2005, I reintroduced H.R. 1040, The Freedom Flat Tax Act, which would establish a voluntary flat consumption tax. The flat tax concept is simple—there are two components, the individual wage tax and the business tax.

Individuals pay a flat rate on their wage and pension income, and there will be no deductions. H.R. 1040, however, would allow for the following personal exemptions:

- \$24,600 for a married couple filing jointly;
- \$15,700 for a single head of household;
- \$12,300 for a single person; and,
- \$5,300 for each dependent.

A family of four, for example, would not be subject to the flat tax until their combined income reached \$35,400, which is 194% above the 2002 federal poverty level of \$18,244. Thus, the flat tax system is slightly progressive because the exemptions ensure that lower wage earners do not pay any federal tax until they reach a certain threshold, after which they pay the flat rate of 17%.

It is important to note that the flat tax would:

- Eliminate the marriage penalty
- Repeal the death tax
- Abolish the punitive Alternative Minimum Tax (AMT)
- Eliminate multiple taxation of investment income
- Allow immediate expensing for business capital equipment

Businesses would pay a flat rate on the total costs of taxed inputs subtracted from total sales; only employee wages and pensions will be tax deductible—this ensures that income is only taxed one time. Under H.R. 1040, both the business and indi-

vidual tax rates are 19 percent, but would decline to 17 percent after the initial two years of participating.

Unlike past flat tax proposals, The Freedom Flat Tax Act allows taxpayers to choose if and when to opt into a flat tax system. That is because I do not believe that we should penalize those who have made investments based on the current tax code. It would be like changing the rules in the middle of the game. My flat tax plan allows taxpayers to transition to the flat tax system on their own timetable.

Now that I have outlined the mechanics of my flat tax proposal, I'd like to discuss the proposal in the context of fairness, simplicity, and promoting economic growth.

### **Fairness**

First, it is fair both vertically and horizontally. Horizontally because no matter how much money you make, what kind of business you are in, or whether or not you are married, you will be taxed at the same low rate as every other taxpayer.

The flat tax system has vertical fairness because it taxes everyone at the same rate, while its limited personal exemption ensures that the tax burden does not fall too heavily on lower wage earners.

The tax code should also have horizontal fairness, and that is best illustrated by what I call the "Clinton paradox," which I encountered in 1993. 1993 was the year that Congress increased the tax rate, retroactive to the first of the year. By some quirk of fate, former President Clinton and I earned almost an identical amount that year. But when it came time to pay to the Federal Government, President Clinton paid just over 20 percent, and I paid over 30 percent. Why should such a discrepancy exist? What is the benefit for the country when we are taxed at different rates on exactly the same income? Currently, simplicity and fairness in taxes are sacrificed for the sake of pursuing a social agenda.

But a social agenda is not the purpose of the federal income tax code. That is why the Freedom Flat Tax Act does not allow credits or deductions, which means that people who earn the same wages pay the same amount in taxes, thus the flat tax has horizontal fairness.

### **Simplicity**

A major advantage of the flat tax is its simplicity—it is a tax system so simple that you can understand it without an accountant. By eliminating tax credits and deductions, abolishing multiple layers of taxation, and eliminating the complex depreciation schedules for businesses, the flat tax will simplify the tax code.

All you need under the flat tax is a post-card sized form. The current tax code, by comparison, requires taxpayers to determine which of almost 500 different tax forms they must fill out in order to comply with the tax code.

The flat tax will allow families and businesses to take back the more than 6 billion hours per year that they currently spend to comply with the income tax. Some simple arithmetic is all that is needed to determine your tax liability each year. The flat tax has the ability to give time back to families because it is easy to understand and easy to comply with.

### **Efficiency/Pro-Growth**

The flat tax will encourage economic growth by treating all economic activity equally, taxing income once and only once, and reducing the cost in time and money for taxpayers and entrepreneurs to comply with the tax code.

The current tax code penalizes savings and investment by imposing multiple layers of taxation. This discourages taxpayers from adding to the capital stockpile for our economic engine. Additionally, the tax code favors certain economic activities over others, which ultimately distorts financial decisions and reduces overall economic efficiency. By eliminating the deductions and exemptions that characterize our current tax code, the flat tax will allow people to base their financial decisions on commonsense economics and not the tax code.

A flat tax would be much less costly, saving taxpayers more than \$100 billion per year and reducing tax compliance costs by over 90%, according to one estimate by The Tax Foundation. This would give individuals and businesses more money to spend, which will increase demand for consumer and business goods, which in turn spurs the economy and increases prosperity. For example, one estimate of the Arney Flat Tax, by Michael Boskin, a former chairman of the Council of Economic Advisors, estimated that the flat tax could increase the size of the economy by up to 10 percent.

Not only does the flat tax create a tax code that is less costly for the individual taxpayer, but the simplified tax code would reduce the cost of enforcement. The current system is clearly not efficient—according to the CATO Institute, collecting the income tax costs the Federal Government 10–20% of all tax revenue collected.

The flat tax especially benefits small businesses, which today create the majority of new jobs and account for half of the economy's private output, by allowing for major simplification and the immediate expensing of capital equipment.

I would now like to discuss a couple of criteria that have not been explicitly articulated by President Bush, but I think is important nonetheless.

#### **Transparency**

It is important that the tax system be transparent—otherwise the government can easily raise rates, as they have done in Europe with the VAT tax. With a flat tax, you will easily be able to tell how big a bite the Federal Government takes out of your income each year. After some simple and brief subtraction, you simply pay 17% of your wages above your personal exemptions. And because everyone pays the same rate, it would be obvious to all Americans if it was raised.

#### **Compliance**

The current tax code's complexity discourages compliance with the tax code. Determining the exact amount of tax that is not paid each year is extremely difficult, but the Internal Revenue Service's most recent estimate of the tax gap estimates the tax gap (which is the difference between what taxpayers should pay and what they actually pay) to be between \$257 billion and \$298 billion for Tax Year 2001. Experience in Russia has shown that the adoption of the flat tax and lowering marginal rates has led to dramatically increased compliance with the tax code. Official Russian statistics show that tax revenue rose 28% between 2000 and 2001, following the adoption of the flat tax.

If we could utilize the flat tax to collect even a fraction of the tax gap, we could reduce the deficit or reduce the rates for everyone.

To conclude, the American people deserve a tax system and a government that rewards them for their hard work. It is time for Congress to give that to them and I believe that the flat tax is the best way to achieve this goal.

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Chairman CAMP. Thank you very much. Mr. Burgess, your proposal would require that taxpayers evaluate two different tax systems, if I understand your testimony: one, a flat tax, and then they could opt into the current system. It would require the IRS to administer two different systems. Can you talk to me about how we achieve the goal of a simpler tax system under that proposal?

Mr. BURGESS. Mr. Chairman, I would submit that it just simply cannot be any more complicated than it already is, and to introduce a flat tax to the IRS, to have them administer it, my belief, my opinion, I personally, without even doing the calculation to see—would I save money or have to pay more money—I would give up that shoebox of receipts in a heart beat and go into a flat tax. Again, whether I paid more money or not would be immaterial to me. The simplicity and the gift of time would be worth my considering the flat tax. I don't know if other people feel the same way I do. From my discussions as just a regular guy back in Texas, I got that impression. Again, Mr. Armey's book was very popular back in my district, and not just because he was my Representative at the time. It was an idea that resonated back home. Unlike Dr. Linder's proposal, the IRS would continue to be there in my proposal, but my belief is that as people worked their way down from those high home mortgage deductions that perhaps they have been encouraged to take on because of our complex Tax Code, that as people work their way through those processes, they will abandon the IRS Code and come to the flat tax. My belief is, at some point in the future, we would be able to entirely eliminate the Code because it would no longer be necessary.

Chairman CAMP. Thank you. Thank you very much. Mr. English, your proposal would focus on the way corporate taxes are

paid, and particularly would exclude export revenues from taxation and would tax imports at 11 percent, if I understand it correctly. Tell me how you think that would affect economic growth in this country, if you could.

Mr. ENGLISH. We have listened to a number of experts speculate on how this could have an impact. What it does, in effect, by setting up a border-adjustable system, you are—which, by the way, is common not only to my proposal, but to a number of others. What it would do is it would level the playing field. A product that would be leaving this country and competing in a third market would be able to compete on an even footing without the tax cost built into the price with foreign products. It could enter another country and compete with product produced in that particular country by here, again, only paying taxes imposed within that jurisdiction, rather than the additional burden of taxes from our system. By contrast, an import coming in, which currently comes in typically border-adjusted, would currently have no foreign tax imposed; and apart from State taxes on things like sales, it would be comparatively tax free. Yet, the cost of our tax system would be built into the price of competing domestic products. No matter which market you are in, the effect of border adjustability is substantial. Now, the issue has been raised by economists, in fact, would not there be an opportunity through changes over time in currency pricing—would that not, in effect, take away the advantage of border adjustability? That, to me, is a macroeconomic analysis from a microeconomic problem. Clearly, a border-adjustable system would add economic growth by making our manufacturers more competitive in all markets, and by leveling the playing field so that the price of our tax system does not become an unfair disadvantage for individual products. This is particularly significant in manufacturing. We think over time it would also be a significant issue in the service industry. As a result, Mr. Chairman, I think you can make a compelling argument that our approach is the one necessary if we are going to have our products competitive over time in global markets and allow us to start to reduce the institutional built-in advantage for imports.

Chairman CAMP. All right. Thank you very much. Mr. Linder, your proposal obviously is a retail sales proposal, and property that is purchased for business purposes or services would not be subject to tax. If the taxability of an item depends on the nature of the transaction, would that be a simpler tax to administer? Because there still will have to be this evaluation: Was the item purchased for business purposes or was it purchased for consumption? If you could just talk about that a little bit, I would like to hear your thoughts on that.

Mr. LINDER. If a business went to Home Depot and bought some goods from Home Depot, they would pay the tax at Home Depot, which sells to both consumers and businesses, and they would keep their receipts, and they would use the value of those receipts as a credit against paying the tax in the future. So, they would not be taxed. We would not ask Home Depot to make the decision whether or not to raise the tax from them. Any business-to-business transfers will not be taxed at all. Now, let me be very clear. Some people are going to cheat. We are Americans. We cheat.

We cheat on our income taxes. People take their spouses to dinner on the corporate ticket and write it off. It is going to be much more difficult to cheat under this system because you are going to have to have two people conspire to cheat. Currently, just one person lies on a tax return, sends it in, and he has less than 1-percent chance of being found. Under our system, you have to have two people conspire to cheat. My guess is that since about 90 percent of this tax is going to be collected by about 10 percent of our companies—right now in California, for example, 92 percent of the tax is collected from 8 percent of the companies, the big boxes, the Home Depots, the Loews, the Penneys, the Targets. They are not going to help cheat. The guy who is going to cheat is the guy who comes to paint your house, and he is going to collect the tax from you. He is just not going to remit it. That is going to be a very, very small part of the economy, and we think that the collection will be significantly higher—we think it would be more like approaching sales taxes at State levels, which collect somewhere in the 90- to 92-percent range right now.

Chairman CAMP. Thank you very much. Mr. McNulty may inquire.

Mr. MCNULTY. Thank you, Mr. Chairman. I am sorry Mr. Neal had to get to another meeting because I did want to discuss a little bit more the AMT issue and to clarify the difference between the personal AMT and the corporate AMT, which was a result of the 1986 Tax Act, after many stories in this country about corporations making billions of dollars of net profit and then not paying anything in Federal taxes because of various tax loopholes, and that was the genesis of the corporate AMT, which, I am assuming, Mr. Neal is not talking about, but I want to talk about it for a second, because it has been the policy of this Administration not only to repeal the corporate AMT, but to repeal it retroactively, and to give rebate checks to all of these corporations or every single penny that they paid in under that tax since 1986. Some examples would be IBM would get a rebate check of \$1.4 billion; Ford Motor Company, \$1 billion; ChevronTexaco, \$800 million; General Motors, \$800 million; General Electric, which has a presence in my district, and which I have helped many times through the years, would get a rebate check from us, the rest of the taxpayers of \$600 million. Now, at a time when we have record deficits and a record national debt and are struggling, the last thing we need to be doing is giving rebate checks to these corporations that are doing very, very well. So, I think it is important to underscore the difference between what Mr. Neal is trying to do with the personal AMT and the corporate AMT.

I would just like to ask Mr. Burgess a little bit about this flat tax issue because, as you know, this issue has been around for many, many years and other people, including Mr. Armey and others, have proposed it. It has always been fascinating to me because you brought up the issue of simplicity, and you made the personal comment that you wouldn't mind paying a little bit more in order to get the simplicity. Now, I don't know how many—you know, I would like to test that theory out a little bit and see how many people feel the same way you do about giving up the shoebox of receipts but we have to pay more. You know, I am looking at sim-

plicity, too, with regard to a flat tax. Basically, if you want to talk about simplicity, there are three groups of people in this country: there are poor people, there are rich people, and there is the middle class. I know, in your proposal, you are not proposing taxing poor people. I have talked to many people about the flat tax through the years, and I have found very few wealthy people who are opposed to it. Most are very enthusiastic about it, which indicates to me that they would pay less under a flat tax. If your proposal is revenue neutral and poor people are not going to pay and rich people are going to pay less, who makes up the difference? The middle class. The basis of your proposal, at least in your conclusion, was that people for the sake of simplicity would be willing to pay more—in other words, more taxes on the middle class. How do you respond to that?

Mr. BURGESS. Well, as far as the simplicity argument goes, we passed as part of your Committee's bill, the FSC/ETI bill last year (P.L. 108-357), we allowed citizens in my State of Texas to take a deduction for their State sales tax on their Federal income taxes. That deductibility had gone away back in the 1980s. It is not a formal survey, but I have asked people at my town halls. I used to keep all of my receipts for sales tax because I thought I could do a better job than the IRS at calculating a table. I don't do that anymore, because quite honestly, my time is too valuable and I am just not able to do that, but I have not encountered anyone who is keeping all of their receipts from all of their purchases, to tally them up at the end of the year and see if they will be able to increase their rate of reduction over what is available in the IRS table.

Mr. MCNULTY. What about the general concept of the simple math here? If your proposal is revenue neutral, you are not proposing taxing the poor segment of the society, lower income? The wealthier people in this country are wildly enthusiastic about your proposal, which is a clear indication to me that they are going to pay less, and if your proposal is revenue neutral, if the poor are not going to pay and the rich are paying less, and the proposal is revenue neutral, in other words, you are bringing in the same amount of money, the middle class has to pay more.

Mr. BURGESS. You know, are you absolutely sure that the rich are going to pay less? The example was given of someone who earned a fantastic income and paid a 12 percent rate.

Mr. MCNULTY. I don't have any scientific information on that because we haven't done it, but I mean, it is a clear indication to me that if wealthier people in this country are so strongly supportive of the flat tax concept, it is not because they are going to pay more. They are not going around saying, "Implement this new proposal so that we can pay more in taxes." I think they are saying, "Implement this new proposal so that we can pay less in taxes." If indeed, they would pay less in taxes, middle income people have to pay more. In all fairness, I really haven't heard from anyone who I would consider extremely wealthy in this country who is enthusiastic about this proposal. It has been a little bit difficult to push the concept uphill, but obviously I would welcome support from any venue.

Chairman CAMP. Thank you. Ms. Hart may inquire.



Ms. HART. Thank you, Mr. Chairman. I am going to ask all of the panelists to answer this question, and I would like you to distill your—I guess, support—or your enthusiasm—into one issue that I am mostly concerned about, because in the communities I represent, people tell me that our Tax Code is simply a deterrent to entrepreneurship and a deterrent to economic growth. So, what I would like each of you to do for me is, in a couple of sentences tell me why your proposal is going to encourage entrepreneurship and promote economic growth. What about your proposal, that is different from our current system, is going to change that? Go ahead, Congressman English.

Mr. ENGLISH. In a nutshell, what my proposal would do is level the playing field in international competitiveness, at the same time dramatically lower the cost of capital and also increase the national savings rate, which, in turn, it will provide more seed resources for entrepreneurship. My proposal is radically pro-growth, radically pro-entrepreneur, and will make it easier to launch many, many small businesses in the future.

Ms. HART. Congressman Linder?

Mr. LINDER. It is clear to everyone that the current tax system punishes savings, thrift, punishes productivity, and rewards consumption. Under our system, the average income earner is going to get a 50-percent increase in take-home pay. He is going to be an investor. The \$10 trillion in offshore financial center and dollar-denominated deposits will be largely on our shores, creating jobs, increasing the value of the markets. We have studies that say within the first year after passage of this, the economic growth rate in the United States will be 10.5 percent. Increase in exports would be 26 percent, and the increase in capital investment would be 78 percent. We know that from '45 to '95 real take-home wages increased in exact correspondence to the increase in capital investment. This is the most solid pro-growth proposal ever proposed, and that is what was said at the Tax Commission by all of the economists who said this is the most effective way to go with the economy, is to tax consumption.

Ms. HART. Mr. Emanuel?

Mr. EMANUEL. Three quick parts. One, number one reason people drop out of college or don't go to college is they can't afford it, number one. So, we would give everybody a \$3,000 credit so they can go to college or graduate school. Second. Homeownership represents about one-eighth of the economy's economic activity. We would provide the mortgage deduction to everybody who owns a home, so 10 million people who today own a home, but don't get the mortgage deduction, would be provided that, and other people who are on the moderate to low-income end, would be brought into the homeownership arena and begin to build their nest egg of equity. Third, as all of us have said, it is that we have a low savings rate here, and given that we create a universal pension, you would actually not only increase the amount of people who save, but the dollars that are saved, which is important for, obviously, capital formation, and allow, actually, the thing that you are looking for: economic activity and entrepreneurship.

Ms. HART. Mr. Kucinich?

Mr. KUCINICH. Thank you very much for the question. Under my proposal, the working poor, in particular, would have more money to spend on their children, which, of course, would amount to a lot of economic activity, particularly for small businesses which are the first point of contact for many of the working poor.

Ms. HART. Mr. Bishop?

Mr. BISHOP. The economic stability of the district I represent is linked inextricably to the quality of our environment. The principle industries of our district are travel, tourism, the second-home industry, farming and fishing, and the preservation of open space is absolutely vital to the quality of the environment, and thus to the stability of the economy.

Ms. HART. Thank you. Dr. Burgess?

Mr. BURGESS. Well, certainly the improvement of savings and investment, there is no question about that. Just focus on the marriage penalty for a moment. Under a flat tax, currently the system is a spouse whose husband or wife earns in excess of \$50,000, \$60,000 a year initially pays tax at the highest possible rate of every dollar that they earn. Under a flat tax proposal, everyone goes back to the same flat rate, so there is no penalty for being married. In my business—my medical practice—when I first started out, I thought a smart thing to do would be to keep 3 months of operating capital in an account in the bank, so I would always have that in case the wolves were at the door. Imagine my surprise to find out, at the end of the first year, I got taxed at 38 percent on that money, that 3 months capital that I had in the bank to prevent the wolves coming to the door. Suddenly, over a third of it was gone. The flat tax would eliminate that from happening.

Ms. HART. Thank you for that. That was pretty quick for Congressmen. I want to go back to Mr. English and his proposal. You exclude export revenue in the conversations we have just been having on trade.

Mr. ENGLISH. Yes.

Ms. HART. I am very interested in that. Can you tell me the genesis of doing that, and why that is such a positive part—

Chairman CAMP. Mr. English, if you could respond quickly because time has expired.

Mr. ENGLISH. Certainly. Since 1948, it has been allowable, under GATT rules, for a border adjustable tax system. Most of our trading competitors have adopted border adjustable tax systems, which allow them to take the tax off of their products at the border, and impose an equal and fair tax on imports coming in. That way, both imports and exports pay the same tax and pay the same share of the freight.

Ms. HART. Thank you. Thank you, Mr. Chairman, for your consideration on that one.

Chairman CAMP. Thank you very much. Mr. Thompson may inquire.

Mr. THOMPSON. Thank you, Mr. Chairman. I have a couple. Mr. Linder, could you help me understand the difference between the inclusive and the exclusive tax provisions in your bill?

Mr. LINDER. We are placing an income tax, which is inclusive of what you earn, so we thought we would have to do an exclusive tax of what you spend. It is 23 percent out of every dollar you

spend will go to the government, and currently 33 cents of every dollar you earn goes to the government. If you were treating it exclusively, it would be a 30 percent tax, a 29.9 percent tax on what you spend. Then to compare that to the income tax, what you have left to spend after government gets is, you have a 50 percent tax as an exclusive tax. So, it is the same 23 cents whether you spend 77 cents times 30 percent gets \$1.23 goes to the government, or whether you spend a dollar and the first 23 cents out of it inclusively.

Mr. THOMPSON. So, it would be 23 percent, not the higher 20 percent?

Mr. LINDER. Inclusive, 23 percent of what you spend—

Mr. THOMPSON. If you bought \$100 worth of goods, what would you pay in tax?

Mr. LINDER. \$23 it would be included in the price.

Mr. THOMPSON. Thank you. Mr. English, your bill does away with the State tax exemption?

Mr. ENGLISH. Yes.

Mr. THOMPSON. Would it do away with all similar State tax exemptions? I think Mr. Burgess mentioned Texas and their sales tax exemption. That would do away with that as well?

Mr. ENGLISH. Yes.

Mr. THOMPSON. Thank you. Mr. Burgess, how do you handle inheritance tax in your bill?

Mr. BURGESS. There would—if a person would like to go under the flat tax, there would not be an estate tax.

Mr. THOMPSON. So, you wouldn't actually pay, what is it, 17 percent on all of the money that you take in, only on wages, the earned income?

Mr. ENGLISH. The concept is that money is taxed just one time, so tax at the point of earning and not at the point of death.

Mr. THOMPSON. So, it is not on all income or not all earnings, just what? What gets taxed under your bill?

Mr. ENGLISH. Wages, income from—dividends would either be—and that would be a decision for this Committee to make—would be taxed only one time. They could be taxed at the level of the business where they were generated or at the time they were distributed to the individual. Investment income would be taxed one time. Wages would be taxed one time. Capital gains would be taxed one time.

Mr. THOMPSON. I have never really understood the tax one time on inheritance, because if you inherit it, you haven't been taxed on it, somebody else was.

Mr. ENGLISH. The taxes have been paid on the money, that is correct.

Mr. THOMPSON. Your wage money is also—somebody has paid taxes on that somewhere down the line as well. Does your bill—

Mr. ENGLISH. Most of the income that I leave when I leave this earth will be income that has been paid to me as wages and has been taxed.

Mr. THOMPSON. When you leave, you are giving it to someone else, so they haven't paid anything on their new moneys.

Mr. ENGLISH. They put up with me.

[Laughter.]

Mr. THOMPSON. Yeah, that may be worth something, I don't know. Your bill also does away with your sales tax exemption that people enjoy now in Texas?

Mr. ENGLISH. If somebody elected to go into the flat tax—and I cannot believe a single person in the State of Texas would say, you know——

Mr. THOMPSON. No, I don't want to debate that. I have no way of knowing what people in Texas would choose to do——

Mr. ENGLISH. If you elect to go on the flat tax, it is gone. That is correct.

Mr. THOMPSON. Thank you very much. I yield back, Mr. Chairman.

Chairman CAMP. Thank you. Mr. Foley may inquire.

Mr. FOLEY. Thank you very much. The first question for Mr. Linder. I am obviously intrigued by your proposal. I think it does a lot of things that are unique, and the one thing I most appreciate is the fact that it really does reward savers. If you are a consumer—if you are spending—you will pay taxes. If you are a saver, you have the opportunity to aggregate wealth, and not avoid necessarily taxation because you are going to have to lay out moneys the live and to operate, but it really does create an incentive, if you will, for frugality. Is that a fair impression?

Mr. LINDER. That is a precise impression, and frankly, if you are wealthy and you want to—if Bill and Melinda Gates want to move to a farm and grow their groceries and live off the rebate, good for them. We will borrow their money and create jobs with it. This is the single-most compelling reason to do that. The second one is, whatever we do, we have got to make an effort to get the tax component out of the price system. It is the one thing that makes us less than competitive in the world economy.

Mr. FOLEY. The concept or notion that your proposal will eliminate the IRS is not accurate, is it? We will still have to have an oversight or collection——

Mr. LINDER. My proposal anticipates that the States will do the collecting and administering, and we would pay them 25 basis points for doing so. The retail, or whatever outlet that collects the money from the individual and remits it to the State, will get 25 basis points. There will be a department in the Treasury of a few thousand people that will be responsible for collecting Internet and catalog sales. I don't believe the guy down the street who builds a building and hires our kids and sells books should be put at a 7 percent disadvantage to Amazon.com. The States in 2003 lost, in collections to Internet and catalog sales, \$23 billion. It is a growing concern for States, so the Federal agency in the Treasury will be responsible for collecting Internet and catalog sales and remitting them to the States and localities.

Mr. FOLEY. So, this is an equalization?

Mr. LINDER. That is correct.

Mr. FOLEY. We no longer have the disparity, if you will, between the big box retailers and the shippers of, as you mentioned, Amazon.

Mr. LINDER. It also eliminates the government choosing winners and losers in respect of goods v. services. I was speaking downtown to a group of physicians who really liked the idea, until

one lady jumped and said, "You expect us to tax our patients?" I said, "What makes you think you are so special? All your neighbors are taxing their source of income right now. We should tax all goods and all services equally."

Mr. FOLEY. The point of collection, obviously, you mentioned a mechanism. Florida has a Department of Revenue, so that is already in place. They would be your collection manager?

Mr. LINDER. That is correct. We would contract with them and oversee their collections and the biggest difficulty for them will move to collecting on services. They don't have the template in place like they do goods. Forty-five States currently collect a sales tax, and they will be contracted with to do the collecting administering, and we have already had States who it—say if those other 5 States don't want to do it, we will do it for them.

Mr. FOLEY. I was hoping Mr. Emanuel would have been available for one question. Maybe his Democratic colleagues can help me with this, because I did want to try and hone in on the terminology used by your side when we have the tax cuts for the rich. There is a conversation that constantly occurs, and it is a wonderful sound bite: This is for the middle class. We want to give tax relief for the middle class. I am trying to determine what that means, if we have a parameter of income that we would consider middle class. If either could venture a guess, because it does sound nice. I talk about it. I say for the middle class, but that is an ambiguous statement, and I do not know where we draw the lines of who is in the middle class today. Somebody living in Chicago—which is why I wanted to pose the question—may have an \$800,000 apartment based on the market prices, but they are two hard-working public servants making \$80,000, \$100,000—depending on locality, pay is different. Is \$200,000 income middle class? Is \$400,000? Is \$60,000? Just for the terms of the rules of engagement, I wish somebody could answer that question, because as long as it is nebulous, we can all get away with saying, "I want it for the middle class." If we don't define what those rules are, then we are talking about atmospherics. Can either Member help me define what the party's position is, relative to middle class, the pay structure or the asset base, so at least I know who we are talking about?

Mr. KUCINICH. Well, it is an important question. I can talk from my own experience with my own constituency. I live in, what I consider to be, a middle class neighborhood. Those who are middle class tend to have jobs. Those jobs tend to be where they make in a range of \$30,000, \$35,000 a year to about \$70,000 or \$75,000 a year, in my neighborhood. They have homes that might be anywhere from \$65,000 to maybe \$200,000. So, that is what I understand from my own experience, where I live. Also, the idea about tax cuts for the rich—those concepts mainly come from the distribution tables, which, in the last tax cut, seemed to—on the basis of some reports—like from the New York Times, where the greatest percentage of the benefits went to people who made over a million dollars. So, they would be in another class from the people who would be in my neighborhood, let us say. I guess you have to go on your own experience. For example, in some neighborhoods, like in California or perhaps in Florida, people could be considered mid-

dle class and they would be living in homes that might be worth upward of a million dollars. I mean, that is possible, actually.

Mr. FOLEY. Well, that is my only concern—

Mr. KUCINICH. You know, there are a number of factors involved, but I would probably say that one of the first factors has to involve your actual income in relationship to what everyone else is in your area, the value of property in relationship to what everyone else's is in your area. It is kind of a relative position for people in a region, but nationally, it is not relative because it really depends on the kind of disposable income you have, not just property assets.

Chairman CAMP. If we could conclude because your time has expired. Ms. Tubbs Jones may inquire.

Mrs. TUBBS JONES. Oh, Mr. Foley, call some of your sociologists to do the research for you and figure out what middle class is. You know what middle class is for purposes—the debate that you want to have on it. Even when your party defines what low-income is, you use \$12,000 for a family of four. That is pure poverty when we start developing. So, you can get a sociologist to do some research for you and define middle class. It will be all right. Because I want to be clear that as we debate this issue out here on the floor, that not only is the Democratic side reflected, but the Republican and all of use license—political license—to use or define middle class the way we want to for purposes of whatever debate we are in or whatever discussion we are in. If you would like me to give you some time to respond, I would love it. If not, I am going to move on to ask Mr. Kucinich a few questions about his tax in piece.

Mr. FOLEY. Would you give me your definition at least of the middle class parameters?

Mrs. TUBBS JONES. Halfway between—between the poorest people of our country and the richest people of our country. That is middle class, okay? You know what the usual definition of “middle” is, in the middle, between the top and the bottom. We talk about lower middle-class, middle middle-class, and upper middle-class, same thing. Okay? I am not a researcher at all. That is my definition. Mr. Kucinich, how are you, sir?

Mr. KUCINICH. Good morning.

Mrs. TUBBS JONES. How you doing? Do you think that there are other things that we could use for purposes of defining—when we talk about simplified family credit—are there other taxing issues out there that we might include in the family credit?

Mr. KUCINICH. Well, I think that you have to go back to how this idea came up. There is a group called the Economic Policy Institute and a gentleman by the name of Max Sawicky. His idea is to look at what we can do to make the Tax Code more progressive, and also what we can do to make the Tax Code have more transparency, which actually is a way of showing people that it is progressive. The idea—Congress has come forward and created a number of vehicles to try to provide benefits for families. You know, we had the earned income tax credit, we have the Child Tax Credit, the Additional Tax Credit, and dependent exemption for children. All of those were attempts to provide some benefits. What this does is it puts—it basically consolidates—all of these various programs

that Congress has already worked on, and in doing that, it simplifies the Tax Code because I think that is something we are always striving to do—provides greater transparency, provides work incentives, which is one of the things we need to do for the constituency that you and I represent, to make sure that people do achieve incentives for work, and have a stimulus effect on the economy, which answers the question that Ms. Hart had.

Mrs. TUBBS JONES. Okay. Thank you, Mr. Kucinich. Mr. Linder, when you talk about your national resales tax being voluntary, that means that—are you suggesting in your proposal that someone either chooses to stay under the current code or they can choose to go under a national resale tax code? Is that what—I mean—

Mr. LINDER. No. The tax itself would be imposed on everyone, but if some chose to buy a used house and a used car and used clothing and live off the rebate, they would pay no tax whatsoever. Currently people—

Mrs. TUBBS JONES. How would you regulate that? Who would be responsible for it administering the rebate?

Mr. LINDER. The person who does the buying. We don't tax anything used. We tax everything new once.

Mrs. TUBBS JONES. No. I am saying, who would be responsible for determining whether or not the person doing the buying would get a rebate?

Mr. LINDER. Every household, rich or poor, would get a rebate at the beginning of every month sufficient to totally untax them up to poverty level spending. Poverty level spending for a household of one is \$9,600 a year. Poverty level spending for a household of four is \$25,660 a year. Their check—

Mrs. TUBBS JONES. Would come from?

Mr. LINDER. Come from the Social Security Department. It might be a debit card. It might be an overnight click into an account.

Mrs. TUBBS JONES. Then Social Security, or the IRS, or whatever we call this agency, would be responsible for the administration of this rebate?

Mr. LINDER. You would sign up with your State administration department with the names and Social Security numbers of who all lives in that household, and your rebate would be sent to you based on the number of people in the household. People today have been spending all—

Mrs. TUBBS JONES. Have you any idea what the administrative cost would be for the proposal you have got?

Mr. LINDER. A whole lot less than sending out 45 million Social Security checks.

Mrs. TUBBS JONES. I don't know. I am just asking. I am curious. Have you—you say it is a whole lot less. How much less?

Mr. LINDER. We believe—and we have had conversation with Visa and Mastercard, that they would administer it, and they would provide debit accounts for your debit card once a month, and it would be very low.

Mrs. TUBBS JONES. So, you are proposing that rather than the government administer the program, we give that responsibility to a private industry to be able to do that for us?

Mr. LINDER. No. I am proposing that this Committee, if it ever looks at this seriously and chooses to do it, will make that decision on how it gets done in the final drafting, but we have looked at all kinds of different ways. You can make a hundred million computer clicks in one evening through the Federal Reserve or through a Social Security Department for about a penny a click and transfer that money.

Mrs. TUBBS JONES. Thanks for your responses, sir. Thank you, Mr. Chairman.

Chairman CAMP. Thank you. All Members have had an opportunity to inquire. Are there any Members who wish to inquire further?

Mr. MCNULTY. Mr. Chairman, I just want to take this opportunity to thank all of the panelists for their very thoughtful proposals and for being here today. Thank you.

Chairman CAMP. I do as well. I want to thank all the Members, on a very busy week and morning, for taking the time to come and testify before the Subcommittee this morning. Without objection, this hearing is adjourned.

[Whereupon, at 11:17 a.m., the hearing was adjourned.]

[Submissions for the record follow:]

Plano, Texas 75074  
August 30, 2005

Dear Honorable Chairman Camp and Ranking Member McNulty:

Below please find my submission this spring to President Bush's Tax Reform Advisory Panel.

I now wish to share my story directly with you in hopes of garnering your support and leadership of the Honorable Sam Johnson's H.R. 3385.

I am employed by Network Appliance in the Plano area of Texas. In 2000 I purchased some of my stock options. During that time the stocks buy value was \$50/shr and the peak value was \$150/shr then within a few months the value dropped to a low of \$6/shr. Consequently, we were taxed at \$50 per share rate even though by the end of the year—the stock was only valued at \$6 per share. We were told we owed AMT in the amount of \$350,000. This was a prepayment of tax for which we hadn't received benefit from. Lets remember, we purchased the asset we didn't sell it and receive capital gains! My wife and I had started building our retirement home and we had to finish the house using our savings rather than gains from the stock. I then had to mortgage the house.

The IRS ruled that we would have to sell our house in order to pay the AMT liability of \$350K. I put the house up for sale and three months later, the IRS attached my wages because the house had not yet sold. When this did not help the house sell, the IRS attached my base salary and my bank accounts—forcing me into bankruptcy. I have always paid my taxes on time and I have never been audited. I am 57 years old and all my savings were in the house. The house never sold and eventually was foreclosed on—eliminating any future liability for the payments, but leaving us with no equity to pay the IRS. We finally got the IRS to negotiate a settlement (after 18 months in bankruptcy) on the amount to be paid over a six-year period. I have hundreds of thousands of carry-forward losses but they cannot be used for previous years. We settled on paying the IRS \$240 over six years which will take most of my income. **Then, I will start to try to build up retirement when I'm sixty-two years old!!** Since I was forced into bankruptcy, I don't have a credit card to travel and do my job—I can't rent a car. I use a bankcard for hotels and meals and get rides from other employees in the cities I visit. I would have paid anything I could afford from day one—the IRS didn't have to force me into bankruptcy. This Policy & the IRS has ruined my credit, cost me thousands in legal and accounting fees (all of which could have gone to paying them). I'm at a loss as to why someone who has never done anything but pay his taxes on time can be treated in such a vindictive manner!

The ISO AMT law is beyond unfair! **IT'S CRIMINAL** and should be changed immediately!! It has ruined my families retirement and has forced me into bankruptcy



unnecessarily. Your support is respectfully and urgently requested so that other families and other honest taxpayers don't get caught in this horrible AMT trap.

Nelson R. Allen

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**Statement of Susan Schroeder Anderson, Mountain View, California**

Thank you for taking the time to read this letter. I believe the Alternative Minimum Tax (AMT) and its treatment of pre-taxation on Incentive Stock Options is wrong. I have submitted my story on numerous times to my Senator, Congressperson as well as the Ways & Means Committee and the President's Advisory on Federal Tax Reform. I feel that the AMT, which was originally created because 155 wealthy businessmen didn't pay any taxes, was not intended to financially ruin the middle class worker. It is an unfair tax and should be abolished immediately. This tax has caused our family undue stress and anguish. As a taxpayer and citizen, I urge you to please support H.R. 3385.

Here is my story: In 1995 I joined a start-up high tech company called VeriSign. I was hired as an Executive Assistant to the President and my salary was \$45,000. Over the years, I was granted Incentive Stock Options (ISO). I tried to regularly exercise and hold my ISOs for one year in order to pay long-term capital gains on the stock. In July 2000, I decided to leave my job so that I could plan my wedding and also start to plan a family. I had stock that needed to be purchased when I quit my job in July of 2000, so I exercised the stock. As everyone knows, the stock market then suffered the **worst stock market downturn in history!** At the time, I did not sell my stock in hopes that the market may recover. Had I known about the AMT, I would have sold the stock immediately. I come from a middle class background; my father worked for AAFES (Army & AirForce Exchange Service) and my mother was a nurse. I could not go to my parents for advice regarding my stock options because they had no experience with stock. I tried to get a financial advisor but had a difficult time finding one since, at the time, here in the Silicon Valley, financial advisors would only take people with large portfolios. My only financial advisor was the broker that I used through VeriSign, who was biased since they worked for VeriSign—they suggested I hold my stock. Many people had similar situations to mine. My tax preparer told me that I would be subject to the Alternative Minimum Tax and that I could receive a tax credit and I could use that to offset a sale later on. Unfortunately, my tax preparer wasn't aware that I would only be able to recover \$3,000 per year in my AMT tax credit. At the time, most tax preparers hadn't had much experience with AMT and therefore, could not give any detailed advice on how to handle the stock. At that time, my salary for 2000 was \$50,747 and my taxes paid to AMT were \$408,627—**over 8 times my annual salary** on money that I did not have nor received!! I had to take all the stock and sell it and take a loan in order to pay my taxes. On top of that, I had to pay lawyers and accounts in excess of \$20,000 to help me to understand AMT and to try to fix this problem. The amount of stress was and is still unbelievable.

I never received any benefit from my ISOs—in fact, I now have a tax credit that I will never be able to use in my lifetime. Since AMT is also a self-reported tax, I have many sleepless nights thinking about how I shouldn't have reported the stock to the IRS, how it doesn't pay to be honest, etc. I personally know many people did not report this tax because they felt that the chances of being audited were very slim. At the time, I did consider this but having spent my entire life working and paying taxes, I knew in my heart that I was not the kind of person to lie to the government.

AMT was never intended to trap the little guy. It was originally intended to make sure the very rich, who years ago had tons of loopholes to hide their money, would pay taxes. This law is flawed on so many levels:

1. It's self-reported, the IRS has no way to track who reports and who doesn't;
2. You are pre-taxed on gains that have never been realized;
3. After paying AMT, you are given a tax credit that never gains any interest (on the flip side, if we owe the IRS money, we have to pay interest plus penalties);
4. The AMT tax credits will never be fully used—mine is \$408,627 and it would take me 136 years to use this credit.

The mental anguish over this tax is unbelievable. I know that many people think that those of us who were caught in the AMT ISO trap were greedy but that isn't the case. I personally feel that my lack of understanding ISOs and the stock market along with the confusing way that AMT is calculated helped to get me in this AMT

mess. I just didn't have the knowledge to fully understand the ramifications of this law. Those of us who found out the hard way had to make a decision, either report it or not—many did not. I chose to report the tax even though I felt it unjust and unfair. However, my honesty only got me a huge AMT bill while others walked away and didn't report their AMT. Those who didn't report, wait for the statute of limitations to go by and then breathe a huge sigh of relief when they find they haven't been audited. The IRS has no way of tracking stock sales and exercises and they rely solely on the taxpayer to supply this information—this seems awfully stupid to me as it can lead to underreporting, etc. of this and other taxes.

I am working with a law firm to try to recover some of the AMT that I've paid. My amended returns have been with the IRS for over two years. The IRS holds amended returns "hostage" so they can sit out the statute of limitations instead of making decisions regarding our arguments for getting credits back faster. I believe they do this because they are afraid to do the "right" thing and call this law unfair. The IRS refuses to respond to my amended returns. The only recourse that I have is to take the IRS to court—which means spending another \$15,000–25,000 of money that I don't have—and then knowing that the courts don't want to make the "fair" decision but want to make the "constitutional" decision (following the law). If I did go to court—I could be tied up in court for another 5 years. The only way to get justice is for the law to actually change.

I hope that my letter puts a "face" on what this horrible law has done to the average person. I am not an executive, I am not a founder of a company, I ended my career at VeriSign as a Project Manager—nothing fancy. If you saw my tax returns for the last 10 years—you would see that I never made over \$75,000 a year in actual salary. I always paid my taxes on time. I'm a responsible citizen who has voted in every election since I turned 18. I believe that my government will do the right thing. However, in the future, I would never accept stock in lieu of salary like I did at VeriSign. I don't ever want to be in a position of having to make decisions that will ruin my financial life and the life of my family.

I hope and pray that the Ways & Means Committee will have the courage to listen to all the comments from people like myself and make some real changes in this law. We did what we thought was right, we reported our stock exercises and then ended up paying millions of dollars in pre-tax to the government on stock that we never saw any financial gain. It's wrong. Plain and simple. If it happened to you or to one of your family members—you would be outraged. Time is running out for those of us who couldn't pay their AMT—if the Ways & Means Committee does nothing—many will lose everything they ever worked for—their savings, 401Ks, their children's education funds, their homes. Please do something about this before these honest citizens end up homeless.

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#### **Statement of Ross Ashley, Dallas, Texas**

I ask for your support of H.R. 3385. This bill is a good first step towards alleviating the pain and suffering that my family is experiencing right now and, with no end in sight, for many more years.

I worked as a software engineer for a once high-flying software company, i2 Technologies. I was not an executive or even a mid level manager. I was simply a hard-working individual contributor. I made several significant contributions to our products and later helped our customers solve special problems. I was granted incentive stock options every year from 96 through 2003 and our stock price rose along with others during the tech bubble. In 2000 I exercised options with a market value at that time of about \$450k. The exercise of those options resulted in a tax liability that I didn't fully understand at the time. The AMT tax that I incurred was about \$150k. By the end of the year, the value of the stock that I owned by virtue of the options I exercised was about \$75k, or about half the value of the AMT tax I owed. i2 Technologies was trading in the spring of this year at approximately \$0.50.

Congress passed laws encouraging individuals to buy and hold stock rather than trading it on a short term basis when they reduced the capital gains tax rate. When I exercised the stock options I intended to hold those shares and that's exactly what I did. When more of my options vested I planned to exercise them and hold them also. I had no inside knowledge of the impending collapse of the tech industry. As far as I knew, our products were world class and our solutions were saving our customers real money.

In early 2001, I thought that we were experiencing a market correction and that i2 was a great company. Soon the market would see that i2 saved its customers money and it would reward the company with a higher stock price. So I didn't sell

the shares in early 2001 even though the value of those shares was then less than half of the tax liability. Later that year, I submitted an Offer In Compromise of about half the value of my IRA, which at the time was about \$40k. It was rejected.

Today I am living with my wife's family, on disability, with virtually no savings other than a very modest IRA which today is worth about \$10k. My tax liability has increased through penalties and interest to about \$200k. The appeal of my first Offer In Compromise was rejected in May 2003 since at that time, although confined to a wheelchair, I was still employed even though I explained that since my condition, Freidriech's Ataxia, was progressive and incurable, it was not likely that I would be able to work for more than 9-12 more months. I finally had to quit work in March of 2004, about 10 months after my appeal.

The tax liability that I have is ridiculous and unfair. The fact is, if the AMT threshold of \$40k, which was established in the late 1960's, had been adjusted for inflation, the unintended victims of this shortsighted tax law would still be unaware of what AMT means.

In my case, the tax liability has hung over my head now for more than 4 years. I have submitted another Offer In Compromise, this one significantly smaller than the one that was rejected over 2 years ago. I no longer own a home and my savings has dwindled. The appeals agent at the IRS that heard my first Offer told me that although she sympathized with my situation, her hands were tied by the Service and she could not accept my offer.

If the AMT tax was simply applied in the manner it was intended when it was established, even during the tech bubble, the average worker who had been rewarded by her company for excellent work would not face financial ruin at the hands of the IRS. After all, I didn't benefit from owning that stock. Why should I owe any tax on it? Why should I owe so much more than I am worth? Why doesn't the IRS allow it's appeals agents to make decisions that are good for the treasury and good for the individual taxpayer?

I have a Collection Due Process hearing scheduled for Sept. 1. After that meeting, even as I continue to be optimistic, I will probably consult with my legal representative about filing for bankruptcy. I owe much more than 10 times my net worth in taxes and my only income is Social Security Disability and the long term disability provided by a private insurer. My IRA is being decimated by legal fees and I am utterly powerless to stop this unfair and unreasonable action against me and my family.

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Manchester, Michigan 48158  
*August 31, 2005*

#### House Ways and Means Committee

I am an average middle class American working in the high tech computer industry. I have been employed with the same company for about 7 years. I was granted ISO stock options as part of my compensation package when I first started. During the Internet boom on the stock market, my ISO stock options had a paper value of approximately \$2M. I never saw this money due to the dramatic rise and then crash of the stock market valuations. In the year 2000, I had income of approximately \$100,000. However, when my accountant calculated out what I owed due to AMT, the amount equaled \$371,000. . . . This is due to the overvaluation of the stock during the year 2000 and not taking into account the dramatic fall of the stock. I was absolutely certain the accountant was wrong, because how could tax rates exceed my entire income! I checked with many attorneys, and tax accountants to find that, in fact, the accountant was correct and it was due to a little known tax called Alternative Minimum Tax, which is basically an interest-free loan to the government that gets credited back to you over time. . . .

So, I entered the paperwork that says I owe \$371,000, however I did not have the money, nor do I have it today. In fact, that stock that was valued at \$150 per share was now trading at \$5 per share and my option price was \$4.28 per share. So, my stock value that was left was less than \$10,000. As you can see the AMT is not working the way it was intended. I conducted a lot of research into the tax, the history, and joined an organization that is made up of many other hard-working, honest taxpayers that this has affected.

My wages are currently being garnished by the IRS and only allowed to take home \$332 per week. With the current gas prices over \$3.00 per gallon, it costs me about \$32 a day to drive to work and back home. So after paying for gas, I am left with about \$172 per week. I am borrowing money weekly to stay afloat financially and going into more debt by the day. . . . My life is being destroyed by a huge, un-

fair tax burden and since I am also raising 2 children, I am barely able to buy them groceries, let alone put money away for their college education. I have filed for an installment agreement with the IRS and that was denied. I have filed appeals with the IRS and those were denied. I am currently looking for help in any fashion to pay the IRS a reasonable amount to move on and get on with my life. When the accountant did my taxes without AMT for 2000, the tax would have been \$10,000 extra over what I paid thru the year. However, even when I offered to pay the IRS \$1,000 every month for 7 years, (\$84,000) they refused and continue to take my paychecks except the \$332 per week they think I can live on. . . . HELP!!!!

Michael K. Brown

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**Submission of Herman Cain, New Voters Alliance, Stockbridge, Georgia**  
***The Federal Tax Code Must be Replaced with a Fairer and Simpler System***

**I. Introduction**

The current income tax system cannot be reformed. It creates disadvantages for multinational businesses, domestic businesses, individuals, and our government.

No amount of tinkering with a portion of the tax code is going to fix it. It is too complicated. It inflates the costs of U.S. goods and services to other nations. It is too unfair and inefficient. It discourages people from working harder to achieve upward economic mobility, which destroys hope and opportunity.

The current tax system needs to be replaced. It can be replaced with an integrated plan including a progressive national sales tax, also known as the FairTax (H.R. 25 and S. 25).

Several commissions over the last twenty years, including the one I served on in 1995 (The National Commission on Economic Growth and Tax Reform or Kemp Commission), have all concluded that a replacement tax system should satisfy six principles.

First, it should promote economic growth by reducing marginal tax rates and eliminating the tax bias against savings and investments.

Second, it should promote fairness by having one tax rate and eliminating all loopholes, preferences and special deductions, credits, and exclusions.

Third, it should be simple and understandable. Simplicity would dramatically reduce compliance costs and allow people to truly comprehend their actual tax burden.

Fourth, it should be neutral rather than allowing misguided officials to manipulate and micromanage our economy by favoring some at the expense of others.

Fifth, it should be visible so it clearly conveys the true cost of government and so people would not be subjected to hidden changes in the tax law.

Sixth, it should be stable rather than changing every year or two so people can better plan their businesses and their lives.

In remarks made in March 2005 before the President's Advisory Panel on Federal Tax Reform, Federal Reserve Chairman Alan Greenspan stated, "Many economists believe that a consumption tax would be best from the perspective of promoting economic growth particularly if one were designing a tax system from scratch because a consumption tax is likely to encourage saving and capital formation."

Consider the compelling advantages of replacing the current income tax code with the FairTax.

- Gross Domestic Product increases, according to several independent economists, by 10.5 percent in the first year and levels off in succeeding years at approximately 5 percent annually.
- Consumer prices decrease, again according to independent economists, an average of 12 to 25 percent due to corporate taxes and compliance costs currently embedded in the costs we pay for goods and services.
- A single-rate national sales tax rate on all new goods and services at approximately \$0.23 from every dollar spent is revenue-neutral and replaces the current annual tax revenues of nearly \$2 trillion.
- The annual amount of tax avoidance by an army of 18-million non-filers, according to IRS estimates, is nearly \$300 billion. This amount does not escape the FairTax.
- The annual cost of compliance with the tax code is estimated at over \$250 billion. In addition, businesses and taxpayers spend nearly seven billion hours each year filling out their IRS forms and many more calculating the tax implications of business decisions.

- The annual amount of tax loss due to illegal activity is estimated between \$500 billion and \$1 trillion. Under the FairTax, those engaged in illegal activities no longer avoid paying their fair share.
- Imported goods are treated the same as domestically produced goods. This means U.S. businesses are much less likely to locate their plants overseas and foreign manufacturers are far more likely to locate their plants in the U.S.A.
- All taxpayers have an equal voice, not just people who can afford tax lobbyists and skilled tax accountants.
- The FairTax effectively untaxes the poor, due to its rebate provision, greatly simplifying the current earned income tax system, while better encouraging work. What encourages work more than no federal taxes of any kind being taken from a paycheck?
- The FairTax does not punish those who work second jobs to improve their family's economic situation.
- The FairTax untaxes education, by allowing parents to save and invest for their children's futures.

These advantages of the FairTax plan have been well researched, analyzed, and documented by some of the most respected business people, economists, and academicians in the country. Hundreds of thousands of citizens are now actively supporting a change from an income tax to this national sales tax on consumption. The FairTax unleashes the full potential of the U.S. economy, and the potential inside businesses and individuals to pursue economic freedom.

## **II. Description of proposal**

The FairTax is a non-partisan proposal that abolishes all federal income taxes including personal, estate, gift, capital gains, alternative minimum, corporate, Social Security, other payroll, and self-employment taxes and replaces them all with one simple, visible, federal retail sales tax.

The FairTax dramatically changes the basis for taxation by eliminating the root of the problem: Taxing income. The FairTax taxes us only on what we choose to spend, not on what we earn. It does not raise any more or less revenue; it is designed to be revenue neutral. The FairTax is a fair, efficient, and intelligent solution to the frustration and inequity of our current tax system.

### **Collection Methods**

Retail businesses collect the tax from the consumer, just as state sales tax systems already do in 45 states; the FairTax is simply an additional line on the current sales tax reporting form. Retailers collect the tax and send it to the state taxing authority. All businesses serving as collection agents receive a fee for collection, and the states also receive a collection fee. The tax revenues from the states are then sent to the U.S. Treasury.

### **Impact on Businesses**

Today, too many layers of business, income, payroll, capital gains, and estate taxation provide numerous disincentives to expand businesses and hire new workers. According to Harvard University Economics professor Dr. Dale Jorgensen, embedded costs from various forms of taxation account for an average of 22 percent. These embedded costs are, of course, **passed on to consumers like any other cost of production.**

**To remain competitive, each year businesses are forced to ship manufacturing plants and jobs overseas.** Stifling self-employment taxes and the paperwork required to comply with them discourage individuals from exercising the entrepreneurial spirit and pursuing their American dreams.

The FairTax allows U.S. businesses to sell their exports overseas for approximately 22 percent less, on average, than they do now, and with similar profit margins. With the FairTax system in place, businesses can choose to expand their capital investments, hire more employees, pay employees higher wages, and lower consumer prices.

### **Distribution of the Tax Burden**

Under the FairTax, the tax burden falls on those who spend, and it falls greatest on those who spend the most on new goods and services.

The FairTax also contains a rebate feature. All Social Security cardholders who are legal U.S. residents receive a monthly rebate equivalent to the FairTax paid on essential goods and services up to the poverty level. The size of the rebate is determined by the Department of Health and Human Services' poverty level multiplied by the tax rate. This calculation includes considerations for food, clothing, shelter, and medical care.

The rebate feature, which is funded from the sales tax revenues, effectively untaxes the working poor and those on fixed incomes. In addition to receiving the monthly FairTax rebate, these taxpayers are freed from regressive payroll taxes, the federal income tax, and the compliance burdens associated with each. They no longer pay the imbedded taxes on goods or services, and they can purchase used goods tax free.

Because of the rebate feature, those below the poverty line have a negative effective tax rate and lower middle-income families enjoy lower effective tax rates than they do today.

Under the FairTax, the tax burden is fairly distributed. It is, in fact, much more fairly distributed than under the current income tax code. Wealthy people spend more money than other individuals. The FairTax taxes them on their purchases and as a result, they pay both a higher effective rate and more in taxes.

The FairTax is premised on the notion that it is fairer to tax individuals when they consume for themselves above the essentials of life, rather than when they invest in their businesses and their children's futures.

Education is one of the keys (along with savings and hard work) to an improved standard of living. That certainly was true in my case. I was the first person in my family to attend and graduate from college. It took a lot of hard work, and a lot of sacrifice by my parents. The FairTax is education friendly and is dramatically more supportive of education than current law. The FairTax embodies the principle that investments in people (human capital) and investments in things (physical capital) should be treated comparably. The current tax system, in stark contrast, treats educational expenditures very unfavorably.

For nearly every citizen, attainment of a quality education is an absolute minimum requirement for success in life, whether you measure success by economic status or virtually any other standard. Yet the tax system today punishes people who invest in education, virtually doubling its cost.

Today, to pay \$10,000 in college or private school tuition, a typical middle-class American must earn \$15,540 based only on federal income taxes and the employee payroll tax.<sup>1</sup> The amount one must earn to pay the \$10,000 is really more like \$20,120, once employer and state income taxes are taken into account.<sup>2</sup>

The FairTax does not tax education expenditures. Education is paid for with pre-tax dollars. This is the equivalent of making educational expenses deductible against both the income tax and payroll taxes today. Thus, a family needs to earn \$10,000 to pay \$10,000 in tuition, making education much more affordable. The FairTax makes education about half as expensive to American families compared to today.

### **Exemptions, Deductions, Credits, and Exclusions**

Exempting items by category is neither fair nor simple. Numerous studies have shown that the wealthy spend much more on unprepared food, clothing, housing, and medical care than do the poor. Exempting these goods, as many state sales taxes do, actually gives the wealthy a disproportionate benefit. Also, today these purchases are not exempted from federal taxation. The purchase of food, clothing, and medical services is made from after-income tax and after-payroll tax dollars, while their purchase price hides the cost of corporate taxes and private sector compliance costs. Tax lobbyists and special interest groups work hard every day to create and protect tax credits, loopholes, and deductions that benefit their clients. Those who have the money will send lobbyists to Washington to obtain special tax breaks in their own self-interest. This process causes unfair and inefficient distortions in our tax code and our economy and must be stopped.

Though the FairTax eliminates all credits, loopholes, and deductions, homeowners and those who contribute to religious and other charitable organizations realize a greater financial benefit than they do under the current system. Currently, 70 percent of taxpayers do not itemize deductions on their income tax returns. Of the 30 percent who do itemize deductions, those who take the home mortgage interest deduction pay their interest with post-Social Security/pre-income tax dollars. They then pay their principal with post-SS/post-income tax dollars. The 70 percent who do not itemize receive no tax benefit at all. Under the FairTax, all homeowners make their entire house payment with pre-tax dollars. With the FairTax, mortgage

<sup>1</sup>\$15,540 less 7.65 percent in employee Social Security and Medicare payroll taxes (\$1,189) less 28 percent in federal income taxes (\$4,351) leaves \$10,000.

<sup>2</sup>Economists generally agree that the employer share of payroll taxes is borne by the employee in the form of lower wages. This figure assumes that employees bear the burden of the employer payroll tax and that they are in a seven percent state and local income tax bracket. \$20,120 less \$5,634 in income tax (28 percent), \$3,079 in payroll taxes (15.3 percent) and \$1,408 in state and local income taxes (7 percent) leaves \$10,000.

interest rates fall by about 25 percent (about 1.75 points) as bank overhead falls; this is a huge savings for consumers. For example, on a \$150,000, thirty-year home mortgage at an interest rate of 7.00 percent, the monthly mortgage payment would be \$999.12. On that same mortgage at a 5.25 percent interest rate, the monthly payment is \$830.01. Over 30 years, the 1.75-percent decrease in interest rates in this instance results in a \$60,879 cost savings to the consumer. First-time buyers also benefit under the FairTax, which allows them to save for a down payment much faster. Under the FairTax, home ownership is a possibility for many who have never had that option under the income tax system. Lower interest rates, the repeal of the income tax, the repeal of all payroll taxes, and the rebate mean that people have more money to spend, and have an increased opportunity to become homeowners. Contributions to religious and charitable organizations depend on one factor more than any other: The health of the economy.

For all of the money that pours into churches every Sunday and into a broad range of charities every day, only the 30 percent of donors who itemize deductions receive any tax benefit. The other 70 percent donate their money and receive no tax benefit. The FairTax allows all people to make charitable contributions from pre-tax dollars. As a result, those generally less affluent taxpayers who do not itemize see their cost of charitable giving go down under the FairTax. The wealthy make decisions on charitable giving based on the cause. Once they have determined the cause is worthy, their contribution is structured to maximize the gift and minimize the tax. But the intention to give comes first; taxes simply determine the structure—rarely the amount—of the gift.

### **III. Impact of proposal relative to current system**

#### **The FairTax Encourages Economic Growth**

The FairTax significantly enhances economic performance by improving the incentives for work and entrepreneurial activity and by raising the marginal return on savings and investments.

Entrepreneurs and small business owners get greater access to capital, the lifeblood of a free economy. Investments rise, the capital stock grows, productivity increases and the output of goods and services expands. The economy creates more and better paying jobs for American workers and payrolls increase considerably.

Although the magnitude of the economic growth generated by a single-rate, neutral tax system causes lively debate among economists, virtually all agree that the large marginal tax rate reductions with a national sales tax, combined with neutral taxation of savings and investments, has a powerful positive effect on the economy.

For example, Dr. Jorgensen conducted a research analysis in 1997 that showed that a national sales tax produces a 10.5-percent increase in Gross Domestic Product, a 76-percent increase in real investments, and a 26-percent increase in exports in the first year of a national sales tax enactment.

Those increases level off at 5 percent, 15 percent, and 13 percent respectively over the succeeding twenty-five years. Nothing promotes the competitiveness of U.S. businesses more than growth in our national economy, more dollars to grow our businesses, and a level playing field for selling our products and services to other nations.

#### **The FairTax is Simple**

The FairTax is a simple, single-rate tax on the retail price of new goods and services. Individuals who are not in business have absolutely no compliance burden, nor are they subject to the discretionary interpretation of the current, convoluted tax code.

Businesses also benefit under the FairTax. There is no more alternative minimum tax, no more depreciation schedules, no more complex employee benefit rules, no more complex qualified account and pension rules, no more complex income sourcing and expense allocation rules, no more foreign tax credit, no more complex rules governing corporate acquisitions, divisions and other reorganizations, no more uniform capitalization requirements, no more complex tax inventory accounting rules, no more income and payroll tax withholding, and the list goes on. Retail businesses simply need to keep track of how much they sold to consumers.

Compliance costs, therefore, fall under the FairTax while compliance improves. Today, individuals and businesses spend about \$250 billion each year and an estimated seven billion hours filling out forms, hiring tax lawyers, accountants, benefits consultants, and collecting information needed only for tax purposes. To the extent these costs are incurred by businesses, they must be recovered and consequently are embedded in the cost of everything we buy.

In addition, the FairTax is easy to collect. Retail businesses collect the tax from the consumer, just as state sales tax systems already do in 45 states; the FairTax

is simply an additional line on the current sales tax reporting form. Retailers simply collect the tax and send it to the state taxing authority. All businesses serving as collection agents receive a fee for collection, and the states also receive a collection fee. The tax revenues from the states are then sent to the U.S. Treasury.

#### **The FairTax is Neutral**

Under the FairTax, all consumption is treated equally. The current tax code punishes those who save and rewards consumption. Under the FairTax, the tax system is no longer in the business of picking winners and losers. The tax code is neutral in the choice between savings and consumption, neutral between types of savings and investments, and neutral between types of consumption.

#### **The FairTax is Visible**

The FairTax is highly visible, because there is only one tax rate. Moreover, all citizens are subject to any tax increases, not just a targeted few. It would be much harder for Congress to adopt the typical divide-and-conquer, hide-and-disguise tax increase strategy it uses today. The FairTax explicitly states the contribution to the Federal Government each and every time a new good or service is purchased—right at the bottom of the retail sales tax receipt.

#### **The FairTax is Stable**

The FairTax is a more stable source of government revenues than the present system for two reasons.

First, because it is so simple and transparent, it does not invite tinkering in the way that the current system does with its thousands of pages of code and regulations. The public would resist attempts to make it more complex and they would resist any attempts by Congress and special interests to reward certain groups or certain types of behaviors.

Second, taxing consumption is a more stable source of revenue than taxing income. There are fewer fluctuations in the consumption base than in the income base. A recent study by the American Farm Bureau Federation showed that for the years 1959 to 1995, a national sales tax base was less variable than the income tax base. Why? When times are unusually good, people will usually save a little more. People tend to smooth out their consumption over their lifetime. They borrow when young, save in middle age, and spend more than their income in retirement.

### ***IV. Transition, tradeoffs, and special issues***

#### **The FairTax is Revenue Neutral**

The 23-percent tax rate, when compared to current income and payroll tax rates, has been carefully calculated to (1) raise the same amount of federal funds as are raised by the current system, (2) pay the universal rebate, and (3) pay the collection fees to retailers and state governments. Unlike some other proposals, this rate has been independently confirmed by several different non-partisan institutions across the country. Detailed calculations are available from [www.FairTax.org](http://www.FairTax.org).

The FairTax pays for all current government operations, including Social Security and Medicare. Government revenues are more stable and predictable under a consumption tax than with the federal income tax, because consumption is a more constant revenue base than is income.

If you were in a 23-percent income tax bracket, the Federal Government would take \$23 out of your paycheck for every \$100 you made. With the FairTax, if the Federal Government receives \$23 out of every \$100 spent in America, the same total revenue is delivered to the Federal Government. This is revenue neutrality.

So, instead of paycheck-earning Americans paying 15.3 percent of their payroll in Social Security and Medicare payroll taxes, plus an average of 18 percent of their paychecks in federal income tax, for a total of about 33 percent, consumers in America pay only \$23 out of every \$100 they chose to spend. The FairTax is progressive, since it is collected only on spending above the federal poverty level.

### ***V. Summary***

Sales taxes as a stable and reliable source of revenues are not new—most Americans come into contact with sales taxes daily, since 45 states currently use them to collect state revenues. It is easier to switch from an income tax to the FairTax system than it is to switch from gallons to liters or from feet to meters! Of course, those who depend on the structure and complexity of our current system (e.g., tax lobbyists, tax preparers, and tax shelter promoters) will have to find more productive economic pursuits (and they will fight the FairTax plan tooth and nail). However, everyone will have enough advance notice to adjust to the new system.

Under the FairTax, everyone has to think about taxes in a different way. Income—what we earn—no longer has to be documented, measured, and kept track



of for tax purposes. The only relevant measure of our tax liability is the amount we choose to spend on final, discretionary consumption. Tax-related issues suddenly become a lot simpler and more straightforward than they used to be. The aggravation and anxiety associated with “April 15th” disappear forever after passage of the FairTax.

Under the FairTax, job creation booms. Residential real estate booms. Financial services boom. Exports boom. Retail prospers. Farming and ranching prosper. Churches and charities prosper. Civil liberties are enhanced. In short, it is difficult to imagine all the far-reaching, positive effects of this change from taxation on income to taxation on consumption.

The future stability of our nation’s economic infrastructure, and the future for our children and grandchildren, will be determined by the political will and courage in Congress to be aggressive with solving the big issues such as the tax code mess. The 92-year-old income tax code thwarts the natural, individual motivation of citizens to use their God-given talents to pursue happiness and their respective dreams.

Conversely, the FairTax allows all Americans to own all the returns on their sweat equity as the fruits of their labor. Ownership lets people realize their dreams and opportunities and is the key to the greatest nation on earth remaining the greatest nation. We have a moral obligation to protect our Founding Fathers’ vision and to protect the unalienable right of ownership for our grandchildren.

It’s our unalienable responsibility.

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Coalition for Tax Fairness  
Arlington, Virginia 22209  
*August 31, 2005*

To Honorable Chairman Dave Camp, Honorable Ranking Member Michael McNulty, and the Honorable Members of the Select Revenue Measures Subcommittee:

The Alternative Minimum Tax (“AMT”) has received substantial negative press because of its many anomalous provisions. In the case of the AMT imposed on incentive stock option exercises, taxpayers are being forced into bankruptcy ***with tax rates of 300% or more of their income.***

The Coalition for Tax Fairness fully endorses and supports H.R. 3385, legislation introduced by Representative Sam Johnson that provides focused relief for those taxpayers being most seriously harmed by the AMT’s unintended consequences—those trapped by the AMT’s treatment of incentive stock option exercises. H.R. 3385 has already received significant bi-partisan co-sponsorship. We urge the Select Revenue Measures Subcommittee to support this fair and important legislation critical to the financial survival of tens of thousands of hard-working, honest Americans.

*I. H.R. 3385 Addresses a Severe and Unintended Consequence of the Tax Code*

During the 1990s, many employers offered ISOs as compensation to attract more talented employees than they could otherwise afford. Congress encouraged this type of employee investment in their companies and in the economy by creating tax rules that did not tax ISOs upon their exercise and encourage a quick sale, but instead rewarded taxpayers by offering the more favorable capital gains tax rates to those who held their stock for one year.

The AMT, in the context of the economic downturn, eliminated these benefits without any warning and sent taxpayers into a downward spiral from which many have yet to recover. The AMT taxed the transaction on the exercise date as though the taxpayer actually sold the stock immediately and realized a gain, even though he did not receive any actual gain and in fact the stock lost most or all of its value prior to sale. The AMT therefore caused massive tax prepayments on phantom income.

Those entrepreneurs and company employees subjected to this AMT have ended up owing massive prepayments of tax for income never received. ***These prepayments have become interest-free loans to the government that, due to further quirks in the law, will never be repaid.*** Those taxpayers who do not have the resources to make these massive interest-free loans to the government are incurring interest and penalties. Many have lost (or are in the process of losing) their homes, retirement savings, and college savings—while the prepayments they are making build up more useless AMT tax “credits.” Those who exercised ISOs, in the years 1999–2003 especially, and did not sell (in many cases upon the advice of their trusted advisers or due to insider trading restrictions) continue to suffer greatly at the

hands of the AMT. Adverse market conditions and a conflict between the tax and securities laws exacerbated the problem.

#### II. *Summary of H.R. 3385 Relief and Revenue Generating Provisions*

H.R. 3385 will alleviate current and future suffering through refunding the prepayments over a five year period, once the credits have been outstanding for more than four years. This will allow people a window of hope where they can see an end to the financial ruin nightmare they have been enduring.

***H.R. 3385 alleviates this unfair and unnecessary suffering in a manner that generates revenue through enhancing future compliance.*** This Bill reinforces compliance by providing for corporate “matching” reporting to the IRS of employees’ ISO exercises, thereby increasing voluntary compliance and ensuring everyone pays their fair share. This measure prospectively institutes mandatory reporting of ISO exercises, without any additional administrative cost, thereby substantially increasing tax revenues.

#### III. *H.R. 3385 is Good Tax Policy and Good for the Economy*

The irony in this situation is that many people are paying significant interest on loans from private creditors to prepay their interest-free loan to the government. In some cases, the amounts at issue exceed hundreds of thousands, even millions, of dollars. Additionally, the IRS is increasing the burden by imposing interest and penalties on the taxpayers who haven’t been able to pay all of their AMT because they simply lack the financial resources. Under the proposal, returning an excessive AMT prepayment is not a tax *rebate*, nor is it an unprincipled refund. The AMT credits were in fact intended to be returned to the taxpayers in a reasonable time, and to the extent the quirks in the AMT code undermine this repayment intent and extend the “repayment period” out to tens and hundreds of years—H.R. 3385 fixes this mistake.

Without the passage of H.R. 3385, the current application of the AMT/ISO provision will continue to cause unintended, egregious, and devastating tax burdens, and hobble the very entrepreneurial drive that made small business a powerful engine of the U.S. economy. With the passage of H.R. 3385, citizens can spend their ambition, time, and effort growing the U.S. economy—rather than fighting unjust tax laws.

We urge the Select Revenue Subcommittee to fully support this fair and urgent relief for the good of the economy and to give American taxpayers the fair treatment they deserve.

Timothy J. Carlson  
*President*

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#### Submission of Earl Carter, Huntsville, Texas

Distinguished Members of the House Committee on Ways and Means:

First, allow me to thank you for undertaking this most important hearing! It is hugely important to the country that you get it right in reforming our tax code as we will all live with the result for a long time.

Pursuant to that, the only current tax reform proposal that meets ALL the criteria set forth by the President in his charge to the members of his tax reform panel is the proposal set forth in H.R. 25/S. 25, the FairTax plan. Nothing else even comes close in my estimation.

Under the FairTax, the United States will become the most attractive industrialized country in which to manufacture in the world! The cost of capital will decline dramatically. American manufacturers will be more competitive in the global marketplace. American firms will be much more likely to build plants in the U.S. Foreign firms are likely to find the U.S. a highly attractive place to build their plants to serve U.S. and foreign markets, given the stable political environment, an educated workforce, the large domestic market and the lack of an income tax. The construction and operation of these new plants would generate relatively high-paying jobs. Exports would no longer bear the burden of embedded income and payroll taxes and imports would bear the same sales tax burden as domestically produced goods. For the first time, exported and imported goods will have the same tax treatment. Imported goods will no longer be advantaged over domestically produced goods.

The overall U.S. economy will grow dramatically under the FairTax. All known economic projections predict a much healthier economy. Real wages will increase.

People will be able to purchase more and better homes in a healthy economy. Typical estimates are that the economy will be 10 to 14 percent larger than it would have been under the income tax within 10 years, and both production and consumption will grow substantially. Some studies show the potential gains to be much higher. Manufacturers will make more money in a prosperous, growing economy.

The Fairtax plan would also go a long way toward solving the solvency issues currently existing in our Social Security and Medicare programs as well.

And last but far from being least, the Fairtax would return our country's taxing method to something much more in keeping with methods envisioned by our founders as opposed to the current progressive income tax which was endorsed by Karl Marx and Frederick Engels in their "Manifesto of the Communist Party."

The progressive income tax properly needs to be put where its' main adherents political philosophy has already found itself, on the ash heap of history, and I beg you to do exactly that by replacing it with a NRST very similar to that set forth in H.R. 25/S. 25!

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Cupertino, California 95014  
August 31, 2005

To Honorable Chairman William M. Thomas and House Ways and Means Committee

Dear Honorable Chairman Camp and Ranking Member McNulty

I have submitted my testimony and shared my story at the following hearings:

6-15-2004, Ways & Means Hearing on Tax Simplification, Oversight Subcommittee

3-17-2005, President's Tax Reform Advisory Panel

6-08-2005, Hearing on Tax Reform, Full Committee

I now wish to share my story directly with you in hopes of garnering your support and leadership of the Honorable Sam Johnson's H.R. 3385.

Recent updates since my last testimony submission. The IRS is now requesting that I prepay an additional \$400,000, and \$600,000 in penalties and interest. It's not bad enough that I already overpaid my taxes by \$1.4 million, a 2000% tax bracket that will take me 433 years to have returned to us, but they want to now place me in a 3500% tax bracket that will take me 800 years to have returned to me. If this isn't legalized extortion I don't know what you would call it!!! It is ludicrous to cause such a cash flow/bankruptcy situation on the American public for the sake of prepaying a tax that isn't really owed and never returned even after the gain/loss has been determined.

God bless this great country and you our leaders to break the chains of tyranny we find ourselves captive of.

We respectfully and urgently request your support of H.R. 3385.

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Dear Chairman Thomas and Committee Members: My name is Joseph Cena and I am writing on behalf of my family, Dawn and Justin. We appreciate the opportunity to discuss the hardships we have suffered due to the challenges that have been set forth by the Alternative Minimum Tax Laws. We hope that our situation can assist with putting into place changes that will allow for more reasonable tax policy as opposed to such restrictions that have been causing financial turmoil and ruin for so many Americans.

I am attaching the original letter that we submitted June 04 to the Ways & Means Oversight "Tax Simplification Hearing" although the language is a tad bitter, I felt it needed to be included as we truly feel that this has come to harm so many taxpayers. It was a plea for help because our situation, while unique, is so similar to many other Americans and we felt helpless. My only hope is that you will read it with compassion and be open-minded as there are thousands of stories that are more heart wrenching than ours.

Please help us implement a new tax law that does not create a phantom tax on unrealized gain. No one should have to pay tax for something that is not tangible, but rather looks good on paper. We beg of you and your Committee Members to take a look at how this would affect you if you were faced with the same situation. Only then will change be possible.

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Joseph Cena & Dawn Hasegawa

I write to thank you for taking on the difficult task of simplifying our tax code. I respectfully enlist your support and ask you to please act for the sake of thousands of families who are being financially decimated (mine included), for the sake of the general U.S. economy that is being adversely affected, to help hard-working taxpayers regain faith in the IRS and to repeal one of the most egregious applications of Tax Policy ever enacted: the dreaded and stealthy Alternative Minimum Tax (AMT).

This woefully outdated policy forced me and my family into a **2000% tax bracket** in 2000 and required us to provide an **interest free loan to Treasury** that will take us **433 years** to receive back!!

**A little bit about us:**

My family has lived and worked in California for 26 years. Our home is a 56-year-old, 1,245 sq. ft., 3-bedroom ranch home in Cupertino, California. We have a 9-year-old son, Justin. My wife, Dawn, is a unionized Registered Nurse of 23 years who is currently working in the Stanford University Hospital Emergency Room. Both of us are approaching our fifties, and our living parents require our financial support, which we are unable to provide in our current situation. As you will easily understand, our experience with the AMT has been very stressful on our family and we have come close to divorce over this!

I started my career in the electronic manufacturing sector working on programs for the Department of Defense, the first MRI unit, and other dynamic technological areas of industry. I proceeded to Stanford University where I consulted on exciting projects such as the Hubble Telescope, Sun-Net, the Rel-Gyro project (Testing Einstein's Theories), and helped the founders of Cisco Systems. From there it was back into High-Tech in 1994–2001 at Synopsys, and Network Appliance. Both firms offered stock options, and were on growth paths of 50–100% growth year over year. I typically worked 10–14 hours per day, 5–6 days a week.

While I was a Customer Service Manager at Network Appliance, I was diagnosed with a life threatening disability and in December 2000, I started chemotherapy treatment. In spring 2001, while undergoing chemo, our accountant informed us that we were subject to a parallel tax called AMT and we were responsible for \$2.1 million in tax to the IRS and California even though we didn't sell or have a gain.

I was shocked to learn that the tax imposed had absolutely no correlation to actual gains; and that it would actually be an **overpayment of \$1.4 million!!!** How is it possible that a law that was enacted in 1969, to catch 155 wealthy people who didn't pay taxes, is now forcing tens of thousands of hard-working citizens and entrepreneurs to legally **pre-pay a tax** and making it nearly **impossible** for them to recoup the overpayment in their, or their children's lifetime? To add insult to injury, the taxpayers who overpaid their taxes to the government do not earn interest on their own money even though Congress has established such safeguards for consumers requiring banks, escrow companies, landlords and others to provide interest income even on funds held in trust for even just a short term.

Many are being driven into bankruptcy over phantom gains. I am certain that Congress did not intend to drive people to bankruptcy when it created the AMT in 1969. Under the regular tax system if a taxpayer overpays, he or she receives a refund in a lump sum, not so under AMT.

**Impact on us and the U.S. economy by not having our tax credit returned:**

Other than perhaps homeland security, there is no more important issue affecting my family than the AMT. Thankfully, my illness is now in remission. My wife and I had wanted to have more children, but we discovered we are medically unable. We then thought to adopt but we are financially unable to do so. I was laid-off during my disability in 2001 and have been out of work for three years. My unemployment ran out long ago and we need the money. For example, my wife's 1991 Nissan truck has 133,000 miles and needs replacing. It would help us tremendously even if all we received was the interest on our credit.

I have drawn up few business plans for "start-ups," one a consumer wireless application, real estate venture and others. If I had my credit back I would put it to use to launch these businesses and help contribute to our economy—putting people back to work—people who would be paying income tax!!

Thank you for your time and consideration. I hope that with your leadership and help Congress can quickly enact a fair and principled reform to the ISO-AMT provisions and help us grow the economy.

Joseph Cena & Dawn Hasegawa

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Foster City, California 94404  
*August 30, 2005*

The Honorable Chairman William M. Thomas  
 The House Ways and Means Committee

To the Honorable Members Ways and Means Committee:

Thank you for giving me the opportunity to write to you concerning tax reform. Specifically, I would like to address the Alternative Minimum Tax and its treatment of Incentive Stock Options.

My name is Jeffrey Chou, and I have a wife and 2 daughters—one is 4 years old, and the other is 1 year old. We currently face an AMT bill, from exercising Incentive Stock Options, which is greater than all our assets. And, because of the new bankruptcy laws that will be going into effect in October, we are seriously considering declaring bankruptcy within the next month. This issue cannot be more urgent. H.R. 3385 is the only bill that will save me from financial ruin by being taxed on money I never received.

In 1996, I left a secure, stable job at a large company to help start a communications company as an engineer. My compensation consisted of an annual salary of \$80,000 and Incentive Stock Options. Cisco Systems eventually acquired us. It was a happy time for my family, thinking that my hard work in helping to build a company would finally pay off.

In 2000, we decided to exercise my stock options, and were advised to hold the stock for 1 year. We did not and do not live extravagant lifestyles. We live in a 3 bedroom townhouse—I drive a 1997 Toyota, and my wife drives a 1998 SUV. We have good credit and have always paid our taxes in full and on time. In April 2001, following my exercise of the Incentive Stock Options, we faced federal and state taxes of \$2.4M, more than 6,000% of our normal income tax and more than everything we owned. We also faced an ethical and moral dilemma. As we sought professional help to deal with this tax liability, several CPAs advised us not to comply with the law—to simply omit reporting the exercise and the tax. We discovered that the AMT on exercising stock options is a self-reported tax. Many of my friends and colleagues took this approach, did not report their exercise of stock options, and to this day, live happy lives.

However, we decided to “do the right thing” and comply. We had faith that our country, in return, would also “do the right thing” and not ruin its honest taxpayers. Since then, the IRS has sent us threatening letters, placed a lien on our names, attempted to levy our accounts, and actually visited our house demanding payment. The IRS rejected our Offer In Compromise and we appealed. The appeals officer admitted to us that our offer was in good faith and was reasonable, but that he still could not accept it. Today, we are in IRS collections.

I do know that those who did not report are certainly glad they didn't. And I also know that among the many honest people I have met over the last 3 years whose situation is similar to mine, few or none, if faced with the same choice, would comply again. Why volunteer for a 100% guarantee of ruin, when you can win the audit roulette 99.9% of the time? My friends, if caught, will simply claim ignorance of the law. I am told it will be hard to prove that they were not ignorant of the law given how many tax experts are unaware of the consequences of the interaction of the AMT with Incentive Stock Options.

You may ask “Why didn't you sell?”

We are not sophisticated investors. I am an engineer; and my wife is a stay-at-home mom. We listened to advice that told us to hold for 1 year. At the time, I had no knowledge of diversification or hedging strategies. I worked 12 hour days trying to build products and meet schedules. At night, I returned home to help my wife with our newborn daughter. That was my life. In addition, our CEO, all throughout 2000, even as late as December, kept touting Cisco's optimistic future, saying “we will be the most powerful company in history,” “we are growing 30 to 50% every year,” and “we are breaking away from our competitors.” At the time, he was never wrong before, so I felt no sense of danger for my job, for my company, or for the stock. I had faith in my company and its leaders.

I sincerely ask Congress to help those in my situation. We are all honest taxpayers who want to do what is right for the country. Most of us are hard-working Americans who helped build a company and who wanted to remain part of that company instead of “cashing in.” We also want to pay our fair share of taxes—but please tax us like any other investor—tax us when we realize our gains, not on what we might have gained.

I believe things happen for a reason. If I can be a small part in helping to correct this injustice, the faith I have in this great country is justified. My family and I respectfully ask for your support of H.R. 3385. We hope that its passage will come before our bankruptcy completes and our home is lost.

This is the highest priority of my life. Please do not hesitate to contact me any time for any reason.

Jeffrey Chou

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Durham, North Carolina 27705  
August 31, 2005

Dear Chairman Thomas and Committee Members:

My name is John Cole, and I am writing to you to share my story of a severe problem related to the Alternative Minimum Tax (AMT) and the way it has been applied to employee stock options. If you will bear with me I would like to begin by providing some personal background information.

I was born in 1958, and grew up in Durham, NC. In 1977 at the age of 19 I moved to the San Francisco Bay Area, and for the next dozen years had a variety of blue collar jobs including home construction, cooking and waiting tables in restaurants, and working for moving companies. In 1989 at the age of 31 I went back to California Community College where I studied Computer Science for two years. When I was 18 I had attended College for 1 year, but had no clear direction and did not do well, which ultimately led to my withdrawing from school and heading West. However, the second time around I was highly motivated and extremely focused, and although I did not earn a degree I took 2-3 classes a semester while working, and maintained a perfect 4.0 average.

I was determined to provide myself with a solid foundation so that I could break into the growing world of hi tech, but being over 30 years of age with no job experience turned out to be a significant drawback: I applied for literally scores of entry level jobs and was consistently turned down, most often without ever having opportunity to interview with anyone.

Nonetheless I persevered and finally in March of 1992 was able to land a job initially paying \$10/hour with a small startup software company, and over the next 3 years was able to grow within that outfit to where when I left I was the Senior Systems Engineer, and was the primary Technical Account Manager for many corporate customers which had site licenses for our e-mail package, including several large firms based in New York City, also Motorola and Ford Motor Company. It was the norm during that period to work 70-80 hour weeks, but I loved it: It was a period of tremendous personal growth for me, and coincided exactly with the emergence of the Internet as a public phenomenon.

In January of 1996 I joined another software startup located in Silicon Valley. As was common practice at that time as part of a standard compensation package in addition to a base salary I was issued a modest number of Incentive Stock Options (ISOs) which would vest over a 4 year period. This was a model which allowed employees to feel they had a stake in the company, and again I worked on average well above a standard 40 hours/week, doing my part to help make the company a success.

In May of 1998 the company was acquired by Cisco Systems, and my startup options converted to Cisco options numbering roughly 3,000 total. A drop in the bucket compared to what management was issued, but a very healthy number for a rank-and-file employee like me. And over the next two years the stock split 2-for-1 twice, and 3-for-2 once, for an effective 6X increase, bringing my ISO total to 18,000!

Due to the death of my sister after a long battle with cancer I decided in March of 2000 to leave Cisco and take some time off, stay close to home, and spend time with my mother, who was then 85. It just so happened that my leaving Cisco coincided precisely with the high water mark for the stock market, with the result being that the ISOs I had to "use or lose" within 90 days triggered a huge paper gain which ultimately resulted in over \$225,000 in AMT liability. Unfortunately by the time the tax came due in April of 2001 the value of the stock had dropped by roughly 80% from its high point a year earlier, with the result being my tax bill exceeded the value of the stock assets that triggered it!

I never sold any of the stock, never had any money whatsoever pass through my hands, never in any way benefited from owning the stock, yet I was about to be wiped out simply from exercising and holding on to what appeared to be an excel-

lent investment in a very good company with real products used by organizations of every kind worldwide!

I filed my year 2000 Federal return with an installment plan, but it was rejected due to the large amount of the tax liability. I called the IRS and attempted to expedite processing of my case, but was told I was "in the queue and would just have to wait to be contacted by someone in IRS Collections." For the next year while waiting for that contact on my own initiative as a sign of good faith I made monthly payments which ultimately totaled over \$67,000 toward my pending tax bill! Finally in late June 2002 I was contacted by a local Revenue Officer who was unwilling or unable to discuss anything other than collection of my assets, so I engaged a former IRS Collections Officer practicing as an "Enrolled Agent" and submitted an Offer In Compromise (OIC) in July 2002.

Cisco, Nortel and other large employers in the RTP area of North Carolina had not only stopped hiring, they had laid off thousands of workers, flooding the local job market with highly qualified job seekers. The tech job market had completely dried up, and not for lack of trying I had been unable to secure work. Save for a failed attempt to establish myself as an independent consultant which resulted in only a single paying job I remained largely unemployed for over 2 years and my tax bill (which had grown due to penalties and interest) exceeded my net worth by roughly 150%, yet my OIC was rejected at the field level due to an insistence that I could pay it off in total!

I was actually told in a letter from the IRS Offer Specialist handling my case that "Mr. Cole has the ability to pay the taxes outstanding in full and should withdraw his offer from consideration. . . . no offer amount is sufficient, and no offer would be accepted." The Asset/Equity and Income/Expense tables the Offer Specialist used to justify that claim contained several computational errors, but the most egregious was that my "ability to pay" was substantiated by the Offer Specialist counting my remaining Cisco stock asset both as a source of ongoing monthly income, (to the tune of over \$5,000/month), as well as a lump sum asset. In other words, the stock was counted twice, with ongoing income from it assumed after it was liquidated!!

My representative pointed out this flawed logic to the Offer Specialist, but to no avail: The OIC was rejected at the field level. I appealed, and after another 13 months the IRS Appeals office finally accepted my OIC, but only after adjusting it to a dollar amount that reflected my net worth at that time, with terms of 50% of the settlement amount to be paid within 30 days, another 25% within 120 days, and the final 25% within 240 days. I was able to make the first (50%) and second (25%) payments, but I have not been able to find more gainful employment, and at this point am unsure exactly how I'm going to make the final 25% payment, which is due mid August 2005.

I filed and paid all my state and federal taxes for the last ten years, and have no outstanding tax issues other than these problems associated with ISO transactions from the year 2000. I was finally able to find full time employment in August 2003, yet ironically back at Cisco, working in a group which has been outsourced to a vendor which pays less than 1/3 what I was making when I was previously a direct Cisco employee. I am grateful to have the job, yet the income barely pays my basic living expenses, and now on top of dealing with the final OIC payment I'm also trapped in a cycle of credit card debt, with high interest rates and monthly service charges. I have been trying to build on being back in the tech work-place and find more gainful employment, but to date have been unable to do so. I guess I'm one of the few lucky ones who have been able to secure an OIC settlement, but at this point it doesn't feel that way; I just don't know how I'm going to make ends meet going forward.

The payments I made proactively toward my year 2000 tax bill and the OIC settlement amount total up to about \$180,000. Ironically, I have an AMT Credit available which can offset regular income tax for years to come, yet the IRS would not consider that credit as an asset to be considered as part of an OIC settlement, and due to the relatively small yearly income I make now I can't take significant advantage of that credit. The one thing that could help me stay afloat would be to return some or all of that AMT credit sooner. I implore you to consider that avenue of relief.

Thank you for taking the time to consider my case, and of those in similar situations.

John Cole

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Richardson, Texas 75080  
August 31, 2005

Committee on Ways & Means  
U.S. House of Representatives  
1102 Longworth House Office Building  
Washington D.C. 20515

Dear Honorable Chairman Camp and Ranking Member McNulty:

We have submitted our story in the past and are hoping to garner your support and leadership for the Honorable Sam Johnson's bill 3385 on September 20, 2005 at the Committee for Ways and Means.

My husband, Jerry and I live in Richardson, Texas where Jerry owns and manages Canyon Creek Art & Frame. In April of 1999, I joined Avanex Corporation and accepted a lower salary in lieu of an Incentive Stock Option grant. I was unfamiliar with ISOs but it was explained to me that someday the company might go public and that the stock could potentially provide a small gain or contribute nicely to a retirement fund.

The company went public in February of 2000, and like many companies in that same year, did surprisingly well. It was scary and exhilarating all at the same time. The company advised their employees to talk to a financial advisor regarding long-term capital gains, short-term capital gains and AMT. We consulted a tax accountant, who told us we needed to be concerned about the capital gains, but that AMT was only for the very wealthy and we did not qualify. The tax accountant explained that we should buy what we could and hold it to protect against short-term capital gains. Later that year a coworker mentioned the need to check out the AMT situation and again we inquired with our tax advisor and again he assured us that we had nothing to worry about.

We soon discovered that he was incorrect and we were truly uninformed about AMT. When we finally discovered the problem, it was too late to sell as the stock-trading window had closed and before the next open window arrived, the stock had plummeted. Our tax bill came to \$92,000, more than double my starting annual income, and in order to pay the bill, we were worried we might have to take out a second mortgage and may lose our business. Fortunately, for our financial future, during the next open window, we were able to sell all our stock and pay most of the bill. By depleting our savings, we were able to pay the remaining balance. Now, with no savings and the hope of a small retirement fund from our ISO grant gone, we are starting over with retirement planning.

We are outraged that the government saw fit to apply a tax to phantom money! We are outraged that we now have NO savings and NO retirement!

I respectfully and urgently request your support of H.R. 3385.

Barbara Cornelius

Alameda, California 94052  
August 31, 2005

Committee on Ways & Means  
U.S. House of Representatives  
1102 Longworth House Office Building  
Washington D.C. 20515

Dear Committee on Ways & Means:

My name is Eric Delore and I am writing on behalf of myself and my family to ask for your active support and co-sponsorship of H.R. 3385. I have a huge Alternative Minimum Tax (AMT) tax debt incurred on "phantom" gains due to the application of the Alternative Minimum Tax to incentive stock options (ISOs). I owe \$420,000 of AMT on under \$5,000 of actual income derived from the sale of frightfully deflated Incentive Stock Options (ISOs). I am not wealthy. I am a middle-classed citizen struggling to raise a family on a single income.

I have already paid the IRS \$40,000+ of taxes, but they want more. They want everything. One collection agent suggested that I sell my home and give them all the proceeds. Bear in mind that by raiding various immediate and extended family bank accounts, I have already paid the California State Franchise Tax Board



\$100,000 of AMT tax on this same \$5,000 of income. That more than \$140,000 of taxes paid to date.

Again, I would like to ask for your active support and co-sponsorship of H.R. 3385. This important legislation was recently introduced by Reps. Johnson (TX), Neal, McCrery, Jefferson, Ramstad, Lofgren, Shaw, Honda and Johnson (CT), to provide relief for taxpayers subjected to unfair and unjust tax treatment due to the AMT treatment ISOs. In addition to unfairly affecting me, this serious problem has impacted many employees of small and large companies across America, often resulting in taxes up to and exceeding 300 percent of these employees' annual salaries. Workers are being forced to pay tens of thousands, hundreds of thousands, and even millions of dollars in tax overpayments on income they will never receive.

Please join the groundswell of support for remedying this serious injustice through this ISO AMT legislation. This bi-partisan effort is building support in Congress, the Press, Corporate America, the Taxpayer Advocate's office. Grassroots organizations like the ReformAMT, [www.reformamt.org](http://www.reformamt.org), and the Coalition for Tax Fairness, [www.fair-iso.org](http://www.fair-iso.org), are actively supporting this important legislation, and may be contacting your office to secure your support.

I thank you for your leadership on this effort, as your support is critical to restoring a fair and just tax system for all Americans—including hard-working, entrepreneurial Americans. Please do not hesitate to contact me if you have any questions.

Eric Delore

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#### Statement of the Doherty Family, Chantilly, Virginia

Mr. Chairman and Members of the Committee: My name is Nina Doherty and I would like to first thank you for the opportunity to speak with you today.

I am a married working mother of three living in a modest Northern Virginia suburb with my husband of 17 years. Today, I work full time for a small software company. I am sharing my story with you in the hope that it will shed light on how the Alternative Minimum Tax treatment of Incentive Stock Options can have a devastating impact on average hard-working people like me.

In 1994, I became the first employee of a small start-up Telecommunications Company. Part of my compensation included Incentive Stock Options. Seven years later, I found out to my huge shock that there could be an egregious impact from exercising Stock Options due to unintended consequences of the Alternative Minimum Tax.

Back in March 2000, before I learned about the Alternative Minimum Tax, I exercised some stock options and it appeared that all my hard work and sacrifice in working for a start-up would pay off. My company was going public as many did at that time, and it was everyone's expectation that the stock value would remain stable and perhaps even grow. Unfortunately, shortly thereafter, the stock market tumbled and my "paper" stock value was reduced to nothing. Despite the dwindling stock value, I never thought to sell them even after my restrictions lapsed in September 2000. I continued to hold onto my stock because I was told by my financial advisor before I ever exercised any options that due to the way the law was written with regard to capital gains tax penalties, it was more beneficial for me to hold it for more than one year.

In April of 2001, while on a Girl Scout trip with one of my daughters, I got a call from my accountant about the taxes he had just prepared. He told me that because of the Alternative Minimum Tax, I owed a lot of money, but he didn't want to tell me how much until I got back into town. Alarmed, I asked him to tell me right there and then—and that is how I found out that I owed tax equal to 100% of our annual family income! I was dumbfounded, and quite frankly, so was my accountant. Now my family is facing potential financial ruin as a result of this massive penalty.

Unfortunately, the highly complex nature of the Alternative Minimum Tax code befuddled both my highly trained financial advisor and my accountant, a situation affecting family after family across this country.

And it wasn't just complicated code that led me to hold onto the stock. The spirit and intent behind the *incentive* in an Incentive Stock Option is that employees like me are encouraged by law to hold onto our stocks for a longer period of time, to help our companies grow by investing in the future. Certainly, the intent was NEVER to hurt the very people that contributed to a company's success. Despite this, countless families are facing financial ruin due to the ISO AMT issue—mine is not a unique story.

The big problem with paying the AMT is that the tax payment is simply a prepayment of tax. When this law was written in the sixties, the volatility of the stock market was not anticipated by Congress and there was no evidence at that time that prepaying this tax would create hardship. Unfortunately, many families like mine cannot afford to prepay this tax. Because there was no actual gain for victims like me, this tax will generate a useless tax "credit," meaning that our prepayment of this tax is nothing more than an interest-free loan to the government. By today's law, we can only recover the tax prepayment in credits at \$3,000 per year, which for our family means 30+ years—for many people the credit will well exceed their life expectancy.

Recently, the IRS levied our bank accounts, seizing \$30,000 that my husband had in savings from a loan against his 401(k). This money was needed to do repairs on our ten year old home and replace our failing minivan. Next we received official notice that there was a Federal lien filed by the IRS on any and all property that we own. With this and the past three years of worry about this problem, there has been terrible strain on my family and my marriage. Every day this issue is like a dark cloud over our heads and we wonder if we should just declare bankruptcy.

My family and I respectfully urge those of you on the Committee to take immediate action on correcting this injustice, through a repeal of the AMT/ISO provision, or through targeted and principled measures that will help those of us currently facing this problem, and also prevent similar results from occurring in the future. For many families like mine, time has run out: the IRS is enforcing the strict letter of the law—threatening to take our homes and retirement funds to collect the money despite the fact that we never had any actual gain.

Please don't allow this injustice to continue. Taxpayers deserve fair treatment in connection with simpler rules, and we appreciate your current consideration of a solution that is fair and just.

Again, thank you for your time.

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#### **Statement of Rol Donie, Houston, Texas**

Job loss in America has become a major problem. Our jobs keep flowing offshore. American workers are showing up on the dole instead of showing up for work. One of the biggest reasons for fewer jobs is the way we collect taxes. The income tax system drives away existing jobs and limits the creation of new jobs to boot.

A better plan is the FairTax. The FairTax (H.R. 25/S. 25) implements a National Retail Sales Tax to replace the income tax. The amount of taxes collected will remain the same. Government will receive the same amount of funding it receives now. The big difference is that the FairTax lets us fund government without losing jobs in the process.

##### **The FairTax Plan**

- Lets businesses spend the billions now spent annually on tax compliance on job growth instead.
- Lets businesses create new jobs based on good business planning instead of tax planning.
- Lets businesses redirect the hundreds of millions now spent on tax lobbyists into creating productive jobs instead.
- Lets businesses spend all the money they now pay as matching Social Security contributions on expanding their workforce.
- Lets businesses compete in the global marketplace on a more level playing field. Prices for American products will no longer include all the embedded expense incurred with the income tax. Demand for cheaper American products will soar. Job growth for Americans will soar.

Americans that want their job back, Americans looking for their first job and Americans concerned about the way our jobs are going can find more information at [www.fairtax.org](http://www.fairtax.org).

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#### **Submission of Charles Emery, Aiken, South Carolina**

Ladies and Gentlemen of the Panel,

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of the biggest reasons for fewer jobs is the way we collect taxes. The income tax system drives away existing jobs and limits the creation of new jobs to boot.

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Americans that want their job back, Americans looking for their first job and Americans concerned about the way our jobs are going can find more information at [www.fairtax.org](http://www.fairtax.org).

Please consider the FairTax for the sake of American jobs as well as a host of other reasons for this change in the way federal taxes are collected. Thank you for your time and consideration.

Chandler, Arizona 85226  
*August 31, 2005*

Dear Honorable Chairman and Members of the Ways and Means Committee

I wish to bring to your attention the story of ISO and AMT and how it impacts me and many Americans who have been affected by AMT tax laws.

ISO stocks were granted as an incentive to employees to reward them for good performance and long term retention. Favorable tax rate was one of the key elements of ISO stocks. It was recommended that ISO stocks be held for at least one year after exercise so that they do not become "disqualified disposition."

While this strategy worked for upward moving markets where stocks appreciated in value, no one (including the proponents of the ISO/AMT tax codes) ever fully comprehended the unprecedented financial havoc this may cause in case of drastically decreasing stock market and market that is depressed for a long time.

The AMT rules pertaining to ISO stocks do the following.

- Calculate paper profit based on exercise price and option price.
- Recognize the paper profit as income in a parallel calculation under AMT rules.
- Adjust income with some other incomes, refund etc.
- Levy tax based on AMT income (more than real income), which includes paper profit.
- The difference between regular tax and AMT tax is imposed as additional AMT tax.
- When the ISO stocks are sold later (after the hold period), part of the advanced AMT tax can be recouped.

Please note that in a rapidly declining and continuously depressed market, the AMT tax cannot be fully recouped as the exercised stocks will always be below the exercise price. By selling the exercised stocks, the individual will further incur regular capital gain, and accumulate AMT Capital Loss.

This results in paying tax once (AMT tax) for exercising the ISO and, taxed again due to regular Capital gain by selling the stocks (albeit at lower than exercise price). Opportunity to recoup the AMT taxes is very slim in the current environment, and we will not probably be able to recoup it in our lifetime.

I personally paid (forced to pay) AMT taxes in hundreds of thousands of dollars, and in the process was burdened with huge loans. I humbly request the intervention by Congress to relieve us from the loan burden, and return us the advanced taxes we paid in the form of AMT taxes. The advanced AMT taxes are rightfully ours,

which we can never get back unless Congress makes sweeping changes in the ISO/AMT tax rules.

I am a strong believer of paying our fair share of taxes for the benefit of the society, but it is utterly unfair to pay taxes based on fictitious profit and not be able to get it back.

I urge you to support the Tax Reform proposal by Honorable Sam Johnson's H.R. 3385. I respectfully and urgently request your support of H.R. 3385.

Mohammad Faruque

Cary, North Carolina 27511  
August 31, 2005

To House Ways and Means Committee

Dear Honorable Chairman Camp and Ranking Member McNulty:

I have submitted my testimony and shared my story at these following events:

- 6/15/2004, Hearing on Tax Simplification, Oversight Subcommittee
- 6/23/2004, Hearing on Select Tax Issues, Select Revenue Measures Subcommittee
- 6/08/2005, Hearing on Tax Reform, Full Committee
- April/May 2005, Senate Finance Committee Chairman Grassley
- Spring/Summer 2005, President's Tax Reform Advisory Panel

I now wish to share my story directly with you. I hope this Committee will extend the relief H.R. 3385 offers people that executed Incentive Stock Options (ISO) in years 1999, 2000, and 2001 to people that executed NonQualified (NQ) stock options in those same years. H.R. 3385 will not help my situation, because H.R. 3385 requires a person to have "AMT credit." I have no AMT credit, since my stock options were NQ, but I suffer the same detrimental effects of executing stock options in year 2000.

I am in a very bad situation because of the tax liabilities that were generated in year 2000. Because of the economic downturn of the telecommunication industry, I was laid off from Cisco in March of 2000. This situation forced me to execute the NonQualified (NQ) stock options I had accumulated over the 5+ years I had worked at Cisco, or lose them forever.

I did not know that the single act of executing NQ stock options becomes a taxable event in the eyes of the IRS. I did not sell stock; I did not receive any cash; I did not realize any gain whatsoever in the transaction—not a single dime! I only executed the option to buy Cisco stock at a price offered to me when I was hired.

Because of the complexity of the tax laws, I paid a CPA \$900 to prepare my taxes and tell me I owed \$1.7 million in taxes for the year 2000 even though I make less than \$100,000 a year! How can this be? The CPA office that prepared my taxes commented to me:

"This is the most unfair and unfortunate tax return our office has ever prepared. Many officers have verified the accuracy of your return and we believe it to be correct."

I was a habitual saver and lived a very meager lifestyle. At the time I executed the NQ stock options, I lived in a 1,400 sq. ft. house with my wife, a dog and a cat. I drove a 1979 F100 pickup, no air, manual steering, 3 speed on the column, 160,000 miles—worth about \$600. My wife drove a 1987 Olds Cutlass with 224,000 miles. I did not live the life of our executives—I was just an engineer trying to save for a brighter future.

The Cisco stock that I bought declined more than 80% in 2000 and 2001. I sold everything and took out multiple loans to pay the IRS. Because of my prior savings, my meager lifestyle, and the kindness of my bank; the IRS received the money April of 2001. My bank has given me two interest only loans. Today I live in a 60 X 14 trailer by myself. My wife and I divorced in 2004. I still drive the same Ford pickup (over 270,000 miles now). 70% of my salary goes to maintaining these loans, which I have been paying for over 4 years now.

This unfortunate situation has taken my financial future from me. I am addressing this letter to you so that you may know how this stealth tax is destroying the

lives of so many common people, like me. It is just plain wrong to tax people of all their assets when they have realized no financial gain whatsoever.

Kevin R. Frank

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**Statement of Scott Frisoli, Chicago, Illinois**

In 2000, I exercised stock options with the company I work for, PurchasePro.com. As the stock market continued to fall, I was forced to sell my stock well below the price I paid for them to pay my 2000 AMT bill. I paid my 2000 AMT taxes in the amount of \$286,000 after getting nothing back from the sale of my stock. I was married in December of 2000 and our family has been set back a great deal financially. I had to sell many of my assets and borrow a large amount against my house. We are way too young to have financial problems for the rest of our lives. The way current tax code is written it will take 43 years before I get all of my money back without interest! I am now stuck holding onto thousand of shares of a company that is out of business with NO HOPE of recouping my money.

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Madison, Wisconsin 53703  
August 26, 2005

Dear Honorable Chairman Camp and Ranking Member McNulty:

I am writing to ask for your support and would appreciate your taking a moment to read this. I have submitted my testimony and shared my story for previous hearings regarding this issue. I now wish to share my story directly with you in hopes of garnering your support and leadership of the Honorable Sam Johnson's H.R. 3385.

I'm currently 43 years old and have worked very hard for 9 years for a start-up Internet Service Provider that was successful. In 1999 I left the company to move back to Wisconsin to be with family and raise my own family. When I left the company I was required to exercise my stock options (WorldCom stock).

Doing so caused us to incur an AMT liability well in excess of \$1 million, which we paid in April 2000. It's now well known that the WorldCom stock lost virtually all its value. Our AMT tax payment is now a credit (amounting to an interest-free loan to the government) that we can never effectively use because the ways in which we can draw it down are too restricted. In essence, we've lost almost all of our investment money simply to create a tax credit in our IRS account. It is fundamentally unfair to have been forced to pay a large AMT bill on a phantom gain rather than an actual gain.

Along with many of my co-workers and friends, I now find myself in this situation, many others are much worse off. Several of us had to declare bankruptcy and others are forced to sell or liquidate assets (including college funds, savings, cars, 401k/IRA pension plans, homes, etc.) or to refinance homes to help pay the taxes. In our case, we had to liquidate our life savings and obtain a loan secured by my in-law's assets to pay our tax bill, we're now deferring college and retirement savings as we pay back this loan with its interest—all while we have \$1 million tax credit. We're hard-working, honest taxpayers who are incurring financial difficulties due to the unintended consequences of the AMT laws.

To summarize, it's fundamentally unfair that we have provided the government a substantial (over 1 million dollars) interest free loan that will never be repaid while we're having to pay off a loan with interest and defer college and retirement savings. Further aggravating the unfair situation, the complexities of the AMT law require us, an average middle-class family, to pay premium accounting fees to navigate the complexities of our tax situation.

I respectfully and urgently request your support of H.R. 3385.

Shari Galitzer

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**Statement of Sunil Ganu, Santa Clara, California**

My life is changed because of the alternative minimum tax (AMT). I am suffering from acute panic disorder and stress. If my age is X, I look like X+10 years, thanks

to this AMT. Moreover, people think either I was either greedy or stupid. I never did anything wrong in my life to have all this trouble. My credit scores are 758+. I always paid my credit card balances and loan amounts on time. I followed the advice of my advisors at Morgan Stanley. They advised me not to sell the stock I purchased through the exercise of incentive stock options (ISOs) earlier—but there is no point in blaming anybody now. It's my mistake and it seems nobody can save me now. I have already paid more than \$150,000 in AMT from the tangible assets I had and owe substantially more. My AMT credits will exceed \$400K, which I will only be able to claim at a rate of \$3,000 per year for the rest of my life or 133 years.

I exercised (bought) 15,000 ISO shares. I couldn't sell most of them before the company (Exodus Communications) filed for chapter 11, as I hadn't owned the shares for at least one year. Initially I paid \$110K in AMT by selling some of the stocks at \$15.00 per share in 2001, remember now, I was taxed as if I sold them for \$76 a share! I didn't realize that my company would be bankrupt soon. I still owe \$150K plus penalties. The IRS has kept all my refunds—worth about \$45K in the last 3 years—but penalties keep accruing.

I have tried to negotiate with the IRS but we are rejected on every offer I made. My first OIC was turned down in 2002. I have appealed to the IRS again and increased the amount of my OIC. That too was turned down in April 2003. The IRS evaluation process is faulty. They are looking for all the money available in my 401(k) plan apart from whatever assets assessments are done based upon my car, credit cards statements etc. Though I don't have any bank balances, the IRS already put a lien on my Condo and basically I will be in a debt trap if I borrow from my credit card to pay off IRS as the interest rates are so high. The important point is that the IRS is seeking all this money for income I never realized. What a nightmare! Meanwhile I got laid off in August 2003. Luckily I got a job in another company with a lower salary in 3 months. The trauma I went through during that time is unimaginable.

Please do what is necessary to reform the draconian provisions of the law. Morally I don't believe I owe anything to the IRS but then legally and financially I have a sword hanging over my head.

Aloha, Oregon 97007  
August 31, 2005

Dear Honorable Chairman Camp and Ranking Member McNulty:

I have submitted my testimony and shared my story at these following events:  
Ways and Means Committee Hearings:

- 6-15-2004, Hearing on Tax Simplification, Oversight Subcommittee
- 9-23-2004, Hearing on Select Tax Issues, Select Revenue Measures Subcommittee
- 6-08-2005, Hearing on Tax Reform, Full Committee
- April/May 2005, Senate Finance Committee Chairman Grassley
- Spring/Summer 2005, President's Tax Reform Advisory Panel

We now wish to share our story directly with you in hopes of garnering your support and leadership of the Honorable Sam Johnson's H.R. 3385.

We are Liles and Naomi Garcia and we are homeowners. Liles was in the Air Force for four years, and has worked for three high-technology companies for a total of thirty years. Naomi has worked for a high-technology company, Tektronix, Inc., for thirty-two years.

When Liles was working for PMC-Sierra, Inc., the company gave him some stock options which often occurs in high technology companies. At the end of September 1999, PMC-Sierra laid off some employees and Liles was terminated at this layoff. There was no warning of the PMC-Sierra layoff; it was a complete surprise. Because of the layoff termination, Liles had to purchase his stock options within a short period of time or else lose them.

At that time the stocks were worth about \$965,000.00, and when Liles purchased his stock, we unknowingly incurred a \$273,000 Alternative Minimum Tax. We have been doing our own income taxes for many years, and did not know what the AMT was.

We submitted an Offer-in-Compromise to the IRS in July 2001. The IRS rejected our OIC and an OIC Appeals Officer told us that he would only settle for the entire amount. This decision devastated both of us because of the large amount that we will be required to pay. We are currently making monthly payments to the IRS, but we still owe more money than we will ever be able to pay. The IRS can take every-

thing that we have through their collection process. To us, this does not seem right. Many thanks for any help that your Committee can give us. We respectfully and urgently request your support of H.R. 3385.

Liles and Naomi Garcia

Southbury, Connecticut 06488  
September 1, 2005

Dear Chairman Camp and Ranking Member McNulty:

I have submitted my testimony and shared my story at the following events: Spring/Summer 2005, President's Tax Reform Advisory Panel and the 6/08/2005 Hearing on Tax Reform, Full Committee. As a resident of the 5th Congressional District, I now wish to share my story directly with you in hopes of garnering your support and leadership of the Honorable Sam Johnson's H.R. 3385.

As a 64 year old retired taxpayer the current alternative minimum tax is of great concern. Each year more and more Americans fall prey to this unfair tax. Approximately five years ago, because of the ISO AMT provision, I incurred a huge federal and state tax bill, which I paid. The year following my huge tax overpayment my accountant informed me that I would have to live another 60 years to recoup my AMT credit. This was hard for me to believe! Five years have since passed and I have reduced my AMT credit by about 8%. At age 64, I do not believe that I will last another 60 years. The Federal Government continues to hold my money without paying me one penny of interest. Once I leave this earth my AMT tax credit will become property of U.S. Treasury coffers. The credit will not be passed on to my heirs. Does this seem fair?

One thing that I do know is that my federal tax credit will follow me no matter where I reside in the United States. This is not true on the state side. If I move out of Connecticut I lose my ability to recoup my state AMT tax credit. This foolish law that was intended to prevent wealthy individuals from escaping federal income tax has become a burden to the all classes of taxpayers.

I respectfully and urgently request your support of H.R. 3385.

Leonard P. Garille

Paso Robles, California 93446  
August 30, 2005

Dear Honorable Chairman Camp and Ranking Member McNulty:

I have submitted my testimony and shared my story with the President's Advisory Panel On Tax Reform on April 29th, 2005.

I now wish to share my story directly with you in hopes of garnering your support and leadership of the Honorable Sam Johnson's H.R. 3385.

The following describes the devastating effect the AMT has had and is still having on my wife and I.

My wife received stock options from her company as part of her compensation for all her hard work. Throughout the year in 2000, we saved money and used it to exercise the options. We considered the tax implications of selling or holding. We were advised and agreed to follow the strong tax incentives Congress put in place for ISOs to hold on to the stock for long term capital gain and support her company, rather than selling immediately and paying approximately \$50,000 more in short term taxes. We believed strongly and still do in our company, and in the market for the long term, looking to accumulate stock and other assets for our future and for our eventual retirement.

In 2001, the market's steep decline reduced the value of our stock by over 90%. To make matters worse, we received a tax bill from the IRS and the California Franchise Tax Bureau (FTB) for a combined amount of close to \$150,000. **This was over 5 times the amount we realized from our stock holdings.** We had never heard of the AMT, nor could we have ever imagined we would have to pay taxes on stock GAINS WE NEVER REALIZED.

Our situation grew steadily worse, I lost my job, our savings were dwindling quickly, and we started getting calls from IRS and FTB collection agents demanding that we pay the taxes due. We could barely pay our bills much less pay \$150,000

in cash to the IRS and the State of California. The IRS had suggested an installment agreement, but the \$3,800 a month they required was far beyond anything we could afford. We were also warned that if we accepted the agreement and missed or were late on a single payment, the full amount would be due immediately and collection actions would be taken, i.e. seizing of assets and property.

The IRS knew we never made the money on the stocks for which we were being taxed, but that didn't matter to them. They were aware I had been unemployed for 18 months, and they didn't care. They said I had the potential to earn, which in their mind is the same as cash.

Meanwhile, we tried to refinance our home to lower our payments so we could have additional money to pay bills, but the IRS had placed a lien on our property and we were denied the opportunity to take advantage of the lowest interest rates in history. The IRS refused to lift the lien, even temporarily, to allow us to refinance.

We were forced to hire tax attorneys and CPA's to help us with our predicament, all to no avail. We submitted an Offer In Compromise. We were rejected, the IRS claimed we had the ability to pay, even though I had been unemployed for over a year and a half and had been dipping into my home equity line of credit just to survive and pay our bills. For over three years we lived in constant fear of losing our home, our car, our bank accounts, everything. All the while dealing with harassing calls from the IRS and the FTB. My wife was afraid we'd be sent to prison for not paying the taxes. She had heard so many horror stories of what the IRS does to people who don't pay their taxes.

Having been an independent contractor for many years and using credit cards to pay for travel and business expenses, I had established a fairly high credit limit. The IRS told me that I had access to credit so PAY UP. I was forced into an installment agreement to keep from losing our home (the IRS had placed a lien on it). The IRS demanded \$50,000 in cash and monthly payments of \$730 per month to pay off the remaining \$74,000. I was forced into putting it on my credit card. Since the IRS compounds interest daily, we will never be able to pay off the balance in our lifetime. Prior to that, we had been forced into an installment agreement with the FTB, paying \$700 per month. There was no way we could pay both monthly payments, equaling over \$1,400 per month (remember, I had been unemployed for 18 months), so we were forced into paying the remaining \$18,000 balance due the FTB with my credit card to eliminate at least one of the monthly payments.

I was unable to keep up with the credit card payments on an outstanding balance of close to \$70,000. Now, I am several months behind on credit card payments. The credit card companies and collection agencies are now making threatening calls daily. I'm now getting letters from attorneys on behalf of the credit card companies. My credit rating, which was perfect all my life, is now ruined. This nightmare just keeps going on and on . . .

I'm 51 years old and I should be turning my thoughts toward retirement and a comfortable future. My own government has dashed these hopes and dreams forever. We are being punished in the worst way possible, and our crime? Our crime was working hard and being honest. I always felt that these were the values that America embraced. Study hard, get a good education, get a good job, work hard, be honest and be rewarded. Unless relief comes quickly, I will have been sadly mistaken.

This law needs to be changed immediately to help the thousands of people who are in the same predicament as my wife and I. We hope that you will understand that there are some very good people who have been caught in the AMT nightmare and are facing financial ruin for the rest of their lives. Please show your leadership and do what you can to change this law.

I respectfully and urgently request your support of H.R. 3385.

Mark Garner

Redwood City, California 94065  
August 25, 2005

Dear Honorable Chairman Camp and Ranking Member McNulty:

I have submitted my testimony and shared my story at these following events:

- 6-15-2004, Hearing on Tax Simplification, Oversight Subcommittee
- 9-23-2004, Hearing on Select Tax Issues, Select Revenue Measures Subcommittee



- 6-08-2005, Hearing on Tax Reform, Full Committee
- April/May 2005, Senate Finance Committee Chairman Grassley
- Spring/Summer 2005, President's Tax Reform Advisory Panel

I now wish to share my story directly with you in hopes of garnering your support and leadership of the Honorable Sam Johnson's **H.R. 3385**.

My name is Hisham Ghazouli and I am writing on behalf of my wife Irma, and our two children. We appreciate the opportunity to discuss the hardships we are suffering due to an outdated and complicated portion of the tax code called the Alternative Minimum Tax.

In July 1998, I went to work for a startup in Redwood City, Ca. In exchange for a lower paying job, I was granted 60,000 shares of incentive stock options. I worked very hard helping the company develop its product and grow. In Feb of 2000, the company went public and the stock quickly climbed to \$100. I could not exercise my options at the time because I was blocked from doing so. Approximately 6 months later, when the stock was trading around \$20, I decided to exercise my options and hold the stock for 18 months. By the end of the year the stock was trading at \$1.00 a share. I didn't know that exercising the stock options would trigger AMT, which taxes you on the day of exercise even though incentive stock options are not supposed to be taxed until sale. After filling out our tax returns, we realized that we had a \$33,000 AMT Federal tax bill and a \$6,000 state AMT tax bill. I was forced to pay taxes on stock options as if they were trading at \$20 a share regardless of the reality that the stock was trading at less than \$1 a share.

We had to liquidate all of our savings to pay for the AMT bill. That year we paid over \$65,000 in Federal taxes on income of \$100,000, which I am sure is an unintended consequence of the tax law. As of tax year 2003, I have received less than 10% of the AMT money I loaned the government in 2000. It will take another 5-10 years to fully recover the amount.

I don't believe that the law was intended to so severely tax hard-working and honest middle class Americans. Please fix the law so that we don't have to pay taxes on income we don't receive, and we can access the "credits" in a more timely manner.

I respectfully and urgently request your support of H.R. 3385.

Hisham Ghazouli

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#### **Statement of the Gorokhov Family, Germantown, Maryland**

Members of the Committee: My name is Mark Gorokhov and I am writing on behalf of my wife Nadezhda Gorokhova and our family. We appreciate the opportunity to discuss problems we faced due to an outdated and not fair portion of the tax code called Alternative Minimum Tax.

In August of 1998 I took a job as a software engineer at Celera Genomics. The offer letter stated that I was granted a stock option (ISO). The essence of employee stock options involves employees sharing in the future growth and success of a company by receiving financial rewards based on future increases in stock price. In 2000 I exercised my Incentive Stock Option. In plain English this means that I bought my company stock at discounted rate \$8.56 while its market value was in \$70-\$100 range. When I exercised my ISO I did not have any monetary gain because I did not sell my stocks. However, the tax law required us paying huge AMT tax on this phantom gain. This had dramatic impact on our family. The total tax we had to pay significantly exceeded our entire family taxable income we reported on form 1040 for the year 2000. The effective tax rate was 130%.

The deadline to pay this huge sum to IRS was April 15, 2001. By that time stock price plunged and we could not pay our tax even if we sell all stocks we acquired. We borrowed all available money from my wife's and my retirement investments, from 2nd mortgage and credit cards. Also, we emptied all our assets on bank accounts. In year 2004 we are still paying loans we made to pay tax year 2000.

The tax we paid for exercised ISO stocks is a prepayment of tax with a corresponding Minimum Tax Credit that applies against capital gains tax when we sell stocks. Now when the stock price drops we do not have an efficient way to recover the leftover excess pre-payment of tax. Thus we gave the Federal Government an interest free loan in the sum, which is over \$100,000.

In 2001 tax return we recovered \$2,433 from our AMT tax carry forward. At this pace it would take 51 years to recover the whole sum.

In 2002 tax rate was lowered, but AMT rate stayed the same. In 2002 tax return we recovered \$820 from our AMT tax carryforward. At this pace it would take 149 years to recover the whole sum.

In 2003 and 2004 tax rate was lowered again, but AMT rate stayed the same. In 2003 and 2004 tax return we recovered \$0 from our AMT tax carryforward. At this pace we NEVER recover the whole sum of credit we gave to a government.

We ask your help to change the outdated AMT tax law and help us to recover the AMT tax we paid in year 2000.

Allen, Texas 75013  
August 31, 2005

Dear Honorable Chairman Camp and Ranking Member McNulty:

I have submitted my testimony and shared my story at these following events June 2004.

I now wish to share my story directly with you in hopes of garnering your support and leadership of the Honorable Sam Johnson's H.R. 3385. I live in his district. This is my previous statement:

I do telecommunications development for Cisco Systems. No one would likely call me financially rich, but I am a very blessed man with a wife and 2 adopted daughters.

I have ISOs from Cisco that I could exercise and, according to one part of the tax code, I should receive preferential tax treatment if I hold the stock for at least a year. Truth be told, I think the smarter investment would be to buy the stock and hold it for at least 10 years.

However, with the present ISO AMT laws and with fluctuations in telecommunication stock prices, I can not make such smart investment choices (buy Cisco and hold for 10 years) because the stock price may go down temporarily, and I would owe more in taxes than the stock is worth. It doesn't make sense that on the one hand the tax law would encourage my long term investment (which, under normal circumstances would be a wise strategy for me, my employer and the economy), but on the other hand the tax law so heavily discourages such long term investment by mandating taxpayers risk losing more than their investment to acquire the stock.

Please bring sense to these laws. Thank you.

Duane Guthrie

### Statement of Angela Hartley, San Diego, California

Dear Congressmen:

I have submitted my testimony and shared my story at several Congressional hearings, including written testimony for April 17, 2005 hearing. I will share my story again in support of the Honorable Sam Johnson's H.R. 3385—it is my last hope for financial survival. Please support this bill.

In 2000, few people were even aware of the AMT, and even fewer understood it, including many tax professionals and even some IRS agents. When I exercised Incentive Stock Options in 2000, I followed the standard recommendation of holding that stock for one full year to achieve the capital gains treatment for which Incentive Stock Options had originally been designed. Imagine my surprise when I discovered that there was a parallel universe called the AMT, where the rules were opposite of common sense and regular IRS rules, and instead of benefiting from long term capital gains treatment like an ordinary stockholder, I was penalized for NOT selling my stock.

As a result, my effective tax rate for 2000 was almost 250% and left me with state and federal tax obligations well over \$300,000. This was impossible to pay because it was many times my annual income and the stock had dropped to a fraction of its former value. Although I have made payments against the debt, it grows too rapidly to ever pay off.

The irony is that the AMT also allows a credit back to me that would offset this liability—but there is a cap on the amount of credit I can recover each year—it will take over 90 years for me to gain the entire credit back, and unlike *my* AMT liability to the government, I receive no interest on the money owed back to me by the government. So my debt grows by leaps and bounds and the government holds my money interest-free indefinitely.

I have offered all the equity in my 1,500 square foot home, my car, my life savings, and my retirement to settle this—everything I have managed to put aside over my entire working life to pay arbitrary and excessive taxes on profits I did not receive (by the way, the IRS refused this offer as insufficient). Actually, after paying over \$100,000 so far, I have only about \$11,000 left out of my savings/retirement and the IRS has a lien on my house, which also serves to ruin my credit. I am 52 years old and have been a compliant taxpayer since I earned my first dollar, paying in full and on time, without complaint, but I fail to see how bringing an honest middle-class taxpayer to financial ruin serves any purpose.

Legislation is being introduced that would allow me to pay the proper percentage of whatever gains were actually realized from the stock sale. While I realize the entire AMT needs to be addressed, the first logical step would be to support relief for those who have suffered the most unfair and egregious effects of this outdated law. Please stop the unnecessary financial crippling of some of your most hard-working and productive citizens. We can't wait two or three more years—we are losing our homes, our retirement, and our entire economic futures today!! There is no way a "fix" several years from now will ever allow us to recover.

The AMT no longer serves its intended purpose, if it ever did, and is increasingly punishing hard-working families. We respectfully ask that each of you understand the enormous risk involved in ignoring this growing malignancy in our tax system, and take action now.

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La Cañada Flintridge, California 91011  
August 31, 2005

I am writing to beg you to change the tax code so that stories such as mine never happen again. You can help do so by approving ISO AMT Bill H.R. 3385.

When eToys was started in 1997, its founders quickly realized that it would be difficult to know their market if everyone that worked for them was a childless, young male. So it wasn't surprising that they hired me as their 5th employee, a mid-thirties suburban mother with experience in marketing and website design. I only worked part-time, however, as I wanted to spend time with my young children. When the company was low on cash, they offered to give me part of my compensation in stock options. I didn't know anything about stock options, but accepted, knowing that whatever happened, I was there primarily because I really enjoyed my job.

The company went public in May 1999, but because of a lockout period and a blackout period, we weren't able to sell any of our stock until February 2000. In the meantime, I exercised as many shares as I could, sometimes when the stock was trading as high as \$68. I had also become a full-time employee, because the company decided it didn't want part-timers anymore.

Unfortunately, by February 2000 I needed to sell my stock just to pay my tax bill. Even though my income for 1999 had been \$85,500, I had to pay an Alternative Minimum Tax of \$424,100 because I was taxed as if I'd had income as high as the price the stock was selling for each day I exercised my options.

Thankfully, the company's stock hadn't been de-listed yet, so I was able to sell my shares to pay my tax bill. I've been trying to get this money back from the IRS, so far to no avail.

I implore you to do what you can to reform our nation's tax code so that this doesn't happen to anyone else. Taxation without income is wrong. Thankfully, so is taxation without representation, and I'm relying upon my representatives to do the right thing. Please vote "yes" on ISO AMT Bill H.R. 3385.

Kathryn C. Hernandez

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New York, New York 10024  
August 29, 2005

Dear Honorable Chairman Camp and Ranking Member McNulty:

I am writing to respectfully request your support of H.R. 3385, otherwise known as the AMT Credit Fairness Act of 2005." I have submitted my testimony and shared my story at the following events:

- Hearing on Tax Simplification, Oversight Subcommittee (6–15–2004)
- Hearing on Select Tax Issues, Select Revenue Measures Subcommittee (9–23–2004)
- Hearing on Tax Reform, Full Committee (6–08–2005)
- Senate Finance Committee Chairman Grassley (April/May 2005)
- President’s Tax Reform Advisory Panel (Spring/Summer 2005)

I wish to share my story in brief with you in hopes of garnering your support and leadership of the Honorable Sam Johnson’s H.R. 3385:

“I am yet another unsuspecting victim of the Alternative Minimum Tax. Due to a stock options exercise in 2000, I’m being taxed over \$1.2 million on stock that yielded actual capital gains of approximately \$125,000. I can’t possibly afford to pay a tax on money I never received, yet the IRS seems unable or unwilling to work out a solution that is in line with the actual capital gain I realized.

Four years has passed, and I’ve gone through a failed Offer in Compromise and seemingly endless paperwork in Tax Court. My wife and I are expecting our first child next month, and I have no idea how we’ll ever cover our basic costs if the IRS starts garnishing my wages. I can’t even begin to describe the negative impact this experience has had on my personal and professional life.

I still hold hope that there is light at the end of the tunnel—I don’t believe the AMT was ever intended to snare taxpayers for capital gains never received, and that’s what this legislation can help remedy.” I respectfully and urgently request your support of H.R. 3385.

Tony Kadillak

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#### Statement of Todd Keen, Westminister, Massachusetts

Dear Honorable Chairman Camp and Ranking Member McNulty:

I have submitted my testimony and shared my story at these following events: Spring/Summer 2005, President’s Tax Reform Advisory Panel.

I now wish to share my story directly with you in hopes of garnering your support and leadership of the Honorable Sam Johnson’s H.R. 3385.

I was contacted yesterday via email by an organization I have been associated with for the last several years known as ReformAMT ([www.reformamt.org](http://www.reformamt.org)). I joined this organization sometime after being hit with a substantial tax bill in the form of AMT tax in the tax year 2000. They have informed me of your panel and you’re looking for input on the following items regarding current tax laws:

- Headaches, unnecessary complexity, and burdens that taxpayers—both individual’s and businesses—face because of the existing system.
- Aspects of the tax system that are unfair.
- Specific examples of how the tax code distorts important business or personal decisions.
- Goals that the Panel should try to achieve as it evaluates the existing tax system and recommends options for reform.

In regards to the following item:

- Headaches, unnecessary complexity, and burdens that taxpayers—both individuals and businesses—face because of the existing system.

I have worked most of my adult life at start-up high technical companies which commonly issued stock options as a form of compensation. One grant I received in 1997 was for ISO options, the rest were for Non-Qualified options. It is the ISO options that have created my headache. With the ISO options the general prevailing philosophy on the sales of these options was to exercise them and hold them for at least a year so that they would be taxed as long term capital gains. This philosophy appears to have been a recipe for overtaxation in the form of AMT tax when held in the context of the boom period of 1999–2001. While my employer held seminars on the implications that stock options had on potential tax burdens, we would be advised to consult with our own private tax consultant on our specific details. The problem is many tax consultants seemed to be inadequately informed on the matter of stock sales, ISO options and AMT tax implications. The result of attempting to do the correct thing for me to put myself in a tax situation where my ISO options would be taxable as long term gains resulted in being taxed on potential income that I have never made. Indeed four years later the stock my ISO’s were granted in have still not approached the values that my AMT tax was based upon. I have

since sold these shares to pay for my AMT obligation, but I am extremely disappointed at the opportunity lost. I am not an accountant and to this day still do not know what would have been the correct way to handle my ISO options.

I have continued to seek accounting help in this area several years after the fact, I have involved myself in the organization ReformAMT and hope that some day a clearer more representative taxation on my ISO sales will be implemented and I will have some restitution on my AMT taxes paid.

I am not a millionaire. I do not earn \$200,000.00 every year. I had several exceptional earnings years based upon stock options in the late 90's and early 2000. I am not now nor have I ever been close to bankruptcy. I have paid all my tax bills. I do believe that due to the current tax laws and lack of correct advice I have been overtaxed in the form of AMT tax on ISO options for profits I will never earn. I also feel that the government has impacted my ability to provide greater stability in the form of financial security to both my children and my spouse and I as we get older. This seems shameful to me that taxation laws could have this kind of impact on a family.

In regards to the following item:

- Aspects of the tax system that are unfair.

Any tax law that taxes people on potential future earnings and then does not return those taxes if the earnings are not realized is just plain unfair.

In regards to the following item:

- Specific examples of how the tax code distorts important business or personal decisions.

For me my important decisions had to do with funding my children's educations and providing for my wife and I in retirement. Due to the complexity and lack of correct advice in ISO/AMT matters my ability to properly plan for these items have been adversely impacted.

In regards to the following item:

- Goals that the Panel should try to achieve as it evaluates the existing tax system and recommends options for reform.

My primary goal for this panel is to recover AMT taxes assessed in the year 2000 for exercise of ISO stock options. My secondary goal would be obviously for others who have been impacted similarly to have their AMT recovered as well. My third goal would be a review of the AMT tax laws to see if they make sense and do whatever it is they were originally intended to do. If they do a new less complicated method of implementing these needs to be developed. Currently the AMT taxation rules are even too complicated for most accountants to properly explain to clients.

While I have not commented on specifics of my AMT impact other than the time frames and personal feelings towards the issue, I would be more than happy to meet with the panel to discuss any specific detail of my AMT experience. I am not comfortable providing more specific details in this letter, as I am told it would be public record.

I respectfully and urgently request your support of H.R. 3385.

Lakeland, Florida 33803  
August 25, 2005

Dear Honorable Chairman Camp and Ranking Member McNulty:

I wish to take this opportunity to share my story with you and the other Members of the Ways and Means Committee, and to request your support for H.R. 3385.

The Alternative Minimum Tax, required to be paid in advance and in anticipation of profit, had had a profound effect on our family.

Our son, with a young family, was excited to be given stock options in Dragon Systems. When he was finally able to exercise these options, he invested 15,000 hard earned dollars. He was prohibited from selling these shares for a period of time, and during that time the company was sold, and the stock became worthless.

In the meantime, the IRS tax form required that he check the box stating that he'd exercised his options. His tax burden on the 'unearned but anticipated profit' was an identical \$15,000. If our son had not had family to help pay this tax, he would have lost everything to the IRS for inability to pay.

This was over five years ago, and the IRS still has the \$15,000 in taxes he paid, but will never have a profit in his name to charge against his account.

I sincerely hope you can find it in your hearts to find a way to release these funds back to the hard-working, honest individuals who have been adversely affected by the AMT by supporting H.R. 3385.

Thank you,

Beatrice C. Kempster

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### Statement of Daniel T. Kirby, Pensacola, Florida

Distinguished Congressmen and Congresswomen;

Thank you for letting me have this opportunity to speak on behalf of the Fair Tax Act or national sales tax. Congressman Linder has done an excellent job in creating this idea. It is fair and would work better than a flat tax.

Simply put, the Fair Tax would replace the way we're currently taxed, based on our annual income; with a tax based on goods and services.

Briefly outlined is the FairTax. The FairTax proposal is a comprehensive plan to replace federal income and payroll taxes, including personal, gift, estate, capital gains, alternative minimum, Social Security/Medicare, self-employment, and corporate taxes. The FairTax proposal integrates such features as a progressive national retail sales tax, dollar-for-dollar revenue replacement, and a rebate to ensure that no American pays such federal taxes up to the poverty level. Included in the FairTax plan is the repeal of the 16th Amendment to the Constitution. The FairTax allows Americans to keep 100 percent of their paychecks (minus any state income taxes), ends corporate taxes and compliance costs hidden in the retail cost of goods and services, and fully funds the Federal Government while fulfilling the promise of Social Security and Medicare.

#### **Americans take home their *whole* paychecks.**

Not only do more Americans have jobs, but they also take home 100 percent of their paychecks (except where state income taxes apply). No federal income taxes or payroll taxes are withheld from paychecks, pensions, or Social Security checks.

#### **No federal sales tax up to the poverty level means progressively like today's tax system.**

To ensure no American pays tax on necessities, the FairTax plan provides a prepaid, monthly rebate (prebate) for every registered household to cover the consumption tax spent on necessities up to the federal poverty level. This, along with several other features, is how the FairTax completely untaxes the poor, lowers the tax burden on most, while making the overall rate progressive. However, the FairTax is progressive based on lifestyle/spending choices, rather than simply punishing those taxpayers who are successful. Do you see how much freer life is with the FairTax instead of the income tax?

#### **No tax on used goods. The amount you pay to fund the government is totally visible.**

With the FairTax you are only taxed once on any good or service, the sales tax is charged just as state sales taxes are today. If you choose to buy *used* goods—used car, used home, used appliances—you do not pay the FairTax. If, as a business owner or farmer, you buy something for strictly business purposes (not for personal consumption), you pay no consumption tax. When you decide what to buy and how much to spend, you see exactly how much you are contributing to the government with each purchase.

#### **Retail prices no longer hide corporate taxes or their compliance costs, which drive up costs for those who can least, afford to pay.**

Did you know that hidden income taxes and the cost of complying with them currently make up 20 percent or more percent of *all* retail prices? It's true. According to Dr. Dale Jorgenson of Harvard University, hidden income taxes are passed on to the consumer in the form of higher prices—from an average 22 percent on goods to an average 25 percent on services—for everything you buy. If competition does not allow prices to rise, corporations lower labor costs, again hurting those who can least afford to lose their jobs. Finally, if prices are as high as competition allows and labor costs are as low as practical, profits/dividends to shareholders are driven down, thereby hurting retirement savings for moms-and-pops and pension funds invested in Corporate America. With the FairTax, the sham of corporate taxation

ends, competition drives prices down, more people in America have jobs, and retirement/pension funds see improved performance.

**The income tax exports our jobs, rather than our products. The FairTax brings jobs home.**

Most importantly, the FairTax does not burden U.S. exports as they are with the current income tax. So the FairTax allows U.S. exports to sell overseas for prices 22 percent lower, on average, than they do now, with similar profit margins. Lower prices sharply increase demand for U.S. exports, thereby increasing job creation in U.S. manufacturing sectors. At home, imports are subject to the same FairTax rate as domestically produced goods. Not only does the FairTax put U.S. products sold here on the same tax footing as foreign imports, but the dramatic lowering of compliance costs in comparison to other countries' value-added taxes also gives U.S. products a definitive pricing advantage which foreign tax systems cannot match.

**The FairTax strategy is revenue neutrality: Neither raise nor lower taxes so consumer costs remain stable.**

The FairTax pays for all current government operations, including Social Security and Medicare. Government revenues are more stable and predictable than with the federal income tax because consumption is a more constant revenue base than is income.

If you were in a 23-percent income tax bracket, the Federal Government would take \$23 out of your paycheck for every \$100 you made. With the FairTax, if the Federal Government gets \$23 out of every \$100 spent in America, the same total revenue is delivered to the Federal Government. This is revenue neutrality. So, instead of paycheck-earning Americans paying 7.65 percent of their paychecks in Social Security/Medicare payroll taxes, plus an average of 18 percent of their paychecks in federal income tax, for a total of about 25.65 percent, consumers in America pay only \$23 out of every \$100. Or about 30 percent at the cash register when they elect to spend on *new* goods or services for their own personal consumption. And this tax is collected only on spending above the federal poverty level, providing important progressivity.

**Tax criminals—don't make criminals out of honest taxpayers.**

Today, the IRS will admit to 25 percent non-compliance with the code. FairTax.org will be generous and simply take the position that this is likely a conservative estimate of the underground economy. However, this does not take into account the criminal/drug/porn economy, which equally conservative estimates put at one trillion dollars of untaxed activity. The FairTax *will* tax this—criminals love to flash that cash at retail—while continuing to provide the federal penalties so effective in bringing such miscreants to justice. The substantial decrease in points of compliance—from every wage earner, investor, and retiree, down to only retailers—also allows enforcement to concentrate on following the money to criminal activity, rather than making potential criminals out of every taxpayer struggling to decipher the current code.

Scottsdale, Arizona 85260  
August 29, 2005

Ways and Means Committee:

H.R. 3385 comments from AZ 5th district:

This letter is a request for support of H.R. 3385 which provides fair relief to taxpayers who have been caught in the unfair AMT ISO trap.

My story. I am a long time resident in Arizona's 5th district. I was a senior executive at FINOVA—a NYSE listed commercial finance company based in Scottsdale, Arizona. During FINOVA's heyday I made lots of money, gladly paid lots of taxes, and contributed to local charities. In fact, during my last six years with FINOVA I paid over \$2.1 million in Federal Taxes. In March 2001 FINOVA filed for Chapter 11 protection and my employment was simultaneously terminated. The value of FINOVA's stock plummeted with the bankruptcy filing. During the two year period before FINOVA's bankruptcy filing and for three months after my employment termination, I was prevented from selling my FINOVA stock under SEC insider trading rules. Consequently, I lost most of my net worth which was heavily concentrated in FINOVA stock, and lost my lucrative employment at the same time.

My history. During FINOVA's good times, I exercised Incentive Stock Options (ISO's), borrowed money to exercise the ISO's and pay Alternative Minimum Tax,

I held the related stock since I was precluded from selling the stock under SEC insider rules, and finally sold 100% of the stock after my departure at a significant loss.

I followed the IRS rules for ISOs which effectively required me to prepay taxes in the form of AMT. The IRS rules were undoubtedly established with the belief that this "prepayment" was appropriate since the taxpayer would incur an eventual gain on the ISOs. A logical rule that put taxes into the Treasury coffers. But the critical problem is the very difficult process of recapturing this credit if the ISO gain never materializes. In my situation, the gain never occurred as I sold the stock at a loss. So, in summary I prepaid taxes for a gain that never occurred. And the only way to get those prepaid taxes back under current IRS rules is to make lots of money (more than \$500k per year)—and in my four years after leaving FINOVA my earnings have averaged under \$100,000 per year.

Fortunately H.R. 3385 has been introduced to right the inequity of the AMT ISO trap. H.R. 3385 does not try to fix all of the issues with AMT—it focuses solely on the ISO trap. When I try to be as unbiased as possible on this issue, I can still can not justify the unfair nature of AMT credits related to ISO. The only argument I can muster against H.R. 3385, is that it reduces tax revenue in a time of budget deficits and record debt. But the continuation of an unfair tax because it is not comfortable to address the source of repayment is little comfort. Without this bill, I have no way in the foreseeable future to recoup \$135,000 in taxes I paid for a benefit I never captured.

Please support this bill.

Robert M. Korte

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Mountain View, California 94040  
*August 11, 2005*

Dear Chairman Camp, Ranking Member McNulty, and Committee Members:

Thank you for the opportunity to voice my concerns regarding tax reform. I have previously submitted my testimony to the President's Tax Reform Panel earlier this year, as well as to the Tax Reform Hearing of June 2005, and to the Tax Simplification Hearing of June 2004, regarding the "AMT/ISO problem" (alternative minimum tax treatment of incentive stock options). At this time, I would like to ask for your support of H.R. 3385, the AMT Credit Fairness Act, introduced by Rep. Sam Johnson.

Originally from Cincinnati, Ohio, I graduated in 1985 with a degree in engineering from Case Western Reserve University, and then began a career in Silicon Valley. I joined Netscape as an engineer in 1996. Five years later, I exercised incentive stock options and held the shares, due to my belief in the company, and paid AMT of over \$180,000, about twice my annual income, on "phantom gains." By 2004, I had sold off all of the stock, but my actual gains were far lower than the "phantom gains" I had paid tax on. Now, I find that I have a six-figure AMT credit balance that is probably not recoverable in my lifetime. Needless to say, this is very disappointing. Whereas I fully accept responsibility for any gains or losses in the stock that I held, I am at a loss to understand why many years worth of my hard-earned savings must be permanently forfeited to pay an outrageously high tax involving "phantom gains."

H.R. 3385, while not providing a "quick fix," will accelerate the return of these tax overpayments by providing refunds in chunks over a period of years. This will help to ease the burden on people like myself, as well as other affected taxpayers who were unfortunate enough to have to sell their homes, declare bankruptcy, and face financial ruin, all because of a severe and unfair tax on "phantom gains." This is not about giving a tax break to the rich, it is a means to return overpayments of tax to ordinary working people who were taxed as if they had gotten rich from stock options, but in reality did not.

Therefore, I respectfully and urgently request your support of H.R. 3385. Thank you for your attention to this matter.

Sincerely yours,

Hans Lachman

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Ben Lomond, California 95005  
August 30, 2005

Dear Honorable Chairman Camp and Ranking Member McNulty:

This letter is to add testimony to those given by others who are suffering from the AMT issues on incentive stock options. In my case it is devastating and has taken all that I have saved to carry me through retirement and left me in a dire position.

I am a software engineer and have worked for wages all my life. I've been continuously employed since I was twelve years old. I'm from a large (5 boys and a girl) poor family. We lived on one income from my father as a technician. I worked my way through high school and college at various jobs to provide me with clothes and transportation and to help supplement the family income.

I have been fortunate enough to work at the state of the art in computer science while at the DOE where I implemented operating systems on supercomputers. My 22 years with DOE at various facilities exempted me from FICA and when I left DOE to work in aerospace, I was quite behind my peers in acquiring Social Security credits. While at various positions in Silicon Valley where I was again working at the state of the art in networking and computer security, there was no real retirement benefits. The work was all consuming and most enjoyable and the years seemed to fly by. When I reached fifty-five, I noticed that I should work carefully to amass a nest egg to carry me through my retirement years. The point was driven home when my grandmother could no longer take care of herself and had no support to help provide comfort until she died. I was her only support as the eldest child (my mother and father died at an early age). She had nothing but Social Security and that was just not sufficient to take care of her. While I had sufficient income to allow her the care she required, it made me aware of the state of risk that I was in. I had never given the fact that I may not be ABLE to work any significant thought and at the age of fifty-five, I did not have many years left to save for a time when I may have to stop working.

I took a position at Exodus Communications as an early employee for a reasonable, but not outstanding salary with stock options. It was explained that if I worked hard and the company prospered, my stock options would become valuable. I liked that idea; I have always been an overachiever. During my tenure at Exodus, I worked harder than I ever have in my life. I worked days at a time and traveled constantly. I have never worked under such stress in my life, but I built a security managed services business for Exodus that was their most profitable service. Eleven group members generated over \$15 million in annual revenue. We were the highest producers in the corporation and watched over a world wide network of security services for the Exodus clientele.

The five years at Exodus took a heavy toll on me and my family but we all supported each other and took pride in the fact that we were building a business that anyone could be proud of. We were counting heavily on the value of the stock options to provide us with the retirement income necessary. We built a retirement home in Colorado and purchased a nice home here in Santa Cruz County that we hoped would provide a little estate for our two children after we passed away.

That was not to be; shortly after the company went public, a new set of management was brought in as part of the process of becoming a large corporation. Ellen Hancock and her staff squandered all the value that all the hard-working staff had generated and drove the company into bankruptcy in a very short time. I was not sure what had happened, but as I learned about Enron, Worldcom, and other corporate criminals, it became obvious that I too was a victim of corporate greed. When it became obvious that all the stock options I had purchased had become worthless, I was most disappointed, but we still had our two houses, an IRA, some savings and I still had a good reputation as a leading software development manager. However, that was not to be. In August, after filing two extensions, my CPA and financial advisory informed me that I had a \$1.7 million tax bill based on all that worthless Exodus stock. That's just not possible, I paid over a half million dollars in taxes the year before, how could I owe another 1.7 million based on worthless stock.

I can assure you that you have never experienced a shock like the one I got when the CPA informed me that I REALLY owed the State and Federal Government all that money. Many times over what I had left from my time at Exodus or that I could make in my viable working years. Until that day, my biggest problem was with finding a new job to replace the income I had at Exodus. Now that I was 60 and the market was tight, no one wanted to hire me even though I'm still the best in the business.

So here I am at 61 still telling myself that just CAN'T happen to me. There must be some way this is incorrect. I've attempted to work out settlements with the IRS

and FTB and they now have all the cash and retirement savings I have accumulated during my 50 years of employment and it appears they are about to take the rest of my possessions. I never thought I'd end up as one of those you see on a street corner with a cardboard sign, but I'm not far away from that today. I've been looking for work for nearly a year now and living on savings which have just been taken by the IRS. There are tax liens on both houses so I can't sell them to buy food and pay rent. There are zero balances in my bank accounts and all the monthly bills are coming due.

I feel really bad for my wife who depended on me to provide us with some sort of retirement. The frustrating thing is with this job market, I can't just say "Oh well, I'll just work until I die." I can't even find a job with sufficient income to pay medical insurance or rent. I just don't know what I'm going to do. It's a mess.

Thanks for your attention. I do hope that some equitable changes can be made in the tax system before we lose our last remaining assets.

Sincerely,

Leroy Lacy and Janis K. Purl

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Hutto, Texas 78634  
August 31, 2005

Honorable Chairman William M. Thomas and House Ways and Means Committee  
Dear Chairman Thomas and Committee Members:

Thank you for looking into what is an extremely egregious situation. The AMT as it affected us due to ISO stock options has forced us into bankruptcy, and due to the extremely large amount of tax it calculates, it may cause us to lose everything we own, including our house. At a minimum, it is forcing us into a Chapter 11, preventing us from a Chapter 13 or Chapter 7, which means our bankruptcy costs are about \$15,000-\$16,000 instead of \$2,000 to \$3,000. Our effective tax rate was over 600% and if nothing is done, it will take us over 70 years to utilize our tax credits. This happened at a bio-tech company not a telecom company, so there are some of us in many facets of U.S. industry, not just one.

How is this fair or right? We went from thinking we were on our way to having a decent retirement after struggling for 20 years to living the last 5 years under the constant stress of what is going to happen to us and how are we going to survive. There hasn't been a single day that we haven't had some issue, be it physical, emotional, stress, or depression to deal with. So far we have been able to stay married and sane, but it has not been easy. Instead of helping our children and parents they are having to help us. Is this the American Dream? Since finding out about the AMT repercussions, almost everything we do has been based on how to deal with it. All we did was exercise my ISO options. How can we owe taxes on something that we never realized? How can the U.S. Government and its tax code be responsible for making thousands of people paupers?

For those of us that are either on the brink of ruin or over the edge, it would be a big help to us to be able to resolve this equitably. It will not put things right for us because we still will not have any retirement or funds and will have to try to rebuild, but it will at least help us to get started. If we can either take the credits that are due to us more quickly so that we can recover the credits that are due to us or if we can treat the exercise and final sale/resolution of ISO options/stock as a single year occurrence, we can at least have a fair way of dealing with this issue.

We have been a middle-income family since we were married almost 25 years ago. We have worked for everything we acquired, and have not been extravagant spenders. In fact since our 2 children started their activities, ballet and dance, ice hockey and figure skating, most of our expendable income has gone for them. I worked at a company, Luminex Corp. that I helped to be successful enough to go public, and was offered ISO stock options as a reward for my efforts. Due to management changes I left the company in July of 2000, and had to exercise my options, but was not aware of the tax implications of the AMT. Everyone including our stockbroker told us to hold on to the stock to get long term gain tax gains as well as I thought the company had a future. What we didn't realize is that the IRS wanted us to pay the taxes on the gain (AMT) even though we did not sell the stock. This would be like paying taxes for the increase (gain) in value of your land, even though you never sold it. All we have left is the house we have been living in for the last 12 years, as we no longer have any savings or retirement, and both of our vehicles are

over 6 years old. Also, since I came from the technology sector, I was out of a job in my industry for over 2.5 years, and worked at whatever jobs I was able to find. I am now working in industry again, but this burden of the AMT is having very serious consequences that are not only affecting ourselves, but is also affecting our children. Instead of being able to pass along some of the fruits of our sacrifices and hard work, we are not able to help our children start their own lives, and in fact are concerned for ours in our later years as our children (17 and 22) are having to help us now.

We had to exercise my ISO options in August 2000. The IRS says that due to the AMT, we owed almost \$300,000 from that year even though we didn't sell them. Because of what happened with the stock value, if we could treat the exercise and the final result as a single transaction, or if we didn't have to consider the AMT, the amount would be more realistic and manageable. We currently are in bankruptcy and the IRS has put a lien on our house for over \$400,000, that if we come out of bankruptcy (the trustee is trying to say there is no outstanding question about the validity of the AMT so is trying to get the case dismissed), they will seize it. We don't understand how we can owe taxes on something we never had. The judge just ruled that the IRS claims are such that we cannot file Chapter 13 but have to file 11, which increase our costs to recover from \$2,000–3,000 to \$15,000–\$16,000. If we are already struggling to recover, how is adding \$13,000 on top of our debt helping?

Your consideration in this issue is greatly appreciated. Please help to make the AMT law apply as it was supposed to, not against normal middle-income citizens.

John Lapaglia

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#### **Statement of Leo E. Linbeck, Americans for Fair Taxation, Houston, Texas**

I serve as the voluntary Chairman of Americans for Fair Taxation (FairTax.org). FairTax.org is pleased to submit this statement in support of the FairTax (H.R. 25) introduced by Rep. John Linder. H.R. 25 is superior to all other tax reform legislation being considered by the Committee.

FairTax.org is the nation's largest, single-issue grassroots organization dedicated to fundamental tax replacement. FairTax.org is the collective voice of more than 500,000 Americans of all ages, ethnic backgrounds, political affiliations and walks of life who share two views on tax reform:

- That Americans can rise above the failed income and payroll tax regimes to develop a more visible, more globally competitive, administrable, fairer, understandable and less costly and intrusive system of collection; and
- That when educated about alternatives in an unbiased way, regardless of ideology and political affiliation, Americans consider the FairTax to be the best plan for our national and individual prosperity and freedom.

#### *The FairTax Plan*

The FairTax repeals all current taxes imposed by the Internal Revenue Code on income and wages; including individual, corporate and alternative minimum income taxes, capital gains taxes, estate and gift taxes, and Social Security and Medicare taxes. In place of these taxes, the FairTax imposes a single, 23 percent tax (tax-inclusive) rate on the final retail sale of goods and services used or consumed in the U.S. The FairTax plan then amends the U.S. Constitution so that the income tax will never return.

The FairTax plan taxes all personal consumption at the point of final consumption. To ensure the FairTax does not cascade, business-to-business transactions are not taxed. Intermediate goods and services are properly treated as inputs into goods and services sold at retail. Unlike the current system which taxes income multiple times and on an inconsistent basis, the FairTax taxes income only once and then when consumed. Furthermore, the FairTax does not tax used goods under the principle they will have already been taxed under the income tax or, after enactment, the FairTax. The FairTax countenances no exemptions for goods or services in order to ensure the broadest conceivable base without special interest exemption or compliance problems.

#### *The FairTax is a Progressive Tax*

While permitting no exemptions, the FairTax holds the poor harmless through a monthly "prebate" equal to 23 percent times the DHHS poverty level for the family unit plus an additional amount in the case of married couples to avoid a marriage penalty. The prebate ensures each family unit can consume tax free up to the pov-

erty level. The amount of tax free consumption for a married couple with two children in 2005 would be \$25,660. Unlike the current system, no poor person will pay any tax under the FairTax. And the effective tax rate for the lower middle class since the prebate will protect most of their spending from tax. Those spending at twice the poverty level will have an effective tax rate of only 11½ percent under the FairTax. Thus, a married couple with two children spending \$51,320 would pay only 11½ percent in sales tax and pay no income tax and no payroll tax.

**A family spending four times the poverty level would pay an effective tax rate of 17¼ percent.**

*The FairTax Rate is Revenue Neutral*

Several independent researchers confirm the FairTax plan is revenue neutral at 23 percent. As the starting point for this rate calculation, consider that in fiscal year 2003, the total taxes the FairTax repeals accounted for about 1.67 trillion. The economy in 2003 produced goods and services valued at 10.4 trillion. Of this, 7/8's or \$8.6 trillion was consumed. To raise the taxes it repealed in that year, the rate on this base without any exemptions would be 19.4 percent, derived by dividing the taxes replaced by the total consumption in the U.S. The FairTax rate must be increased to 23 percent rate to accommodate the FairTax's generous "prebate." The actual tax base calculations are, of course, more complex. Fairtax.org would be pleased to provide the Committee our detailed base calculations.

*The FairTax Imposes the Lowest Possible Marginal Rate of Any Tax Neutral System*

It is a mathematical certainty that broadening the base and imposing a single rate of tax will reduce average marginal rates. Because the FairTax plan utilizes a consumption base larger than both the current income tax base and any other alternative, it imposes the lowest marginal tax rate of any revenue neutral alternative without doubly taxing the same income. In 2001 (the latest year data available), total adjusted gross income was \$6.17 trillion. Thus, the basic building block of the FairTax base—total consumption—is 38 percent larger than the current tax system's starting point—adjusted gross income. Actual *taxable* income under the current system was only \$4.22 trillion in 2001, only 49 percent of total consumption.

*The FairTax Would Stimulate Economic Growth*

Lower marginal tax rates improve the incentive to work, save and invest. A consumption tax base that no longer taxes savings and investment multiple times will increase savings and investment. Higher investment levels will increase the productivity of employees, demand for workers and real wages.

Economists estimate that the FairTax plan will improve wages and the economic wellbeing of virtually all Americans (tax lawyers are an exception). Work by Harvard economist Dale Jorgenson shows a quick 9 to 13 percent increase in the GDP. Similarly, Boston University economist Laurence Kotlikoff predicts a 7 to 14 percent increase. Work by Fiscal Associates' Gary Robbins shows that replacing the current tax system with a flat rate system that taxed capital and labor income equally—such as the FairTax—would increase the GDP 36.3 percent and increase private output by 48.4 percent over the long run. Even work by Nathan Associates, commissioned by the National Retail Federation which is hostile to the FairTax, shows that the economy would be one to five percent larger under a sales tax than in the absence of reform.

*The FairTax Untaxes Education*

Tuition is not taxed by the FairTax plan because the FairTax draws no distinction between investment in human capital and investment in plant or equipment. Rather, the FairTax treats education as a personal investment the primary aim of which is to increase future income.

*The FairTax Untaxes and Uncomplicates Saving*

Americans today save at low rates because our current income tax regime punishes saving and investment. Savings are made with what remains after payroll and income tax, and the return on those investments is taxed multiple times: the income-producing asset is taxed, corporate income (including capital gains) is taxed and dividends are taxed. Although assets in qualified pension accounts approach being taxed in a manner consistent with a consumption tax, the thousands of pages of pension regulations impose further costs that discourage pension plans. FairTax supporters do not see the ability to save as a privilege to be bestowed by the Internal Revenue Code but advocate adoption of the simplest pension plan in the world; one in which everyone can participate—if you don't spend it on yourself after you've met life's necessities, they don't get to tax it. The FairTax offers the equivalent of

a universal, unlimited IRA with no restrictions on how much to save or on who can save.

*The FairTax Reduces Compliance Costs More Than Any Other Tax System*

The current system literally throws away precious economic resources on wasted compliance costs that add no value to the economy. We collectively filed 227 million tax returns in FY 2004, and more than 1.4 billion information returns. In 2002, the Tax Foundation estimates individuals, businesses and non-profits spent an estimated 5.8 billion hours complying with the federal income tax code at a cost of over \$194 billion. This amounts to a 20.4 percent tax compliance surcharge for every dollar the income tax system collected and nearly two percent of the GDP.

*The FairTax Will Ensure Greater Compliance*

The FairTax would be more easily enforced, foster greater compliance and be less intrusive than current law or competing plans. Despite its intrusiveness and large compliance costs, the current tax system is failing. According to the latest IRS data, the annual tax gap—the difference between the taxes due the IRS and the actual taxes collected—is between \$312 billion and \$353 billion. The tax gap would be reduced for several reasons. First, because marginal tax rates are the lowest they can be under any sound tax system, cheaters profit far less from cheating. Second, it will be easier to catch cheaters, since the number of tax filers will drop by as much as 90% since only businesses will file tax returns. Thus, enforcement authorities will be required to monitor far fewer taxpayers and if resources are held constant audit rates will increase (and audits will be vastly simplified). Finally, more than 80 percent of the sales tax is collected by 15 percent of the retailers. Third, simplicity and visibility add to enforcement. Today the more than 228 million taxpayers can cheat in the privacy of an office and bury their cheating in the unnavigable 7,000 code sections with plausible deniability that the taxpayer even understood the law. The FairTax increases the likelihood that tax evasion would be uncovered and leaves little room to hide between honesty and outright fraud. In short, tax collectors can focus enforcement resources on far fewer taxpayers, with far fewer opportunities to cheat, diminished incentives to do so, and a far greater chance of getting caught if they do.

*The FairTax Fully Eliminates the Current Self-imposed Tariff Against American Producers*

American manufacturing faces unprecedented foreign competition. With a negative trade balance in goods with every principal nation and region, the U.S. trade deficit is approaching \$600 billion per year, more than 5 percent of GDP. Despite this, the U.S. has failed to address the central problem: the increasing reliance by our trading partners on border adjusted taxes. 29 of 30 OECD nations (and China) employ border-adjusted consumption taxes rebated on exports and levied on imports at an average rate of 17.7 percent ad valorem. Border adjusted taxes enhance, through WTO legal means, the competitiveness of exports. Since these nations in turn levy consumption taxes on imports, U.S. produced goods are effectively double taxed—paying U.S. income and payroll taxes and foreign value added taxes. Similarly, foreign goods sold in the U.S. bear neither foreign consumption tax or any appreciable U.S. tax.

As the purest version of a destination principle consumption tax, the FairTax completely removes the self-imposed tariff we now impose on U.S. produced exports. The FairTax does not tax goods or services used or consumed outside the U.S. Conversely, it taxes imports the same as U.S. produced goods when they are sold at retail in the U.S. For this reason, the FairTax can play a central role in revitalizing the American manufacturing base lost to foreign competition, and return to America the high-wage manufacturing jobs we have driven overseas. It will also help to make U.S. agricultural and forestry products more competitive.

*The FairTax Benefits Charities More Than Any Other Plan or the Current Tax System*

The FairTax will enhance resources available to charities (1) by improving the primary determinant of charitable giving—economic growth and national income; and, (2) by giving every taxpayer the equivalent of a supercharged charitable contribution by enabling contributions free of income, payroll and sales tax.

Some supporters of the income tax argue the steeper the rate of tax, the more one is inclined to be “charitable,” but empirical data confirm a high correlation between economic growth and the national giving. Total philanthropy has held steady at around 2% of GDP for more than two decades even while the top marginal rate has fluctuated between 28 and 70 percent. Simply put, as people become more prosperous, they give more to philanthropic causes. And virtually every economist who

opines that deductions are needed for charitable contributions also makes the case that a consumption tax would improve economic prosperity.

Equally important, the FairTax lowers the costs of charitable contributions for all taxpayers in ways unmatched by the income tax. The appropriate question with respect to the charitable contribution is not ‘how much of a deduction is provided?’ but rather ‘what must a taxpayer earn in order to make that contribution?’ A taxpayer under the FairTax must earn \$100 to contribute \$100, but a taxpayer able to deduct the contribution today, must earn at least \$108.28 to contribute \$100 (\$118 if both employer and employee share of payroll taxes are considered paid by the contributor). A non-itemizing taxpayer (three-quarters of all taxpayers) in a 28 percent bracket must earn \$176 to make a \$100 contribution to charity given the combined effect of the 15.3 percent payroll tax.

To match the power of the charitable “incentive” under the FairTax, the income tax would not only have to permit charitable contribution deductions against payroll taxes, but eliminate the distinction between itemizers and non-itemizers and the many other restrictions on the deduction.

*The FairTax Benefits Home Ownership More Than Any Other Plan or the Current Tax System*

The FairTax lowers the “true costs” of buying a home. The purchase of new property is taxed as a consumption item under the FairTax, in a manner not unlike today. We currently require homebuyers to pay for their new home with what remains after payroll and income tax today. There is no deduction for the purchase of a home. But unlike under the current regime, the FairTax imposes a lower marginal rate of tax and capital gains from the sales of used or new property are not taxable to the sellers under the FairTax. Moreover, the cost of newly constructed homes should decline as much as 20 percent as a result of the elimination of taxes imposed upstream. More importantly still, purchasers of existing homes (the most common properties bought by first time homebuyers) pay no FairTax on the home sale.

The mortgage interest deduction (MID)—now permitted for servicing the interest on mortgage debt—pales in comparison to the full non-taxation of interest by the buyer or the lender under the FairTax. The intended result of the MID is the non-income taxation of mortgage interest (or more precisely, the funds used to pay mortgage interest). But as in the case of the charitable deduction, the MID cannot be taken against payroll taxes which represent about 43 percent of income-based taxes by receipt. Three-quarters of all Americans pay more payroll than income taxes and they are disproportionately the first time homebuyers. By repealing income and payroll taxes alike, the FairTax plan ensures mortgage interest payments are made with totally untaxed earnings. If the MID were to treat mortgage interest that favorably, it would have to allow the deduction against payroll taxes. Finally, since lenders are not taxed on interest they receive the FairTax is estimated to lower interest rates by about 250 basis points (toward the tax-free bond rate) which will further reduce the carrying costs of purchasing a home. The FairTax also benefits home ownership because it enables homebuyers to save without swimming against the tide of taxation to amass the down payment.

*The FairTax Will Provide a Template for a Uniform System of Taxation for States*

States today are struggling with how to tax Internet and mail order sales. They miss the larger picture. It is not the sale of goods and services that presents a problem, but the taxation of income which can shift around the world as the speed of light. The FairTax offers states a chance for uniformity in adopting a common tax base that will enable states to reach out-of-state retailers selling into the state. And using all measures of variance, consumption is less variable than the taxable income.

*Unlike Other Plans, The FairTax Will Not Morph Into The Income Tax*

Not only does the FairTax tax consumption rather than income, it would eliminate the administrative means to collect an income tax. The FairTax offers the only alternative that can assure no return of the income tax because it is the only comprehensive reform that can exist after repeal of the 16th amendment. The flat tax, the USA tax and other similar plans keep the entire income tax apparatus in place and can easily be transformed back into an income tax.

*The FairTax Will Bring Honesty to Government by the Most Visible and Transparent Tax*

Today, small changes to the Code shift tens of billions of dollars to particular groups of taxpayers in ways not as visible as direct appropriations, but just as effective. With each special exemption, credit, deferral, deduction or definition that re-

sults, the marginal tax rates are increased on everyone else. When taxes are transparent, they are generally more difficult to raise.

*The FairTax Respects Privacy More Than Any Other System*

The FairTax eliminates the need for individuals to file tax returns. It will make our tax system consistent with our historically hallowed notions of privacy. The truth is that we could hardly have devised a more intrusive tax system for prying into our houses, our papers, our effects, our lifestyles, or our decisions. And we could have hardly devised a tax that—because of its many temptations to a large number of filers, its perceived unfairness, and its complexity—requires such intrusiveness as a prerequisite to its enforceability. By its own unalterable nature, from the cradle to the grave, the income tax eventually extracts, collates, and chronicles almost every detail of our financial and personal lives as a necessary condition of its enforceability.

*The FairTax is Supported by Small Firms*

The FairTax is the only plan specifically endorsed by a wide array of small business groups; including, the National Small Business United, the Small Business Association of Michigan, the Council on Smaller Enterprises, the Associated Builders and Contractors and the American Farm Bureau Federation. These groups, who consist of retailers as well as manufacturers and service providers, support the FairTax because it will eliminate tax on productive income, reduce compliance costs, and create economic growth.

*The Flat Tax and the Freedom Flat Tax Act*

The Hall-Rabushka-Army-Forbes flat tax is a modified value added tax that taxes labor value added at the individual level and capital value added at the business level. It retains the basic income tax apparatus with tax returns filed by both businesses and individuals. Because it expenses capital and treats savings as if they were in a Roth IRA, the Hall-Rabushka flat tax is a type of consumption tax. The flat tax taxes U.S. exports and imposes no tax on imports into the U.S.

Princeton economist David Bradford and more recently Robert Hall (the Hall in Hall-Rabushka) have proposed the X Tax which is the flat tax with graduated rates on labor income.

The flat tax could be converted back into a serviceable graduated income tax with the following changes:

1. Depreciate capital rather than expense capital;
2. Deduct inventories when sold rather than when purchased;
3. Make interest both taxable and deductible;
4. Tax dividends, royalties and capital gains; and
5. Make tax rates graduated rather than flat.

The fact that such straightforward modifications can transform the flat tax into a graduated rate income tax should give its supporters pause.

Although an improvement over the current system the flat tax is inferior to the FairTax because:

1. it retains the income tax apparatus and can be easily transformed into a graduated rate income tax;
2. it requires individuals to continue to file tax returns;
3. it is not nearly as transparent or understandable as the FairTax (as is evidenced by the fact that most flat tax supporters don't even understand what it is)
4. it hides a large portion of the total tax burden in the business tax; and
5. it continues to place American producers at a disadvantage both in U.S. markets and abroad.

Rep. Michael C. Burgess has introduced the so-called Freedom Flat Tax (H.R. 1040). This proposal would allow taxpayers to choose between a flat tax and the current system. The proposal thus would retain all of the special exclusions, credits, preferences and deductions in the current system and all of its complexity and compliance costs. It then adds a new layer of complexity. The proposal cannot be revenue neutral because it affords taxpayers an option between the current system and the flat tax. Virtually all taxpayers will do their tax returns both ways and file whichever way leads to the lowest tax bill.

*The Simplified USA Tax Act or "SUSAT"*

Rep. Phil English has proposed the simplified USA Tax. The proposal would impose both a business transfer tax (a subtraction method value added tax) and a type of consumed income tax (with graduated rates) where all individual savings is treat-

ed as if they were in a Roth IRA. The proposal does represent an improvement over the current tax system in that the tax base is consumption and the marginal tax rates are somewhat lower than the current system. In addition, the business transfer tax is border adjusted and would improve the competitiveness of U.S. producers in international markets.

Nevertheless the proposal retains the current income tax apparatus. It is quite complex compared to the FairTax and would have much higher compliance costs. Although an improvement over the current system the simplified USA Tax is inferior to the FairTax because:

1. it retains the income tax apparatus, including graduated tax rates;
2. it only modestly reduces marginal income tax rates;
3. it requires individuals to continue to file tax returns;
4. it is not nearly as transparent or understandable as the FairTax; and
5. it hides a large portion of the total tax burden in the business tax.

#### *Conclusion*

The FairTax is superior to the current tax system and to all of the alternatives being considered by the Congress. The FairTax represents the best plan to improve the wellbeing of the American people while raising the revenue needed to fund the Federal Government. It is more fair, will better promote economic growth and competitiveness, will better foster thrift, charitable giving, education and home ownership, will reduce needless compliance and administrative costs and protect privacy.

San Diego, California 92122  
August 26, 2005

Dear Honorable Chairman Camp and Ranking Member McNulty:

I have submitted testimony and shared my story to the President's Tax Reform Advisory Panel during the Spring of 2005.

I now wish to share this story directly with you in hopes of garnering your support and leadership of the Honorable Sam Johnson's H.R. 3385.

In Year 2000 during my employment at a high technology company, I exercised unvested incentive stock options that were issued by my company with an exercise price that was significantly less than the fair market value on the date of exercise. I wasn't able to sell these in Year 2000 so I incurred a significant AMT preference item that resulted in my alternative minimum taxable income being much greater than my regular taxable income. As a result, I had to pay approximately \$34,000 in AMT to the Federal Government and approximately \$5,000 in AMT to the state of California. These AMT values that I paid are over and above the regular tax amounts that I paid in Year 2000. The AMT tax itself that I paid was actually greater than the ordinary tax that I paid. I submitted an 83(b) election which effectively recognizes the AMT income in the year that this election was submitted. In order to pay the tax, I sold all equity holdings that I possessed.

The payment of these taxes put me and my family in a very challenging financial situation. I refused to take on any credit card debt in order to maintain our standard of living so we cut our spending dramatically. In fact, I turned off the heat in our house during the winter in order to save a few hundred dollars a month although I did keep a space heater running in our new baby's bedroom during the night. We did not contribute to our IRA accounts in Year 2001 and I even cut back my bi-weekly 401K contribution rate to one percent of my salary from a contribution rate that would result in me contributing the maximum yearly amount.

The AMT that is paid becomes an AMT credit which can be claimed by an amount that equals the regular tax minus the alternative minimum tax. In Year 2004, I will be able to claim approximately \$1,500 of this AMT credit. The yearly rate of recalculation of the AMT credit is generally low relative to the outstanding AMT credit for people in my situation. This AMT credit provides federal and state governments with an interest free loan that is paid for by the taxpayer since the taxpayer can't collect any interest on this money for himself. In fact, I understand that the taxpayer actually loses this credit upon his death.

Understanding the AMT tax system took many hours of my time. The time was spent reading appropriate tax books, reviewing some message boards on appropriate websites, and long discussions with my colleagues at work. The time required to understand this tax has a negative effect on productivity at my place of work. I can imagine that Joe taxpayer generally won't even be able to comprehend this tax even though he will be affected by it sooner or later.



I know well over twenty people who were adversely affected by staggering amounts of AMT. I know of one individual that needed to sell his house and move his family in order to pay the tax as he got laid off as well in Year 2001. Many of these individuals suffered psychologically as a result of the financial straits that they were subjected to as a result of the AMT. As a result, work productivity notably suffered as well.

I would like to add that many of my colleagues at work were adversely affected by exercising non-qualified stock options where the exercise price was much less than the fair market value on the date of exercise. The tax that is based on the difference between these two values becomes due on the date of exercise. It counts as regular tax and not alternative minimum tax. Unfortunately, my colleagues were not able to sell immediately since the shares weren't vested. The underlying stock price had already fallen dramatically enough when the exercised shares could be sold. The result is the tax paid in Year 2000 is much greater than the amount for which the shares could be sold. Reclamation of this loss will take decades for most of these individuals as only \$3,000 of the amount could be reclaimed annually. This regular tax coupled with their AMT burden has adverse financial consequences for my colleagues to this very day.

Some Recommendations for Tax Reform:

1. Elimination of the alternative minimum tax and payment of all outstanding AMT credit to individuals that are due this credit.
2. The loss of the billions of dollars from AMT payments by individuals needs to be obtained from other sources. This may be achieved by the following methods:
  - a. Changing the marginal tax rates to their prior values at minimum
  - b. Establish a federal consumption tax. In order to mitigate the regressive effects of this tax on low income families, provide additional income tax relief to people in this group.
  - c. SIMPLIFY! The simplest solution is almost always the best solution and the correct solution. Any lack of coverage by a simplified tax code will be more than made up by the billions of dollars that will be saved by administering a complex tax code, the decrease in worker productivity that occurs when individuals spend many days trying to figure out the best tax strategy, the corresponding loss of tax revenue as companies earn less when the employees are less productive, and anecdotally, the hundreds of millions of dollars that are unnecessarily paid to tax preparers that are required to prepare complex tax returns.

I respectfully and urgently request your support of H.R. 3385.

Gerald M. Marx

Boca Raton, Florida 33432  
August 31, 2005

Honorable Chairman William M. Thomas and House Ways and Means Committee  
Dear Chairman Thomas and Committee Members from the Florida 22nd Congressional District:

I was an employee of Qtera, in South Florida, of one of the many acquisitions of Nortel Networks during the telecommunications boon of 1998 to 2000. I received incentive stock options and subsequently have paid to the U.S. Treasury Department, Alternative Minimum Tax, in excess of \$230,000.00.

I was hired as the 17th employee in 1998, three years after completing a Bachelors degree in Mechanical Engineering. Working for Qtera, in Boca Raton, FL, was a fantastic experience. The team that was assembled was of the highest quality and some of the most motivated individuals I have ever worked with. Our devotion, hard work and technical expertise made us an acquisition target of both Cisco Systems and Nortel Networks in late 1999, Nortel Networks ultimately acquired us; seventy employees had achieved the impossible. Instantly, all our Qtera ISO's were converted to Nortel Networks ISO's at approximately \$60 per share. Our success received a wealth of media coverage, from the Wall Street Journal to NPR.

Soon after the media broke the news of our success, the stockbrokers and investment bankers began courting our employees. As employees with much work ahead of us, we had little time or energy to learn about the Alternative Minimum Tax

code. Some of the investment firms provided seminars on the Alternative Minimum Tax code but usually we were left with more questions than answers. AMT soon became the number one discussion topic, on the surface, we found ourselves quite versed in the subject, yet few of us really understood the dirty details.

My plan was to exercise and hold the shares as Congress had intended then after holding the stock for a year, sell enough shares to pay AMT and invest the rest. The first sign of trouble was the gradual decline in Lucent's stock price during 2000. We continued working incredible hours to meet our company milestones during our one-year transitional period.

By the middle of 2000 many employees had stockbrokers managing their investments. Not only brokers, but accountants, estate planners and life insurance brokers, everyone was after our potential wealth. I retained a local accounting firm to manage my tax liability and a nationwide brokerage house to manage my account. The accountants were confident they were experienced with Alternative Minimum Tax. Their experience turned out to be limited, but since they had fifteen of my co-workers on a yearly \$4,000 retainer, they had no problem getting their hands dirty with the tax code. I reasoned that the Alternative Minimum Tax code was so complicated that I should have professional support, no matter the cost.

April 15th 2001. The year had gone so quickly and I exercised options twice during the previous year resulting in an Alternative Minimum Tax on "Paper Gains" of \$195,000.00. It was strongly suggested, by my investment broker, use margin to pay the tax bill. The margin loan sounded like a reasonable idea, the investment firm provided a low interest loan without liquidating the account, as long as the account value is not less than the loan. Little did I know the bottom was about to drop out.

I began to diversify my account, but the majority was still in Nortel stock. Meanwhile, while no one was watching, Nortel stock fell below \$20 per share. The Nortel management was positive on the company's growth and their overall market position, the low price was just a small correction in the overall market. (We now know these earnings were inflated.)

By summer of 2001, the margin debt was nerve-racking and I was forced to sell Nortel shares and diversify as the share price continued to slide. I began to exercise and sell, just to raise cash for the 2001 Alternative Minimum Tax. Nothing could stop the hemorrhaging stock price or margin calls. The tax models the accountant had prepared last year were useless. My only concern was having enough cash to pay the AMT and pay off the margin debt. By the end of 2001, we got word that Nortel would soon be downsizing their operations in Florida. Nortel Networks needed to reach the "break even point" and the cutbacks began. By the third quarter of 2001, the share price was under \$10 and Nortel was laying off two thirds of their worldwide workforce.

April 15th 2002. I had paid estimated tax throughout the year, in hopes of making the April payment manageable and avoiding penalty fees. Each of those quarterly tax payments went on the margin loan. By April 2002, I reached my personal debt limit and liquidated my account to pay off my debt and pay the AMT. The 2001 tax bill was only \$37,000.00, a few thousand less than my yearly salary! I ended my contract with my accountant, sold 90% of my investment account, and prepared myself for the possibility that I too would soon lose my job. My fears were realized and by the second quarter of 2002, I was unemployed.

I learned many valuable lessons through this experience and I am fortunate that I am not financially ruined like so many of my former colleagues. Many will have their wages garnished, or have filed for personal bankruptcy, some were fortunate enough to negotiate settlements with the IRS. The Alternative Minimum Tax code was implemented to prevent wealthiest 2% of Americans from using special tax benefits to pay little or no tax. For various reasons the Alternative Minimum Tax has reached many hard-working, middle class Americans in South Florida 22nd Congressional District, some who don't have very high incomes or special tax benefits. I hope those in the United States Congress have the compassion and foresight to realize the growing negative effect of the Alternative Minimum Tax and bring change to the outdated tax code.

Timothy Masters

Austin, Texas 78736  
August 31, 2005

Honorable Chairman William M. Thomas and House Ways and Means Committee  
Washington, DC

Dear Honorable Chairman Camp and Ranking Member McNulty:

I have previously submitted 6/05 to the Ways & Means Tax Reform Hearing.

I now wish to share my story directly with you in hopes of garnering your support and leadership of the Honorable Sam Johnson's H.R. 3385.

Our three children, and I, along with my wife Julie have been seriously impacted by the Alternative Minimum Tax (AMT) that I had to pay due to the exercise of stock options. The AMT laws pertaining to Incentive Stock Options are unfair and I would venture, unconstitutional. I appreciate the time you and the Committee are taking to review this matter, and would ask that you consider changing this seriously flawed and unjust law of the tax code. I also ask that you consider doing what's right for those already impacted, a large majority of which, was caused by the "perfect storm" when the market went south in 2000.

I, personally, consider myself one of the lucky ones. . . . I have the possibility of actually recovering the AMT amount paid in over my lifetime, if everything works out, and even though it's having a direct impact now on our lives, it could have been worse. Thank God I only exercised 346 of the 512 stock options I was originally going to! Even with this stated, I am personally writing for those who have had their lives turned upside down. It's devastating to hear some of these stories! Single mothers who are janitors owing hundreds of thousands of dollars . . . just because they listened to their tax accountants, the IRS and a poorly written policy, called AMT. This belittles the ~\$35-\$40,000 (52.55% affective rate) difference the AMT law made on my tax bill (\$29,355 in actual taxes owned + the amount I would have got back, had it not been for the AMT "law").

My story starts back in the middle of 1996. I had a prior job with a retirement benefit that I received. As I was struggling to make ends meet while supporting my wife (who's presently disabled) and three children (two of which were from my wife's prior marriage, and at that point, had received NO child support. I loved my family then, and do to this day, so it was just one of life's struggles we have to deal with), we had to roll over the retirement account to a standard IRA. Around 1999, I found out about the ROTH IRA, and as things were looking better with my job and our finances, it sounded like a good item to move towards looking into our future. We realized it would be a struggle to pay the taxes on it, but were going to deal with that hardship to invest in our future retirement. So in early 2000, things were looking like we could finally pull off coming up with the taxes at the end of that year, so we converted the IRA to a ROTH IRA. In Feb. 2000, when our companies stock was doing well, I contacted some tax accountants and made several calls to the IRS regarding exercising my stock options utilizing the 83-b, so I could lock in the tax benefits. Things were really looking up and we were highly encouraged to invest in our company by management, and so I did. All my calls to the IRS didn't really amount to much as hardly anybody knew about the Form 83-b, but the basic information they kept telling me is that it's a huge tax benefit. I'd only have to pay long term capital gains tax on the options exercised, as long as they weren't sold for a year (even the options which hadn't vested yet, and wouldn't until even the latter part of 2001). As the markets kept dipping and our stock started taking a dive (much later than most in that year), and I started hearing more mentioned about the AMT tax, I started looking into the AMT implications. I had at least 20 conversations with the IRS themselves, along with consulting with two different tax accountants. NONE of them really knew of this area of the tax code, and ALL called it a "**very gray area.**" Many times, the IRS would have to escalate up the ladder to a more knowledgeable expert in that area. I NEVER did get any real information from ANY of them other than "**it's a gray area.**" If the IRS couldn't tell me about the ISO-AMT laws, who could???

At the beginning of 2001 I continued to keep placing calls to the IRS to find out exactly how my options will be taxed and what or how AMT would apply. I finally got a copy of some tax software after I couldn't get answers to my questions from either the IRS or the tax advisors I was working with. Well, I couldn't believe my eyes when I plug my numbers in. I then made many more calls to the IRS. Finally AFTER the 2000 tax year was completed, some of these "gray areas" start turning into answers. They went something like "Oh, I just had to look into a few of these last week and the IRS has started publishing more/better information on these 'gray areas.'" To my amazement, now that the tax year is over, the IRS had finally got specific, but by now, it was too late for me to do anything. It was a blow that I

couldn't ever have expected, nor believed that there was any constitutional way that I could be liable for this kind of tax. **It meant that we were to pay tax on money we would NEVER receive. It meant that for a \$2 stock option, I was going to have to pay almost \$24/share in taxes . . . yet the value of the stock was only a small fraction of that. EVEN THOUGH I COULD SELL THE STOCK FOR A PROFIT OVER THE \$2 GRANT PRICE, I STILL HAD TO PAY TAXES IN AN AMOUNT THAT MEANT I LOST MONEY. How can you pay taxes on stock that you NEVER saw a gain from???**

Now, comes the real shocker . . . so this is a pre-paid tax . . . I'll just be able to get the tax money back I paid when I file my 2001 taxes, and pay off the money I owed the IRS. . . . NO SUCH LUCK! This law is written to where the only way you could do that is OWE a huge amount of AMT tax again the next year. I will probably NEVER owe AMT tax again (so I thought) in my life . . . now that I'm reading more about it, I find even that may not be true.

**So, here I am, I bought exercised the stock, NEVER sold it and now I have this HUGE debt, with an effective tax rate of 52.55%** (it's realistically higher, as I didn't get back the \$\$ I should have), and am expected to live on that. My disabled wife needed a different used car as hers was becoming undependable with over 130,000 miles on it, I couldn't afford that, I couldn't afford anything I worked for. The IRS kept charging me penalties and interest on my AMT bill, and so I finally had to go into serious debt by borrowing money off of my credit cards to pay off the IRS to get them off of my back.

Now, I went from thinking I could actually do something nice for my family and take our first real vacation, to being horrifically in debt! Something's wrong here. . . . I'd previously in my life worked two jobs for almost two years (putting in 70-100 hrs a week), to get myself where I didn't have to worry about serious debt (mostly due to a robbery), and now because I worked hard and my company attempted to reward me, I'm in the worst shape of my life! I didn't try to get out of the taxes I truly owed . . . never have, never will. But, why isn't our government treating me the same exact way? George Washington would be turning in his grave if he knew about this. **Hard work in this country is supposed to be rewarded, not a punishment. I worked hard for everything I have, never getting any handouts, nor expecting them. I just want my country to treat me fairly in the same manner, as it should treat ALL in this country that way.** Please correct this injustice . . . if not for me, but for ALL citizens, especially those such as the hard-working single moms who have been blindsided so hard by a lack of information and poor tax laws and interpretations of them. Please repeal AMT retroactively, and replace it with something that is TRULY FAIR.

I was about to stop there, but wanted to add one more piece I think you should know about . . . this isn't just about money here . . . this law is putting a serious strain on people's health too. I try to avoid thinking about AMT as much as I can. . . . It gets me literally sick every time I think of it. This was hard once again to write to try to have some action taken on this subject. I knew what would probably happen . . . but I had to write anyway. **I've NEVER felt so strongly about a law so much in my life . . . don't get me wrong, I have strong moral values, and feel there are many which could be improved upon, but this law, I feel, is just plain robbery.**

I respectfully and urgently request your support of H.R. 3385.

Steven D. May

Fallbrook, California 92028  
August 17, 2005

Dear Honorable Chairman Camp and Ranking Member McNulty:  
House Ways and Means Committee

Dear Chairman and Members:

I respectfully and urgently request your support of H.R. 3385 as my wife and I are among other Americans who have been hugely impacted by the Alternative Minimum Tax (AMT) and its treatment of Incentive Stock Options (ISOs).

In 1998, I joined a Silicon Valley software startup. Within 18 months, I exercised incentive stock options and we were instantly "millionaires" on paper. Unfortunately, our stock value plummeted in 2001 with the rest of the NASDAQ. As a result of the AMT, however, we were still liable for nearly \$300,000 in federal income

taxes and approximately \$75,000 in state taxes based on the value of the stock at exercise. Given the dramatic fall in the value of the stock, we were unable to pay the liability in full.

Over the next 3½ years, we tried to reach a reasonable compromise with the IRS on the remaining balance, but our offer in compromise (OIC) with the IRS was rejected, as was our appeal of the rejection. Most recently, at great family hardship, we did a cash-out refinance of our home and liquidated all of our remaining assets to come up with \$262,000 (which included \$187,000 in federal tax and \$75,000 in penalties and interest) to pay the balance of our year 2000 taxes.

My wife and I are now starting over financially due to the AMT. I am 47 years old and the first of my two teenage children will enter college next year, which my wife and I are committed to fund. Given that the AMT has depleted all savings, investments, 401ks, college funds, etc., we plan to cash flow our children's education over the next 7 years and then at age 54, we will *begin* to re-save for retirement.

Please help us, and quickly. We are hopeful that our Leadership will recognize that the AMT and its impact on families like ours is unfair and distorted. We are also hopeful that new legislation, specifically ***H.R. 3385; AMT Credit Fairness Act***, will soon provide relief for families in our situation. **The ability to apply our AMT credits against normal income and tax events would allow us to regain some of our financial security.**

Sincerely,

Steve Mazingo

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**The Honorable Michael McCaul, Representative of Congress from the State of Texas**

Mr. Chairman, I would like to thank you for allowing me the opportunity to submit my thoughts for the record on the Fair Tax Plan. I would like to commend Mr. Linder for his leadership on this very important issue.

The income tax has been a permanent part of the American tax system for ninety-two years. Increased government spending has resulted in such a steep income tax rate that a significant amount of the average hard-working American worker's salary never even reaches his or her pocket. As a conservative, I believe that the American taxpayer is a better judge of how their own money should be spent, and not the government.

Mr. Linder's plan would permanently abolish the income tax and replace it with a national sales tax. His plan would allow workers to receive one hundred percent of their earnings in their paychecks, giving them the right to decide how best to use all of it. American's will pay taxes based on their personal consumption of products, as opposed to how much the government chooses to take from them based on what they earn through their hard work. Taxpayers will save thousands of dollars and hundreds of hours a year by simplifying this process. No more confusing tax forms, no more costly tax compliance. Additionally, our government will save millions of dollars in collection costs and enforcing taxpayer compliance. The fair tax is most, and perhaps only, efficient way to collect federal taxes.

Many tax proposals will be reviewed in the coming months by your Committee. I strongly urge the Committee to adopt the fair tax model for fundamental tax reform. The economic benefits this plan will bring for the country and cost savings for the government are undeniable. It is time the government stopped carving up taxpayers hard earned paychecks and started allowing working Americans to keep their own money.

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Catonsville, Maryland 21228  
August 26, 2005

Dear Honorable Chairman Camp and Ranking Member McNulty,

We have submitted our testimony and shared our story at these following events:

6-15-2004, Hearing on Tax Simplification, Oversight Subcommittee  
9-23-2004, Hearing on Select Tax Issues, Select Revenue Measures Subcommittee  
6-08-2005, Hearing on Tax Reform, Full Committee  
April/May 2005, Senate Finance Committee Chairman Grassley  
Spring/Summer 2005, President's Tax Reform Advisory Panel

We now wish to share our story directly with you in hopes of garnering your support and leadership of the Honorable Sam Johnson's H.R. 3385.

My name is Rita Miller and I am writing on behalf of myself and my husband, Arthur, regarding a huge tax debt that we incurred on phantom gains that were created by the application of the Alternative Minimum Tax. We submitted our testimony previously, but we are respectfully requesting your support of H.R. 3385.

In November 1997, I took a job in Linthicum, MD as an Administrative Assistant for a start-up Internet security company, VeriSign, Inc., whose headquarters is in Mt. View, CA. We incurred a huge tax debt starting in the year 1999 by exercising Incentive Stock Options (ISOs) I received while working for VeriSign, Inc. We held some of the stock. We didn't realize ANY profit from the exercised, unsold stock. We just took the stock from VeriSign and put it into our newly created stock brokerage account.

We have always been in the lower portion of the middle class income bracket. We never owned even one share of stock before. We thought the stock market was for the rich and famous. For that matter we never really ever had a savings account. We raised three sons while just making ends met. But now it had looked as though the all-American dream might be coming true for us. We now had a vehicle to change our financial position and the ability to really be able to save for retirement. I am 56 years old and my husband is 58.

We read everything we could about stocks and taxes and everything pointed to exercising and holding the stock for long term capital gains. We enlisted the help of a reputable financial advisor. The advice from the financial advisor was to exercise and hold the stock so as not to incur the higher short-term capital gains rate. And we did—we held the stock. But unbeknownst to everyone, if you exercise and hold onto stock for the long term and carry it over a tax year, a tax called AMT (alternative minimum tax) can apply, and it did.

We were taxed on the value of the stock on that particular day we exercised them. On some of those days the stock traded as high as \$220. We were taxed as if we sold the stock that day and made a profit. We didn't sell the stock at \$220. We didn't receive, as it would appear, the huge profit on those shares of stock, but we were being taxed as if we did. Taxed on "phantom income." As if we had the monetary gains sitting in a bank account somewhere. That was not the case.

All other assets, like real estate and stock purchased on the open market, are taxed based on the value at the time of the sale, when you actually receive a profit, not at the time of the purchase. Why aren't we just taxed when, and if, we sell the stock? That then would be a *legitimate profit made* and a *legitimate tax due*.

Our total federal taxes due from the years 1999 through 2002 was \$448,873. We managed to pay \$314,784 by selling whatever shares of stock we had. During the year 2000 when the stock market started to plummet, so did the value of our stock. When we sold the stock the prices ranged from \$34 to as low as \$9. Keep in mind that the original amount of \$448,873 was the tax due based on the stock trading at an average \$220 per share. As you can see I didn't sell it for \$220 but I'm being taxed as if I did.

This is not even to mention the amount that we owed to the state. We negotiated with the IRS and went on a payment plan to pay the remaining \$134,089, likewise with the state. We never missed a payment until both my husband and I lost our jobs within a few months of each other in the year 2002. I was unemployed for over a year, my husband is still unemployed.

We requested an OIC and the IRS rejected it—stating that we had a house, a car and some retirement money and if we sold the house, the car and turned in the retirement, we could pay the "phantom taxes" we owed. We came to realize that after filing subsequent years taxes, the IRS now "owes" us \$124,297 in credits for actual overpayment of taxes. We immediately filed another OIC. We offered \$8,002 along with the credit of \$124,297 that the IRS admits was an overpayment of taxes bringing our tax debt to a "paid-in-full" status. Can you imagine our disbelief when we received the notice that the IRS is rejecting this offer too? The IRS wants us to pay them first, then they want to give us back the \$124,297 of "overpayment" by allowing us to recover a small portion, approximately \$3,000, of the credit per year! My husband and I will have to reach the age of 99 and 97 respectively to recover the entire amount of the overpayment.

A travesty just occurred in our lives that added additional hardship. My husband, who has been unemployed since August 2002 and has spent more than a year of processing for employment with the Department of Defense was just notified that the DoD is withdrawing his offer of employment due to the outstanding IRS debt. They said that the tax issue brought into question his credibility—but we only owe this tax because we were honest enough to report our exercise of the stock options in the first place. At almost 60 years old where is he going to find another oppor-

tunity like the one with the DoD? We are hard-working, trustworthy and honest people. We have never avoided paying taxes and have always engaged in honest financial practices. We understand the AMT was put into place to make sure that the very wealthy people paid their fair share of taxes, but it's not working the way it was intended. There has to be some consideration for people like us, those of us that were caught in the AMT trap.

Whenever you tell anyone the details of our situation they are appalled. They say that's impossible. It just couldn't be. Well it did and we have been living a nightmare for over 3 years with daily fear that one day when we open our mailbox there's going to be a letter there from the IRS stating that they are taking our home, the one that we worked all our life for.

We respectfully and urgently seek your support of H.R. 3385.

Rita & Arthur Miller

Las Vegas, Nevada 89149  
August 26, 2005

Dear Honorable Chairman Camp and Ranking Member McNulty:

I have submitted my testimony and shared my story on a number of occasions in the hope something can be done to fix a travesty in the tax code. I now wish to share my story directly with you in hopes of garnering your support and leadership of the Honorable Sam Johnson's H.R. 3385.

My name is Niell Montgomery. I very much appreciate the opportunity to tell my story of suffering and hardship brought on by the application of the out of date and destructive rules for the treatment of Incentive Stock Options under the Alternative Minimum Tax (AMT) code.

My difficulties and those of thousands of others were brought about by events never contemplated when the AMT was devised, i.e., the significant negative tax impact that happens with stock options when a company's stock price experiences a dramatic decline. At the risk of being too basic, please allow me a brief explanation of stock options. A stock option is the right to buy a share of stock at its current price (the strike price) at some time in the future. Non-Qualified Options (NQOs) and Incentive Stock Options (ISOs) differ in their tax treatment. I'll talk first to ISOs. When the option holder exercises the right to buy (obviously the current market price exceeds the strike price), they create an Alternative Minimum Tax (AMT) taxable event. The AMT treats the spread between the option strike price and the stock price when the option is exercised as income (otherwise called "phantom" income). That is, even though there's no tangible income, a tax consequence occurs non-the-less. Now to be fair, when the AMT exceeds the regular tax owed calculation, the taxpayer gets a credit against taxes in future years (the credit's application is complex and can take years if ever to recover). A subsequent sharp decline in stock price does not alter the tax owed even if the stock price goes to zero.

When the tech bubble burst, huge numbers of share owners were left with tax bills resulting from the AMT treatment of ISOs while their shares had become nearly or even totally worthless. Remember, the real value of the stock has nothing to do with taxes owed. What was supposed to be an "incentive" and accepted in lieu of cash compensation turned into a tax nightmare (an obligation to pay taxes where no income/gain was realized). People were forced to mortgage/sell their homes, take out loans, or sell whatever they could to pay these absurd tax bills. It seems *incomprehensible the IRS would enforce such harsh collection measures for tax dollars that become a credit in the taxpayers account.* This AMT tax treatment is complex and unfair and has caused untold financial hardship, ruin, and heartbreak. Side note: how does the government account for these prepaid taxes?

The tax treatment for NQOs is even worse. Tax law requires the treatment of the NQO as an income event at the time of grant. The income results from the difference between the strike price of the option and the stock price on the grant date. This is without regard as to whether the NQOs are even exercised and, if they were, whether or not the shares were sold. Again, in a market such as we've experienced, a decline in the price of the stock is just a personal misfortune. The tax is owed even if the stock price goes to zero.

Looking at the larger picture, I'm not sure anyone can assess the positive impact the awarding of stock options has had on our economy. I know their use has been widespread and it's my opinion they've been a significant factor in holding down wages and inflation. Thousands of employees had been willing to accept below mar-

ket wages in exchange for options. The belief was that by working hard and making their company a success, they'd have a share of that success. Unfortunately, for many, it didn't work out that way. If the negative tax treatment of stock options isn't fixed, their use as an incentive and benefit on holding down wages will be lost.

Now for my story. By way of background, I worked 31 years in the telephone industry starting at the lowest entry level job and working my way to General Manager. In 1993, I left a good paying job to become an "entrepreneur." Two years later, I founded MGC Communications. Having worked my entire career in large impersonal corporations, I thought it was important that our employees be owners as well. We accomplished that goal by granting stock options to everyone who joined the Company. At the most senior level, we were able to hire very qualified people at compensation levels below market rates by sweetening employment packages with stock options. As a young Company, it was essential we conserve our cash. Since salaries and bonuses represented such a significant portion of on-going cost, the use of ISOs was an effective way to do that. ISOs also incented our employees, as owners of the Company, to really apply their talents to building the business.

As the most senior officer/leader of the Company, I was committed to and embodied these goals. In lieu of a salary more typical of my position (my successor's annual salary was \$500,000), mine was \$150,000 with ISOs as additional compensation. In lieu of cash bonuses (my successor's annual bonus was \$500,000), I took ISOs. Little did I know of the tax nightmare lying ahead.

Unlike many victims of this cruel conspiracy of events, I had access to good tax planning help. My personal banker was with one of the largest public stock firms in New York. When he didn't have answers, he had the best talent available to him in the corporate offices. My accounting firm was one of the big five national firms. Like my banker, when they needed help, they turned to specific experts on their corporate staff. Yet with all this knowledge and talent, none of them really understood the complex treatment of options within the AMT.

Here's what happened in my case. When I exercised my options in early 2000, the stock priced was \$66 per share. Since the options had been granted in the early days of the business, the strike price for the options was very low. When the spread was calculated and the AMT rules were applied, I owed an additional tax of \$4,400,000. Within six months of exercising my options, the stock had lost 90% of its value (the Company eventually declared bankruptcy). While the intended holding period for ISOs is one year, I was forced to sell shares sooner to raise the money to pay the taxes. To further compound the situation, I owed taxes on the shares being sold. In the end, I sold all the shares acquired thru options to pay the AMT and still ended up \$200,000 short. I have said many times jokingly, if the IRS would have accepted everything I owned in the Company in exchange for the AMT owed, I would have been money ahead.

All I have to show for founding the Company, creating thousands of jobs and building a good business is a substantial tax bill; a tax bill that resulted from a purchase event. I understand and accept the tax consequences when there's a purchase and sale which results in a net gain. What I reel at is the application of a 28 percent tax on the purchase of stock as though some form of gain had been realized. This is a virtual sales tax! And, as noted earlier, the tax code is so complex it was/ is impossible to find anyone sufficiently knowledgeable to provide accurate tax planning.

As I've talked to other people similarly situated, I've realized how pervasive this problem is. I also discovered there are three ways in which taxpayers deal with this issue. The first group, like me, reported the exercise event and faced the tax consequences. The second group knew they should report but chose not to. Since there's no reporting/tracking mechanism, the IRS doesn't know there's been a taxable event. The third group just didn't realize they had to report. Of the three groups, I believe those who reported were in the minority. One of the fundamentals of our tax code is the fair and uniform application of the law. Clearly that did not happen here.

As for reform, here are some ideas. Change the AMT formulas so this kind of injustice doesn't happen in the future. Those of us who have credits, at a minimum, make the credit directly applicable to all future taxes owed and not just a factor in the AMT calculation as it is now. At the extreme, send us a check equal to the credit (that would be a real "rebate"; these are real dollars we've paid in excess of what we would have otherwise owed). And if you must hold our money, at least pay us interest at the rate the IRS charges us for late payments. It is absolutely absurd that our prepayment of taxes is a free loan to the government. Finally, if the AMT must continue, please insure it is indexed down proportionate to the regular tax rate schedule.



As for the tax treatment of NQOs, stop treating the event as income at the time of grant. Taxes should be owed when income/gain is realized. That means determining taxes owed when the stock is sold. I would agree a portion could be treated as income and the change in subsequent stock price as a long/short term gain/loss.

If I sound like a tax professional, I'm not. I'm one of the thousands of people granted options only to have this tax nightmare. I've become knowledgeable by default! I just couldn't believe I'd owe taxes for options granted when I hadn't received income or realized a gain. In hindsight, I would have been so much better off to have taken the pay instead of the options. I know thousands of others feel the same way (not a scenario that bodes well for business and our economy). At least I'd have the income to pay the related taxes. We need your help; fix this grave injustice!

I respectfully and urgently request your support of H.R. 3385.

Nield J. Montgomery

Cupertino, California 95014  
August 20, 2005

Dear Honorable Chairman Camp and Ranking Member McNulty:

I have submitted my testimony and shared my story at 6-15-2004, Hearing on Tax Simplification, Oversight Subcommittee.

I now wish to share my story directly with you in hopes of garnering your support and leadership of the Honorable Sam Johnson's H.R. 3385.

My name is Kimhoe Pang. I am a software engineer of Network Appliance. I exercised some stock option in year 2000 under the Incentive Stock Options (ISO) scheme. I did not sell any of the exercised stock to get profits. The ISO exercise created a huge AMT tax. I have \$367,684.00 tax due in 2000. The amount is more than 3 times my annual salary. This tax payment actually becomes a credit and can never be recovered by me. In essence, I can lose all the investment money, and also other assets, simply to create a tax credit in my IRS account.

Due to the stock crises in 2000, I did not have enough money to pay tax. I filed an Offer in Compromise (OIC) and the OIC was denied after two and half years. IRS has started the collection process and has put a lien on all my properties. I am the only one who brings income to my family. My family (five people) still live in a two bedroom rented apartment. However, the IRS officers told us that they were only concerned about the tax we have not paid. They are regardless about the fairness of the tax.

We are still facing financial crisis. IRS already started collection process. We have to pay the huge tax that is based on the profit we never made.

I respectfully and urgently request your support of H.R. 3385.

Sincerely,

Kimhoe Pang

Newnan, Georgia 30263  
August 6, 2005

Committee on Ways & Means  
U.S. House of Representatives  
1102 Longworth House Office Building  
Washington D.C. 20515

Dear Chairman Thomas and Members:

My wife and I ask the Committee to report favorably on H.R. 25, the Fair Tax proposal by Rep. John Linder of Georgia.

We support the elimination of the income tax, the IRS, and the current harmful tax code.

We support a national retail sales tax with a prebate to every household of a portion of estimated sales tax payments.

Thank you.

Sincerely,

Kimball L. Peed

Issaquah, Washington 98027  
August 24, 2005

Honorable Chairman Camp and Ranking Member McNulty  
House Ways and Means Committee

Dear Honorable Chairman Camp and Ranking Member McNulty:

I have submitted my testimony and shared my story at the following events:

- 6-15-2004, Hearing on Tax Simplification, Oversight Subcommittee
- 9-23-2004, Hearing on Select Tax Issues, Select Revenue Measures Subcommittee
- 6-08-2005, Hearing on Tax Reform, Full Committee
- April/May 2005, Senate Finance Committee Chairman Grassley
- Spring/Summer 2005, President's Tax Reform Advisory Panel

I now wish to share my story directly with you in hopes of garnering your support and leadership of the Honorable Sam Johnson's H.R. 3385.

In 1997 I went to work for a new Internet company, Exodus Communications, who granted sales employees pre-IPO stock shares upon hiring. After the IPO and some time of employment I hired a financial planning firm to advise me on how to best handle these options. I was advised to exercise the options as they became available and then hold for one year from that date before diversification. I took this advice. During this time between 2000 and 2001 (within several months) the stock fell from the high \$100s per share to landing at less than \$10. I was laid off in May of 2001 when we finally sold our shares at \$.10 after Exodus's bankruptcy.

I was laid off just before Exodus declared bankruptcy and found myself unemployed for 7 months. Meanwhile, we had to sell our house and all other valuables to make it through this period financially. My husband had quadruple bypass surgery unexpectedly in 2001 causing further financial difficulty and personal stress. We have not recovered from the financial challenges that losing my job, stock value and medical bills caused our family, not to speak of the outstanding balance expected by the IRS for AMT fees.

Since 2001 we have been attempting to work with the IRS as the amount they calculated we owed them based on the AMT value is over \$600,000. As you can tell from this writing we incurred a huge loss on the "ownership" of these granted shares. The IRS denied our Offer In Compromise and has not proactively worked with us. We have retained counsel to help us try to avoid all collection issues with the IRS and had to borrow money exceeding \$15,000 to gain representation.

We have no means to pay the IRS and, of course, feel there is no real debt to re-pay. This has been going on for nearly 5 years with a lien on our credit and ongoing fees to attorneys to keep collection at bay. The next step is the IRS waves our fees or we must declare personal bankruptcy. This AMT situation seems completely unfair and not the proper application for its original intention. We join AMT reform in asking Congress to instruct the IRS to hold off on current collection efforts until new legislation can be addressed.

We respectfully and urgently request your support of H.R. 3385.

Bob and Susan Pessemier

Sunnyvale, California 94086  
July 25, 2005

Dear Ways and Means Committee Members:

*We strongly encourage the Committee's support of Congressman Johnson's recently introduced bill, H.R. 3385, to correct the existing inequities associated with individual taxpayers' ability to recover Alternative Minimum Tax credits. The current law makes it very difficult, if not impossible, for individual taxpayers to recover AMT credits, resulting in perpetual interest-free loans to the government.*

We are a two-income household (both with full-time jobs as individual contributors—not managers or company officers) with three young children living in California—a high-tax state, as you well know. Years ago in lieu of a higher salary, incentive stock options became part of our compensation.

As a result of exercising and holding (to qualify for the long-term capital gains tax rate) Incentive Stock Option (ISO) shares in 2000, we incurred a Federal AMT bill of several times our normal annual income. Luckily, in that year we sought and received sound advice on the AMT implications of that plan. Between doing same-day-sales in 2000 on remaining ISO shares and taking out a loan against a 401(k)

retirement account, we were able to meet our AMT obligation on April 15, 2001. Thus, we have not run afoul of the IRS and have not had to worry about losing our home, unlike many others who exercised and held ISOs during that time period.

With the large decline in the stock markets since 2000, the shares we still hold are worth a small fraction of their value upon exercise. So, at this point the government is holding our entire gain (representing many years of hard work) from the ISOs in the form of a large AMT credit. Please also note that for tax year 2000 we paid *(on shares that we purchased then, but have held for five years now)* at the AMT rate of 28%, while under the current law our long-term capital gains rate upon sale would be 15%. *The mandatory pre-payment of tax under AMT was at almost double the rate that the regular tax system requires!*

When we first saw the size of our AMT credit, we thought we would be lucky to finish recovering it before we both died of old age. After filing our last four tax returns, though, we see that unless something changes we will never recover the vast majority of that credit during our lifetimes.

Here is how much we've been able to recover, on a percentage basis, for the 2001–2004 tax years. (Note that our tax returns for these years have included no other extraordinary events.)

<b>Tax Year</b>	<b>% of AMT credit recovered</b>
2001	0.56%
2002	0.17%
2003	0.13%
2004	0.00%
Total	0.86%

***Less than one percent*** of our AMT credit has been recovered in the four tax years since the credit was established! And the trend down to zero in 2004 does not bode well for future years.

Under the current tax law we have very little hope of recovering this interest-free loan to the government. These funds would go a long way toward ensuring that we will be able to afford college educations for our three children.

*Please support Congressman Johnson's H.R. 3385 to accelerate individual taxpayers' ability to recover AMT credits!*

Thank you very much for your consideration.

Sincerely,

Steven and Danna Pintner

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**Statement of The Honorable Tom Price, a Representative of Congress from the State of Georgia**

Tax System Reform unites the American people unlike any other. Everyone can agree that reform is much needed and long overdue. Reducing the onerous burden imposed by an overly complicated tax code that creates enormous compliance costs for American citizens and businesses should be a priority for Congress.

The current U.S. tax code numbers over 10,000 pages, 600 forms, and 16,000 lines. If that is not complicated enough, those who call the Internal Revenue Service get correct answers to their questions only fifty-three percent of the time.

The purpose of this letter is to urge the Committee on Ways and Means to support the FairTax proposal which would create a National Retail Sales Tax. The goals of the FairTax are consistent with responsible goals for our tax structure—fair, simple, and efficient. Americans deserve and desire a tax system that encourages savings, a tax system that is void of loopholes, and a tax system that is no longer subject to the influence of special interest groups. The FairTax meets these objectives by eliminating the income tax in its entirety and replacing it with a consumption tax on spending for new goods and services.

The FairTax is more equitable than our current tax system because it is based on what one spends over a lifetime, not what one earns in a given year. Furthermore, the FairTax has a rebate component so as not to burden the poor, the elderly, or those on fixed incomes.

The FairTax rebate was created in part to eliminate the tax that Americans pay on the purchase of necessities. In fact, the FairTax is the only proposal, including current law, that completely “untaxes” the poor by (1) eliminating the payroll tax, a highly regressive tax that only targets wages, (2) eliminating hidden federal taxes, corporate taxes, income taxes, and payroll taxes that businesses pass on to consumers in the form of higher prices, and (3) assuring that no American pays taxes on spending up to the poverty level. The rebate feature of the FairTax assures its progressivity and, in fact, makes it the least regressive viable system.

One reason our current tax structure is more regressive is that it deters people from saving. Currently, national savings is at the lowest rate in the history of our country. The FairTax is applied only when consumers spend, not when they save or invest. Saving and investing creates economic wealth not only for ourselves, but also for others. Dale Jorgenson of Harvard University predicts that in the first year under the FairTax, invested capital will rise by 80 percent over projected levels under current law. Over the first decade of the FairTax, the savings rate will level off to 20 percent more than under the current system. This effect will result in a higher standard of living for both those who save (invest in others) and those who work for wages (because the market value of their work will be increased by investment). The value of capital will increase because their buildup is not taxed, and the level of real wages will rise because of the rise in real investment.

Under the FairTax, the United States will become the most attractive industrialized country in the world in which to base production facilities because we will be the only nation with a zero rate of taxation on profits. As a consequence, American overseas investment can be repatriated and direct foreign investment will flow to our shores.

Perhaps the most basic benefit of the FairTax system is that it simply costs far less—about \$225 billion (90 percent) less—to collect the same amount of revenue as the current income tax. Research shows that Americans spend an estimated \$250 billion a year just complying with the current tax code. That’s \$888 per year for every man, woman, and child in America or nearly \$2,800 per family—\$2,800 that would be better spent on education, a mortgage payment for a new house, or a more secure retirement.

The simplicity of the FairTax makes enforcement easier and evasion harder by allowing us to focus resources on fewer filers and by lowering the total number of tax filers from 212 million to only 14 million (retailers). By eliminating loopholes, the FairTax also keeps the tax base broad and marginal tax rates low, dramatically more than any other tax proposal or current law. This reduces the potential gain from evasion and therefore reduces evasion temptation. The elimination of exceptions also decreases the ability of government to pick winners and losers through tax code enticements, thereby unfairly gaming the system. The FairTax would save money by collecting the current level of revenue in a more efficient way.

Please give your serious consideration to this common sense solution to the challenge and need of fundamental tax reform—the FairTax is the answer.

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**Joshua Pritikin, Santa Barbara, California**

I support H.R. 25, the FairTax.org proposal.

The rationale for this bill is already well explained with others, such as Jonathan Steere of Maryland. With this letter, I merely add my support.

Thank you.

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National Taxpayers Union  
Alexandria, Virginia 22314  
*August 9, 2005*

The Honorable E. Clay Shaw, Jr., Chairman  
Subcommittee on Trade  
Committee on Ways & Means  
U.S. House of Representatives  
1102 Longworth House Office Building  
Washington D.C. 20515

Dear Chairman Shaw:

On behalf of the 350,000 members of the National Taxpayers Union (NTU), I write to offer our thoughts on a bill currently being considered for inclusion in a

miscellaneous trade package. It is NTU's strong belief that H.R. 521, the Milk Import Tariff Equity Act, should **not** be included in this legislative vehicle.

Earlier this year NTU strongly condemned the introduction of H.R. 521, which would restrict the importation of milk protein concentrates (MPCs), casein, and caseinate by raising tariffs. As tariffs are nothing more than taxes on the flow of goods and services across national boundaries, NTU believes that this bill would both harm relations with our trading partners and place unnecessary financial burdens on American consumers who use everyday products containing MPCs, such as coffee creamer and infant formula.

In addition to substantive policy concerns with H.R. 521, NTU feels that the bill is simply too contentious for a legislative package that seeks to make technical corrections to U.S. trade laws. The Subcommittee listed "attract[s] controversy" as one of the criteria by which to reject bills for inclusion in the trade package, and since its introduction H.R. 521 has indeed proved to be an extremely controversial proposal. The already fierce reactions to H.R. 521 from various groups—the most important of whom are taxpayers and MPC consumers—would only intensify if the bill were inserted into what is supposed to be an innocuous legislative package. The provisions of H.R. 521 require further congressional scrutiny and therefore should not weigh down a technical trade measure.

Because of policy and procedural concerns, NTU respectfully requests that the Subcommittee refrain from adding H.R. 521 or any of its components to the proposed miscellaneous trade package.

Sincerely,

Kristina M. Rasmussen  
Government Affairs Manager

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#### Statement of ReformAMT.org, Foster City, California

#### To the Honorable Chairman Camp, Honorable Ranking Member McNulty, and the Honorable Members of the Select Revenue Measures Subcommittee:

Thank you for allowing ReformAMT the opportunity to communicate our support for H.R. 3385, the AMT Credit Fairness Act of 2005. This important legislation is addressing some aspects of the Alternative Minimum Tax (AMT) and its treatment of Incentive Stock Options (ISO). The average individual in our organization faces tax rates that exceed 300% of their income.

#### Introduction

Formed in April 2001, ReformAMT is a national grass roots organization whose mission is to educate, correct, and prevent the injustices created by the ISO AMT and its inappropriate means of taxing Incentive Stock Options, which are intended to be a form of compensation. We have members in 48 different states, plus Puerto Rico and the District of Columbia.

Through ReformAMT, we plead with Congress to support H.R. 3385 which helps to correct some aspects of this flawed tax code that has resulted in financial devastation for not only our members but also thousands of others across the country who are too embarrassed or discouraged to publicize their dilemma. Originally intended to "ensure that a very small group of high-income individuals who paid no income tax would pay at least some income tax," the AMT has hit hardest those honest, hard-working employees who traded longer work hours, lower salaries, fewer benefits, and job security for stock options that might someday provide for their children's education, assist in purchasing a home, or help fund their retirement. Unfortunately, caught in the AMT trap, these workers were forced to pay taxes on money they never received and never will receive. Consequently, they are losing or have lost their homes, education funds, and retirement funds.

These people were committed, dedicated, and loyal to their companies. "Hold for the long term," "be a part of the company," and "don't dump and cash in" was the advice of brokers, Certified Public Accountants, financial advisors, and the companies themselves. However, as we all now know, the Incentive Stock Option AMT provisions tax when you *buy*, NOT when you sell, forcing these workers to pre-pay taxes on stock gains they never realized. To add insult to injury, these taxpayers have honestly complied with this **self-reported** tax. While the IRS machine destroys their lives, they have watched many of their fellow coworkers go unharmed by simply omitting the reporting of the stock option transaction.

### Demographics

These are the results of a recent survey of our members in April 2005:

- 65% of our members affected by AMT are secretaries, engineers, lower level managers and other rank & file employees (as opposed to Managers, Executives and Founders).
- Our members owe or owed an average of \$322,428 in ISO AMT over and above what they would owe under the regular tax code for income received (that is *100 times* what the average taxpayer hit with AMT pays in additional taxes, according to testimony by the GAO at a recent Senate Hearing).
- Our members' average tax rate was 355% of their income.
- Our members have an average outstanding AMT credit of \$213,620 due to their overpayment of taxes. With the current annual deduction for AMT credits of \$3,000 per year, it will take 71.2 years—more than a lifetime—to finally recover their overpayment credit. Also, this credit does **NOT** accrue interest—on the flip side—individuals who still have outstanding liabilities are expected to pay interest and penalties on this tax prepayment.
- Because of the extreme difficulty/impossibility of paying huge taxes on money never received, about 3% of ReformAMT members have filed bankruptcy, with another 18% admitting they are considering bankruptcy.
- For every 2 people who complied with the AMT regulations, there were 3 people who did not, taking advantage of the fact that no independent reporting exists.
- For every 4 people who complied, there was 1 person who expatriated rather than have their lives destroyed by working the rest of their lives to pay taxes on income they never received.
- We know of 2 members who committed suicide due to the horrendous effects this ISO AMT tax had on their lives.

### Flaws of the AMT Treatment on ISOs that Distort Business and Personal Decisions and Create Unfair and Unjust Results for Hardworking Americans

- Prepayment Credit Flaw—The regular tax code provides significant incentives to hold on to the stock and grow the company. However, the AMT imposes tax on the purchase date, not the sale date, making the tax rational only in a bull market. In a down market, the AMT can result in unreasonable and totally disproportionate tax rates, easily exceeding an individual's income or even exceeding an individual's entire net worth.
  - ISO AMT credit can easily outlive a taxpayer, since it can be applied only to the difference between the AMT and regular income tax. For those who are ready to retire and who have responsibly saved their entire lives to provide for a proper retirement, the ability to recoup the credit can be impossible.
  - The credit that is generated does not pass along to your family or estate.
- The government does not pay interest on the credit.
- Complexity Flaw—Due to the complexity of the AMT, investment counselors and “tax experts” are frequently unable or unwilling to give proper advice to constituents about the consequences of the ISO AMT. Many people were completely blindsided by the AMT despite getting professional advice on how to treat their stock options.
- Reporting Flaw—The exercise of incentive stock options is not reported to the IRS by the company or by the broker—it is only reported by the individual, making it a self-reported tax. Thus, the ISO AMT provisions punish those who are honest and reward those who fail to accurately report their taxes under the AMT code (either through ignorance or intent).

### Unintended Consequences

In order to pay their AMT bills, taxpayers have been forced to liquidate much or all of their assets, including savings, retirement accounts, and children's college funds. Many have lost their homes. Some are forced to take out second mortgages and loans in order to comply with this pre-payment of tax. Others are forced into bankruptcy or expatriation.

Those who have attempted to resolve their outstanding liabilities through the IRS's Offer in Compromise (OIC) program have faced rejection after rejection. The offers often take years to resolve and result in unrealistic IRS demands, requiring the taxpayers to live at or below the poverty line. According to Nina Olsen's (TAS) 2004 report to Congress, only one OIC submission under the use of Effect Tax Administration (ETA) was accepted that year. The Tax Court recently upheld the IRS position on its refusal to consider the Section 7122 “equity and public policy” considerations of the offer in compromise process for ISO AMT, stating that while it sympathized with the taxpayers, the remedy rests solely with Congress.

The emotional and financial hardship caused by the AMT's treatment of ISOs has taken its toll on thousands. Marriages and families have suffered under the daily stress of dealing with the IRS; they have divorced, decided not to have children or to adopt children; their friends and parents watch in horror as their loved ones lose an entire life's work because of how the AMT can force them into pre-paying taxes on stock for which they never received gains (for individual stories, visit [www.reformamt.org](http://www.reformamt.org)). Meanwhile, those who did not comply with the law are leading their normal lives.

Aside from the obvious "un-American" treatment of imposing taxes based on no realized gain, the effects also reach beyond individuals and families. The ISO AMT provisions are destroying and stifling the productivity, innovation, and companies that contribute greatly to America's economic success and growth. It undermines confidence in the tax system, encouraging non-compliance. These effects cannot be what Congress intended.

#### **Request for Relief**

With the new bankruptcy laws going into effect in a few months, ReformAMT respectfully asks the Select Revenue Measures Subcommittee to support quick passage of H.R. 3385, a key component that will come just in time to prevent even more severe harm to honest Americans.

Our members are struggling with huge tax bills and IRS collections. They have pre-paid taxes from stock compensation for which they never received economic gain. Some of the companies whose stock was affected are now out of business. Our members are on the brink of financial ruin, suffering anxiety and depression that is so severe, it is destroying their daily lives. Please help us.

Thank-you for your time.

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#### **Statement of Robert W. Richards, Abilene, Texas**

Mr. Chairman, Ranking Democratic Member McNulty, and Members of the Subcommittee, I appreciate having the opportunity to submit my comments regarding reform of the Federal Tax Code.

As you have become aware during your hearings, the current Federal Tax Code has become a giant burden to individuals and business, not only in cost but also in trying to comply with thousands of pages of code and regulations. In 2003, there were 54,846 pages to the Federal Income Tax Rules, including the tax code, tax regulations, and IRS rulings. That is many more times the pages in the Holy Bible, War and Peace, Gone with the Wind, and The Complete Works of William Shakespeare (unabridged) combined. The goal of the Tax Reform Act of 1986 was tax simplification and tax reform, but the number of pages in the tax code in 1984 was 26,300. We have more than doubled the tax code since then! (Source: <http://www.cato.org/dailys/04-15-03-3.html>).

In my opinion, we do not need to just tinker around with the current income tax code. We need to scrap it. The Fair Tax Act of 2005 (H.R. 25), sponsored by Rep. John Linder of Ga., replaces the current individual, corporate, estate and payroll taxes with a national retail sales tax. I am sure by now you are well aware of this legislation. It has my full support.

I would hope that Congress would be bold in its reform of the tax laws. Please do what is right for this country and eliminate the beast that the current tax laws have become. Please pass the Fair Tax!

Thank you very much.

Robert W. Richards, CPA

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Allen, Texas 75002  
8/23/05

Dear Ways and Means Committee Members,

My name is William Rinehardt and I am writing on behalf of myself and my fiancée, regarding a huge AMT tax debt that I incurred on "phantom" gains due to the application of the Alternative Minimum Tax to incentive stock options (ISOs). I owed 124% of my taxable income in Federal income tax for year 2000. I owed more AMT taxes due to the exercise of my ISO shares than the market value of the shares when I sold them. I couldn't pay the AMT at the time. If I would have sold all my shares, my house, my car, all of my savings, all of my stocks, my IRA and my 401K, the proceeds from these sales would not be enough to cover my tax liability. I still owe over \$40K in back taxes due to penalty and interest. The truly depressing part of this sad story is that the Federal Government owes me over \$150K

in AMT credits. Of course I will not see any interest from the government and it'll take me decades to recover these credits back under the current AMT tax laws.

I would like to ask for your active support of H.R. 3385. This important legislation was recently introduced by Reps. Johnson (TX), Neal, McCrery, Jefferson, Ramstad, Lofgren, Shaw, Honda and Johnson (CT), to provide relief for taxpayers subjected to unfair and unjust tax treatment due to the AMT treatment ISOs. In addition to unfairly affecting me, this serious problem has impacted many employees of small and large companies across America, often resulting in taxes up to and exceeding 300 percent of these employees' annual salaries. Workers are being forced to pay tens of thousands, hundreds of thousands, and even millions of dollars in tax overpayments on income they will never receive.

Please join the groundswell of support for remedying this serious injustice through this ISO AMT legislation. This bi-partisan effort is building support in Congress, the Press, Corporate America, the Taxpayer Advocate's office. Grassroots organizations like the ReformAMT [www.reformamt.org](http://www.reformamt.org) and the Coalition for Tax Fairness [www.fair-iso.org](http://www.fair-iso.org) are actively supporting this important legislation, and may be contacting your office to secure your support.

I thank you for your leadership in this effort, as your support is critical to restoring a fair and just tax system for all Americans—including hard-working, entrepreneurial Americans.

Here's my personal story:

I moved from Plano, TX to become an employee of Qtera Corp., in South Florida, one of the many acquisitions of Nortel Networks during the telecommunications boon of 1998 to 2000. I received incentive stock options and subsequently have paid to the U.S. Treasury Department, Alternative Minimum Tax, in excess of \$250,000.00.

I was hired as the 31st employee in 1999. Working for Qtera Corp., in Boca Raton, FL was a fantastic experience. The team that was assembled was of the highest quality and some of the most motivated individuals I have ever worked with. Our devotion, hard work and technical expertise made us an acquisition target of both Cisco Systems and Nortel Networks in late 1999, Nortel Networks ultimately acquired us; around seventy employees had achieved the impossible. Instantly, all our Qtera ISO's were converted to Nortel Networks ISO's at approximately \$60 per share. Our success received a wealth of media coverage, from the Wall Street Journal to NPR. Qtera Corp. moved me to Denver to work in the Sales office for our largest customer, Qwest.

Soon after the media broke the news of our success, and the stockbrokers and investment bankers began courting our employees. As employees with much work ahead of us, we had little time or energy to learn about the Alternative Minimum Tax code. Some of the investment firms provided seminars on the Alternative Minimum Tax code but usually we were left with more questions than answers. AMT soon became the number one discussion topic, on the surface, we found ourselves quite versed in the subject, yet few of us really understood the dirty details.

The plan laid out by my financial advisors was to exercise and hold the shares as Congress had intended; then after holding the stock for a year, sell enough shares to pay AMT and invest the rest.

The first sign of trouble was the gradual decline in Lucent's stock price during 2000. We continued working incredible hours to meet our company milestones during our one-year transitional period.

By the middle of 2000 many employees had stockbrokers managing their investments. Not only brokers, but accountants, estate planners and life insurance brokers, everyone was after our potential wealth. I retained a local accounting firm to manage my tax liability and a nationwide brokerage house, (they recommended the accounting firm) to manage my account. The accountants were confident they were experienced with Alternative Minimum Tax. Their experience turned out to be limited, but since they had fifteen of my co-workers on a yearly \$4,000 retainer, they had no problem getting their hands dirty with the tax code. I reasoned that the Alternative Minimum Tax code was so complicated that I should have professional support, no matter the cost.

April 15th 2001. The year had gone so quickly and I exercised options during the previous year resulting in an Alternative Minimum tax on "Paper Gains" of over \$250,000. This even though I only made \$92,000 a year. It was strongly suggested, by my investment broker to use margin to pay the tax bill. The margin loan sounded like a reasonable idea, the investment firm provided a low interest loan without liquidating the account, as long as the account value is not less than the loan. Little did I know the bottom was about to drop out.

I began to diversify my account, but the majority was still in Nortel stock. Meanwhile, while no one was watching, Nortel Stock fell below \$20 per share, then \$16,



then soon after \$12. The Nortel management was positive on the company's growth and their overall market position, the low price was just a small correction in the overall market. (We now know these earnings were inflated.) At one point the stock fell to \$0.40 per share but is now at a healthy \$2.60 per share. I paid the AMT rate of 28% for \$60, \$70 and \$80 per share.

By the summer of 2001, the margin debt was nerve-racking and I was forced to sell Nortel shares and diversify as the share price continued to slide. I began to exercise and sell, just to raise cash for the 2001 Alternative Minimum Tax. Nothing could stop the hemorrhaging stock price or margin calls. The tax models the accountant had prepared last year were useless. My only concern was having enough cash to pay the AMT and pay off the margin debt. By the end of 2001, we got word that Nortel would soon be downsizing their operations. Nortel Networks needed to reach the "break even point" and the cutbacks began. By the third quarter of 2001, the share price was under \$10 and Nortel was laying off two thirds of their world-wide workforce.

By the summer of 2001, I reached my personal debt limit and liquidated my account to pay off my debt and pay most of the AMT. I sold my home that I had purchased in Denver and sold my car. The IRS had placed a tax lien on my home and took the money that I desperately needed to live on when I closed the sale. I ended my contract with my accountant, sold over 90% of my investment account, and prepared myself for the possibility that I too would soon lose my job. My fears were realized and by the second quarter of 2002, I was unemployed. I packed up my used truck and moved back to where I started, Texas. I was broke, unemployed and pretty darn disheartened.

I learned many valuable lessons through this experience and I am fortunate that I am not currently financially ruined like so many of my former colleagues. Many will have their wages garnished, or have filed for personal bankruptcy. None that I know of were fortunate enough to be able to negotiate settlements with the IRS. The Alternative Minimum Tax code was implemented to prevent wealthiest 2% of Americans from using special tax benefits to pay little or no tax. For various reasons the Alternative Minimum Tax has reached many hard-working, middle class Americans in Texas and all over this great country. Most of those folks don't have very high incomes or special tax benefits. I hope those in the United States Congress have the compassion and foresight to realize the growing negative effect of the Alternative Minimum Tax and bring change to the outdated tax code. AMT is not a fair tax. Why are certain Americans being punished with AMT? Because, we were perceived to be "rich" for a six month period of our lives? This is truly ludicrous! This will inevitably lead to bankruptcy for many Americans guilty of nothing more than exercising the promise of long-term investment in an employer they trusted. Not even the most diabolic communistic state could have come up with a worse tax system! I just can't understand this AMT tax law. It is so unfair! Income tax should be on INCOME!

In the end I, (along with many other Americans) could very well have to declare bankruptcy if a tax relief bill isn't passed into law.

I hope that you would be able to help us with this situation, by trying to abolish the current AMT Tax law, (hopefully retroactively to 1999). I would again like to ask for your active support of H.R. 3385. Please let me know what I can do to help you and what your thoughts on this matter are? I'm a law abiding, tax paying, Gulf War vet that thought I was living the American dream. I responsibly held my stocks. When the market crashed, I knew that I had to take the losses. What I didn't know is that I had to pay taxes of "phantom" gains. No American should have to pay taxes on income that was never income!

Thank you and best regards,

William R. Rinehardt

Austin, Texas 78734  
August 22, 2005

Committee on Ways and Means  
U.S. House of Representatives  
Washington, DC

Dear Sirs:

Several years ago, I BOUGHT stock by exercising "incentive" stock options where I worked.

I NEVER SOLD that stock.

I made NO PROFIT on that stock, and I have no hope of ever making any profit on it.

Despite those facts, current Alternative Minimum Tax law required me to PAY INCOME TAX AS IF I HAD MADE A PROFIT the day I exercised the options.

The law allows the U.S. Treasury to collect tax on "*PHANTOM PROFITS*."

I have, in effect, provided the U.S. Treasury an interest-free loan by PREPAYING TAX on income that I will NEVER receive.

This is so bizarre and so unfair that it is hard to comprehend. The U.S. Congress never could have intended to cause such INJUSTICE and should be anxious to correct it.

H.R. 3385, The AMT Credit Fairness Act, was recently introduced by Representatives Johnson (TX), Neal, McCrery, Jefferson, Ramstad, Lofgren, Shaw, Honda and Johnson (CT), to provide relief for taxpayers subjected to this UNFAIR TAX.

Please work to pass H.R. 3385—AMT Credit Fairness Act.

Thank you for your leadership to ensure a fair and just tax system.

Sincerely,

Dr. Terry Ross

Excelsior, Minnesota 55331  
August 25, 2005

To: Members of the House Ways and Means Committee—Hearing on Member Proposals on Tax Issues/Reform

Dear Committee Members:

I have submitted my testimony and shared my story on Alternative Minimum Tax (AMT) at a number of events, including the recent President's Tax Reform Advisory Panel. I am writing this letter to you directly to provide my personal testimony with regards to Alternative Minimum Tax (AMT) for individual tax payers and to ask for your support and leadership in regards to Bill H.R. 3385, introduced by the Honorable Sam Johnson on July 21, 2005 and co-sponsored by a number of Ways and Means Committee Members.

Our family paid over \$1.7 Million AMT in Tax Year 2000, due to phantom gains on Incentive Stock Options (ISOs) that were exercised but not sold. Specifically, the AMT was paid due to paper gains on 70,000 Ariba ISOs that we exercised when at the stock's value was over \$110/share. Due to a Blackout Period, I was unable to trade the stock until after the end of the tax year. The stock is now worth less than \$1/share, with an *economic benefit* of about \$70,000, as opposed to the \$7,700,000 paper gain we were taxed on. I ask that you focus on those numbers. **We paid a \$1,700,000 tax for an economic benefit of \$70,000** due to what Senator Joe Lieberman described as a "Kafkaesque situation" and the "tax equivalent of the perfect storm." These statements were part of Senator Lieberman's Congressional Record statement made when he introduced Bill #S. 1324, an Alternative Minimum Tax (AMT) relief bill with respect to Incentive Stock Options (ISOs) for tax year 2000, on August 8, 2001.

Senator Lieberman is not alone in his search of a fair law to replace the current AMT law and the problem does not appear to be a partisan political issue. Many bills were introduced on this subject prior to 2001 and numerous bills have been introduced since. Several have been introduced into this session of Congress, including the most recent Bill H.R. 3385 for which this letter requests your support. My analysis shows that both Republicans and Democrats support ISO AMT reform. This support includes many Members of the 109th Congress Committee on Ways and Means: Reps. Wally Herger, Jim McCrery, Jim Ramstad, Eric Cantor, E. Clay Shaw Jr., Sam Johnson, Phil English, Jerry Weller, Ron Lewis, Mark Foley, Kevin Brady, Richard Neal, William Jefferson, and Lloyd Doggett.

There is no question that AMT is not serving the purpose for which it was originally intended and that it must be totally revised soon for many reasons. This hypothesis is supported by most informed civilian and government agencies aware of the original intent and the current implementation of the law, including:

- The United States General Accounting Office
- Congress Joint Committee on Taxation
- The Brookings Institution
- The National Taxpayers Advocate (a division of the IRS)

- The American Bar Association (ABA)
- American Institute of Certified Public Accountants (AICPA)
- Tax Executives Institute (TEI)
- The National Venture Capital Association

Tax law for AMT on ISOs as currently written is highly confusing and very unfair. The Instructions for Form 6251 (AMT—Individuals) when filing my 2000 taxes stated the following:

“The tax laws give special treatment to some types of income, allow special deductions for some types of expenses, and allow credits for certain taxpayers. These laws enable some taxpayers with substantial economic income to significantly reduce their regular tax. The AMT ensures that these taxpayers pay at least a minimum of tax on their *economic income*.”

My family has no special credits, deductions, or exemptions that significantly reduce our regular tax and we have been caught in a situation where our AMT tax burden on ISOs has far exceeded any *economic benefit* we have or ever will gain from ISOs exercised in tax year 2000. In short, we are 2000 AMT victims that Senator Lieberman described as, “fell into a trap which the tax code created through its perverse and confusing structure” in his Congressional Record statement on August 8, 2001.

I am not a wealthy executive. I am a 46-year-old sales representative that received the ISOs because I joined a company before they were well known and opened a territory for them to make them well known. My wife, Velinda, is a stay-at-home Mom for our 8-year-old daughter Emma and 4-year-old son Quinn. When we became aware of our AMT obligation in 2001, we liquidated all of our assets and paid the AMT, including a substantial penalty that incurred during the period that it took us to liquidate those assets. ***We paid tax on paper gains that exceed my salary for a lifetime.*** I continue to work and pay taxes. Interestingly enough, I seem to get hit with AMT every year. It seems a little odd that the taxes we continue to pay continue to be used to support people that find themselves the victims of unfortunate circumstances, yet no such support is there for those of us that got caught in the AMT trap in 2000.

Please use this testimony as an example of the unfairness of this law as it is currently written and to promote reform of the AMT for Individuals tax laws, including relief for those of us that lost all of our assets in 2001. I believe that doing so is very much on the spirit of President Bush’s tax relief package, which allows Americans to keep more of their own money. I respectfully request your leadership and support of H.R. 3385 as a part of your efforts to accomplish this vision.

Tom Schrepel

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#### Statement of Joe E. Sheldon, Huntington Beach, California

My greatest concern is that the Committee (and Congress and the President, too, for that matter) will fail to realize that the National Anthem is **NOT: “Tiptoe Through The Tax Code Tinkering Tango”** as an acquaintance of mine used to say.

Tinkering with the tax code, no matter how well intentioned, will no longer plug all the leaks in the boat but would require bailing so fast that the boat would catch fire from the friction or sink (or perhaps both).

I truly hope that is realized (and I think, perhaps, it is).

Attempting to retain ANY tax system based upon income taxation will no longer function as has now been adequately proven after almost 100 years of trying. It’s time for a tax system in tune with the 21st century and international competition. It is time for the FairTax.

As the most thoroughly-researched economic/tax proposal ever brought before Congress, the FairTax stands head and shoulders above any form of income taxation (including any flat tax which after all is what the present system started as) or any form of Value Added Taxation.

Any income-based taxation—flat or round—has the sort of warts we have come to know (but not love) such as embedding taxes into the prices we all pay; allowing for great political mischief with all of the exemptions, deductions, and other special tax favors, treating those in similar situations differently (and causing resentment thereby), and requiring a much-detested enforcement arm—the IRS. It also encourages—almost mandates—attempts by Congress to control the populace by altering

the Tax Code. Such attempts are bound to fail as misguided efforts in “Trying to Teach the Elephant to Tap Dance” as the old saying goes and they invariably redound to the detriment of the citizens and eventually the government itself . . . the current untenable AMT being a perfect example.

It is neither necessary nor desirable for the government to attempt to control the lifestyles of its citizens by such means. The citizens are fully capable of doing so themselves and the necessary tax revenue can be raised without such nonsense. Laws for behavior should be separated from tax laws which are, after all, for the purpose of raising the money to run the government. Mixing the two does neither effort (nor the citizens) justice—not to mention the country itself.

The FairTax is the only tax plan that I see before Congress that meets all of the criteria charged by the President. All of the others fail in important aspects. It is time for a real change and not just tinkering again. The people want real change which I think should now be abundantly clear. Do not be forestalled by those who say “no one else has done it that way” and other similar non-arguments. Remember no other country had even had a Representative Republic before and THAT has worked out very well. Slavishly copying failed tax plans from other countries is not a recipe for success.

In addition, the attempts at introducing the FUD Factor (Fear, Uncertainty, and Doubt) used by those who would prefer some form of the status quo can surely be seen for what they are—emotion based attempts to derail a tax system that we so badly need. Claims that the FairTax requires a huge boost in rate over that in the H.R. 25 bill or that evasion will be rampant are examples of the FUD Factor run amok; compliance should actually improve. In fact the FairTax should be scored in a fashion that recognizes the increased revenues it derives which cannot be done by any income-based taxation system. The underground economy in all its many forms of illegal income (illegal aliens, drug transactions, prostitution, and just money theft in general) completely escapes any income tax-based system while under H.R. 25, the cash from those illegal transactions is fully taxed when spent for taxable items. In the case of illegal aliens alone this represents many, many billions of tax revenue and should be scored as such for the FairTax—as should the capture of the other illegal income.

Additionally, the FairTax will obtain tax revenue from foreign tourists who, after all, are benefitting by our (formerly) taxpayer-paid facilities when they visit many places in this country. Also, the provisions of H.R. 25 allow border-adjustable taxation which would help our exporters reduce their prices to be more competitive in other markets . . . and foreign imports would also be taxed when sold as taxable items at retail instead of being tax-free as at present—somewhat like a tariff but allowed and acceptable under international agreements.

Moreover, the FairTax offers another path to the President in his desire to reform the Social Security/Medicare systems.

Perhaps the four overriding goals of a tax system were best expressed by Adam Smith in his “Wealth of Nations” where he set out these four canons—

I. The subjects of every state ought to contribute towards the support of the government, as nearly as possible, in proportion to their respective abilities; that is, in proportion to the revenue which they respectively enjoy under the protection of the state. . . .

II. The tax which each individual is bound to pay ought to be certain, and not arbitrary. The time of payment, the manner of payment, the quantity to be paid, ought all to be clear and plain to the contributor, and to every other person. . . .

III. Every tax ought to be levied at the time, or in the manner, in which it is most likely to be convenient for the contributor to pay it. . . .

IV. Every tax ought to be so contrived as both to take out and keep out of the pockets of the people as little as possible over and above what it brings into the public treasury of the state. . . .”

The present income tax system fails on all four points; the FairTax (H.R. 25) meets all four admirably and in the spirit intended.

Therefore I urge you . . . NO, I implore you . . . to recognize the FairTax as the best alternative for a decent, simple, visible, and modern tax system for this country.

Thank you for your attention and interest.

Ely, Iowa 52227  
August 31, 2005

Dear Honorable Chairman Camp and Ranking Member McNulty:

I am writing to you on behalf of my family because we desperately need your help. We have been improperly assessed by a flaw in the tax code and we need you to step forward and help save our family. In the year 2000 our taxable income was \$105,461. For that same year we received an Alternative Minimum Tax of \$206,191 from the Federal and \$46,792 from the State of Iowa. A total tax of \$252,893 for a gain that we NEVER made.

In December of 1992 I took a chance on a small telecommunications start-up in Iowa called McLeodUSA. To compensate the employees the company used stock options as part of its compensation. This is what we were using to plan our future. We had saved all the options we received to use on building a home, our three daughters education, and our retirement.

In 2000 we were ready to start building our home so we spoke to our financial and tax advisers to determine the best way to use the stock. Based on the current tax laws, they told us to exercise the options and hold them for a year so we would be charged long-term capital gains on the income. We exercised the stock but did NOT sell it. As the home was nearing completion we had our taxes done by an accountant and received this unjust tax bill. The stock value had plummeted so we borrowed money from a local bank to try to pay the tax. We paid the State tax in full and \$94,484 of the Federal in payments. Our local IRS collections agent reviewed our case and told us there was no way we could pay the remainder off and instructed us to inter into the IRS's Offer In Compromise program. They said the OIC program was put in place to solve impossible situations just like ours.

After waiting for 8 months we were finally assigned to an OIC Specialist. The OIC Specialist has utilized the formulas and guidance that our government has put into place and has informed us that we have been rejected from the OIC program. He told our attorney that I have three things going against me, I am not old, I am not disabled, and I have been too consistent. I have been too consistent because I've been employed and paying income tax since I was fourteen years old. I've never filed bankruptcy. I've never defaulted on a loan. According to the archaic computations the IRS used our family should only have housing and utility costs of \$1,067 per month, our actual is over \$3,700. Based on their allotment we are supposed to be able to pay \$2,366 per month to settle the debt and a lien has been placed on our home. There is no way we will be able to pay this amount. We have appealed our case with the U.S. Tax Court but have been rejected by the Court also. Both the IRS and the Court say it's up to Congress to fix this. We desperately need Senate Finance to place a "stay" on the IRS collections pending the Sam Johnson ISO AMT remedial legislation that will correct this horrible wrong. Our story is a legitimate case that can't be disputed as being horribly wrong. Please use the powers you possess to right this inconceivable outright injustice. I beg of your help.

I have been nothing but honest to the letter of the law in paying taxes my entire life. It seems incredible to me that I should be financially destroyed by a tax that is so unjust.

I respectfully and urgently request your support of H.R. 3385.

Ron Speltz

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### Submission of Jonathan Steere, Leonardtown, Maryland

House Committee on Ways and Means:

I am writing this letter to discuss the alternatives you are considering in overhauling the U.S. tax code as requested by President George Bush. In particular, I am in strong support of implementing a national consumption tax in replacement of the current federal income and corporate taxes. (Also known as the Fairtax.)

Though the fairtax and flat tax proponents cite the complexity and cost of complying with the current income tax code as a supporting argument in favor of their respective tax systems, it is not one of my reasons for supporting tax change. I fully expect that if the tax system is simpler, it would promote better compliance by individuals on their taxes, and therefore would be easier to find tax fraud and lawbreakers who will cheat the system regardless of how it is formed. If this were the only benefit, however, I would have no interest in the tax change whatsoever

as I don't mind the current annual 1040 tax forms and I don't feel huge overhauls are necessary just because some people break the law.

I believe that there are incredible gains in many other areas to be achieved by tax reform. I wish to outline them for the Committee now.

#### *Promote Fair Taxation*

One of the biggest fights on taxation seems to always be the struggle between progressive and regressive taxation. As tax rates increase, the incentive to hide your income at higher tax brackets increases, and the incentive to improve your wealth through entrepreneurship decreases. If tax rates become too high, then the wealthiest and the largest producers of jobs will strive to earn revenue in other countries in search of lower tax alternatives, or look for tax breaks here, or defraud the government altogether. If the tax rates are too low, then those poorest among us complain about the rich not paying their fair share of taxes, as the government will struggle to pay for low income benefits.

Unfortunately, taxation is a necessity given the way the government is currently structured. But even so, the burden needs to be balanced and compassionate. When special interests are allowed to influence lawmakers through the tax code, the tax burden becomes more and more unbalanced, as tax laws are written to cater to the lobbyists. This would happen at any tax rate and any income tax system. Even if a flat tax was enacted, it is likely that deductions, tax breaks, and incentives would start to creep into the tax code in future administrations, thereby undoing all the great work that this Committee is trying to enact. Those companies or individuals that qualify for the tax breaks pay less than those that don't. Usually, it is the middle class that bears the burden, as the poor pay little or no tax, and the rich have the resources to utilize the tax shelters set up specifically for them.

The only way to correct this imbalance is to repeal the income tax law entirely and revert to a form of taxation that is fair and balanced for all, and yet has consideration for the poor. I believe the fair tax fits this qualification.

#### *Pro-Growth*

Both the flat tax and fair tax initiatives would promote growth, as there is equal incentive to strive for more success at any income level. The flat tax, however, has the chance to be undermined by future administrations by adjusting the tax rates, re-implementing progressive tax brackets that punish success, or giving incentives for special interest groups to re-implement complexity through narrow tax breaks for special activities. This can be seen in history, as President Reagan simplified the tax code in 1986 to two tax brackets, along with closing some loopholes and other changes. Twenty years and three presidents later, multiple tax brackets have returned and the tax code is as complicated as ever.

Corporate taxes raise costs for domestic companies while reducing their competitiveness with foreign companies that have either lower or no corporate taxes. Since, it raises costs, it will do one of three things. It might reduce their profitability, which slows investment income growth. It may cause them to freeze wage increases, lower wages or lay people off to cut costs, which reduces the tax base and also slows growth. Finally, it might cause them to raise prices on the goods they sell, which adds to inflation. It should be easy to see that any of these three options result in negative consequences for the economy. Indirectly, it also is a form of double taxation for individuals, since most companies reject losing profitability in favor of passing on their costs to either the consumer or their employees. Competition, labor agreements, or resources may restrict their ability to pass these costs on. That leaves them with one other possibility, which is the worst of all for Americans. This would be that the company stop producing locally and import their goods from countries that have cheaper labor costs, cheaper resources and/or cheaper tax rates.

This is the one area where the fair tax is superior to all other forms of taxation. It is the only tax system that levels the playing field between domestic and foreign operated companies. As I have just shown, other taxes make domestic goods more expensive, and many foreign companies do not have this problem. Removing corporate taxes actually has the long-term result of reducing the costs of goods manufactured or services provided in the United States. Although this would be replaced by the fair tax, it does help make American goods more competitive by taxing goods equally whether they are made here or somewhere else. An item manufactured in China would be subject to the same tax as one manufactured in America. But with corporate taxes removed, the Chinese good would cost 30% more, and the American good's price would be more balanced by the lowering of hidden taxes even though the 30% sales tax would apply. Note that this is done without invoking any protectionist measures that might violate foreign trade agreements and cause retaliation by the foreign country.

It is clearly a political benefit to correct the corporate imbalance and make strides towards reducing the incentive for outsourcing jobs, something that was a big issue in the last presidential election. It also potentially could help reduce the huge trade deficits we experience year after year.

*Taxes Previously Untaxable Illegal Activities*

One of the political benefits from using the fair tax system is that the taxation rate can be revenue neutral for law-abiding taxpayers, and still generate significantly more revenue than the existing tax code. For instance, according to the Office of National Drug Control Policy, \$77 billion is spent on cocaine and \$22 billion on heroin, \$2 billion on methamphetamines, \$10 billion on marijuana, and \$2–3 billion on other illegal drugs. (Statistics are from the government web site below.)

[http://www.whitehousedrugpolicy.gov/publications/drugfact/american\\_users\\_spend/section1.html](http://www.whitehousedrugpolicy.gov/publications/drugfact/american_users_spend/section1.html)

90% of this money stays in the U.S. This money cannot be taxed directly by any suggested tax system because it will never be reported. But indirectly, only the fair tax system will generate any revenue at all. Eventually, this money will be spent on other things. At a 30% taxation rate, this would generate \$30 billion or more when this money is eventually spent legally on cars, boats and other goods. This in itself would pay 2.5x what is currently spent on the war on drugs, which is about \$12 billion.

This of course, is one type of criminal activity among thousands. Indirect revenue would also be achieved from prostitution, embezzlement, smuggling, or any other unreported revenue. It should be noted too, that revenue legally earned, though illegally unreported on tax returns would also generate indirect revenue, such as tips, casual labor, or other secret transactions not always reported.

Another source of income would be from immigrants who are here illegally. If the current estimates are correct, then 10–15 million illegal immigrants are not reporting any revenue to be taxed. While it's highly likely that most of these would not pay taxes under the other suggested taxation systems, it provides a disincentive to illegal immigration in that goods are taxed, and yet only legal residents would be eligible for the fairtax prebate. Though this will probably not be sufficient to deter them from living here, it will be another indirect source of 10's of billions of dollars in taxed sales, that results in revenue that likely went to Mexico or another country before.

*Proof of Success and Warnings*

Many years ago, I was a resident of Canada, and was able to view first hand the results of Canada's implementation of the Goods and Services Tax (GST). This is a value-added taxation scheme implemented by the Canadian conservative party. It was a great success economically, but a failure politically. I believe, however, that it can be used as an example of how the tax would affect the United States, and for what policies to avoid.

First, it was a success in that it generated revenue for the Canadian government far beyond what any of the experts predicted. Its success has allowed the government to generate a surplus in which it could reduce its national debt in every year since 1997. It has also allowed the government to reduce the federal tax rates without sacrificing revenues or the surplus. This has resulted in Canada having a lower income tax rate in 2004 than the United States. (The first time this has happened in at least 50 years) As hidden taxes were removed, prices definitely did drop almost immediately on many goods, and although a few things did rise in price because of the tax, it was a net gain for the consumer. Overall, it was the start of a long boom in the economy that coincided with the boom in the U.S. It began more slowly at first, but took off as income tax rates were reduced in stages. Canada's economy slowed only slightly when the U.S. experienced the recession, because while Canadian income taxes were dropping along with interest rates, American citizens had to deal with Clinton's tax increases and rising interest rates.

Unfortunately, it was a political failure in that it's implementation was utilized as a political issue by the opposition party who regained power by promising to repeal the tax. They never did repeal the tax, however, because of the success of the tax. The reasons that it wasn't a political success were twofold. First, the lack of understanding among the general public about it, and the fact that it was seen as an additional tax, since no changes were made to any of the other taxes Canadians were subject to, except the hidden manufacturing taxes.

Clearly, in the Canadian case, the fact that the income tax remained was the reason for the political backlash of the GST, even though in the long run the economy benefited. (Also, if it were not for other problems the party was having at the time,

this could have been mitigated.) The fairtax solution avoids this problem by forcing a repealing of all income and corporate taxation. Though there might be transitional difficulties as there always is with such a large change, the benefits in the long run far exceed any short term pain and confusion. I ask that you consider carefully the benefits of the fairtax, as I feel it is the best overall and fairest form of taxation available to any government looking for tax reform.

Thank you for your consideration of this letter.

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**Statement from Mike Strick, Seattle, Washington**

Dear Honorable Chairman Camp and Ranking Member McNulty,

I understand that there was a House Ways and Means Committee hearing on Tax Simplification with regard to the Alternative Minimum Tax on June 15, 2004. I noticed you were looking for stories of “middle class” Americans who have been affected by the current parameters of the AMT. I am one of those people.

I worked for Internap Network Services, an Internet connectivity company, for almost two years before being laid off in April 2001. While I was working, I was also in graduate school for psychology to become a counselor. At one time, Internap’s stock traded as high as \$220/share before splitting to \$110. Yesterday, Internap closed at about \$1.00/share. I exercised incentive stock options to acquire a number of shares in July, August, and September of 2000 with the intention of holding them for the long term. I assumed I would have enough value in the stock that I could pay off the AMT I owed. I would have never guessed the stock would drop to \$1.00/share and hover there for the next three years . . . and that I would end up owing almost \$100,000 in AMT—money I just don’t have. I find it hard to fathom that I owe so much because I ended up paying huge taxes on a phantom gain. My tax alone was more than two years worth of income for me.

I ended up in negotiation with the IRS via an Offer in Compromise for almost three years. We ended up “compromising” so that I would lose everything I own (retirement savings, investments, emergency funds, IRA’s, etc.), plus about 20% more, all to be paid over the course of two years. This situation has affected every aspect of my life and will impact my future for years to come.

In retrospect, I realize I made a mistake by not delving deep enough into a complicated tax code to understand the possible outcome of my ISO exercises. I am working to pay off my debt as a counselor with developmentally disabled folks. But, I feel the AMT laws as written are not working the way they were intended, and I don’t want others to have to go through the same hardships I am enduring. Change is needed. I would be happy to give more details or talk about my situation. I appreciate your time and concern and I respectfully request your support of H.R. 3385.

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Santa Cruz, California 95060  
*August 31, 2005*

Dear Honorable Chairman Camp and Ranking Member McNulty,

I submitted testimony and shared my story at previous events:

- April/May 2005, Senate Finance Committee, Chairman Grassley
- Spring/Summer 2005, President’s Tax Reform Advisory Panel

I now wish to share my story directly with you in hopes of garnering your support and leadership of the Honorable Sam Johnson’s H.R. 3385.

When we met with our tax preparer for the 2000 tax year, we were very surprised to learn that the IRS demanded from our middle class family AMT tax of more than \$230,000 due to paper gains on stock options that dropped in value during the year, even though we never received gains in reality.

As a result of the tax bill on the “paper” profits that we never received, we had to take out a second mortgage on our home and deplete our daughter’s college fund to pay the IRS and avoid a threatened lien on our house.

Today, we no longer have college savings for our daughter, who is 13 years old and a straight-A student who deserves to go to a good American university. The irony is that all the money she needs to attend college is sitting with the IRS in the form of a tax credit. However, no matter how hard we plan, our AMT and our regular tax bills are nearly identical each year, so we are never able to generate



a sufficient AMT credit to receive a refund that would put the money back into our hands and allow us to invest it in a 529 or other college savings fund on her behalf. Please help ordinary American families like ours recoup AMT credits and send our children to college.

I respectfully and urgently request your support of H.R. 3385.

Michael Sullivan

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Somerville, Massachusetts 02144  
August 18, 2005

Dear Honorable Chairman Camp and Ranking Member McNulty:

I have submitted my testimony and shared my story at the Ways and Means Committee Hearing on Tax Simplification on 6-15-2004. I now wish to share my story directly with you in hopes of garnering your support and leadership of the Honorable Sam Johnson's H.R. 3385.

I am writing to enlist your help in fixing the Alternative Minimum Tax (AMT) law to help me obtain more than \$100,000 that I overpaid to the government while I can still use it to help pay for my children's education, care for my aging parents and, hopefully, afford retirement instead of having to take small credits for each of the next 20 years.

For almost 5 years, I have worked for a company, named webMethods, which has created over 850 new jobs in the last four years of operation. To reward and retain its employees, webMethods makes extensive use of incentive stock options (ISO).

As an early employee of the company, I received a number of stock option grants. Unfortunately, I made the grave mistake of exercising these options in one year and selling them in another. That action, coupled with the fact that webMethods was the #1 software initial public offering (IPO) in history, created an enormous AMT tax bill (\$250K+) for my wife and I. The taxes I paid and the value of the stock exists now only as a \$250K AMT credit, which, as I explain below, I can draw at the rate of only a few thousand dollars a year.

We had to sell most of our long term savings to pay this tax bill. We consider ourselves fortunate that we did not also have to sell our home or declare bankruptcy. All of this, just so we could pre-pay tax at a 28% rate when the actual tax is only 15%. You must also know that the AMT is affecting an increasing number of middle-income taxpayers, which is, and should be, of great concern to many law-makers.

Fundamentally, the AMT treatment of ISOs is wrong and should be fixed—ideally the AMT should be eliminated. That said, our immediate problem is the AMT tax crediting process. Each year, we are only credited the difference between our regular and AMT tax calculations—for the 2002 tax year our credit was a little over \$5,000. At this rate, it will take us more than 20 years to get our entire overpayment back from the U.S. Government. This delay represents opportunity cost for a better retirement, good schools for our children, and money to care for our aging parents.

Clearly structural changes are needed, but what my wife and I want immediately addressed is our outstanding AMT tax credit. H.R. 3385 has provisions that address this issue and I respectfully and urgently request your support of H.R. 3385.

Very Sincerely,

Shawn W. Szturma

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Chesapeake, Virginia 23322  
July 27, 2005

Honorable Committee Members:

I am a dentist in private practice in Norfolk, Virginia. I have practiced in the private sector for thirty-one years. I am also Treasurer of the Tidewater Libertarian Party and an observer and student of human behavior and economics. I note that while the free market has provided us with a wide array of goods and services at competitive prices in other areas, it has failed to do so in healthcare. I believe there are a number of factors related to tax reform that are responsible for the failure of the free market to operate at it's best in this segment of the economy. With the

issue of tax reform before Congress, we have an opportunity to unleash the power of the market to deliver healthcare of great quality and at lower costs, thus making government paid healthcare unnecessary, except for the indigent.

First, there is a distortion in the market mechanism because those who consume healthcare do not directly pay for it. Because our tax laws make it impossible for individual or voluntary organization group healthcare plans to compete with employer provided plans, the great majority of healthcare is paid for by employers who have little control over consumption or delivery of that care. There is no other equivalent disconnect in market forces anywhere else in the U.S. economy.

Secondly, the marginal cost of using healthcare services is distorted by the nature of those employer sponsored group insurance policies. While catastrophic healthcare insurance is necessary for protecting us from unexpected and overwhelming costs, most employer sponsored plans include both a catastrophic insurance element and an element of prepaid routine care to encourage early intervention. This makes sense from the insurer's and the employer's point of view as early intervention often reduces the need for later catastrophic care. But from the consumer's point of view, once deductibles are paid, the marginal cost for consuming more healthcare services is minimal, and after 'stop loss' limits are reached, non-existent. From the provider's point of view, there are liability issues to consider when making decisions, but no doctor has ever been sued for ordering too many expensive tests. This is equivalent to selling houses in such a way that the buyer pays full price for the living room, 20% of the cost of the kitchen, bathrooms, and first bedroom, and nothing at all for additional rooms, with a third party compelled to pay the remainder of the costs. There would be no reason for any homeowner to live in anything less than a mansion. Efforts to control those costs through managed care schemes have proven only marginally effective and detrimental to patient care.

Finally, while the rest of the industrialized world funds government largely through consumption taxes, the U.S. alone relies entirely on taxation of personal and corporate income for government and social security funding. Income based taxation costs to businesses and individuals cascade through the production process, just like any other cost of doing business, and result in an embedded tax component hidden in the price of goods and services. This embedded tax component averages about 20% for goods and 25% for services of all types, but varies greatly depending on the income levels of those providing the services. For example, the services of a low wage gardener or domestic worker would contain relatively little embedded tax component, while services provided by multiple layers of highly paid professionals would carry a much higher than average embedded tax component. Healthcare is provided by general practice and specialty physicians, dentists, optometrists, and other providers backed by layers of technicians, caregivers, clerical personnel and equipment specialists all of whom are paid, and taxed, far above average. The tax component embedded invisibly in the price of healthcare has not, to my knowledge, been individually measured, but must be enormous compared to almost any other service sector, possibly as much as one third of the total cost.

Changing from an income based tax system to a consumption tax, like the FairTax, ([www.fairtax.org](http://www.fairtax.org)) would eliminate the tax advantage of employer sponsored insurance plans. Certainly, most employers, through negotiation with their employees, would continue to offer those plans, but group plans based on professional organizations, health clubs and religious or social organizations would be competitive. Healthcare insurers would again be directly accountable to those who purchase and use their product, reintroducing free market forces to those transactions. There would, at last, be incentives to patients and providers to control costs at the level where the choice of how much and what level of care is appropriate is made.

Although healthcare premiums, and services not covered by insurance, would be taxed just like any other item of consumption under the FairTax, because the tax component embedded in healthcare services being eliminated is far larger than the 23% (inclusive) tax rate, the walk-away cost of healthcare would decline even before competition brought the normal efficiencies of the market to bear on how healthcare is delivered and consumed. Note that this would be less true for a VAT tax, as cascading of costs for consumables would still occur under that system while they do not under the single layer retail sales tax used in the FairTax plan.

Finally, the other economic advantages of the FairTax plan, such as overall growth in the economy, investment incentives, and repatriation of manufacturing jobs, would leave us with a population far better able to directly pay those lowered healthcare costs, with less dependence on third party payers which distort the market.

No doubt, many healthcare providers will balk at facing the competition of direct involvement in the marketplace, but why should the healthcare sector be exempt

from the same competition and innovation that has made us the most free and prosperous people in the history of mankind? Since removing the embedded taxes, now hidden in my fees, reduces the cost of my services to my patients but does nothing to reduce my income, I see little to fear. As a healthcare professional, I would greatly prefer that my patients be able to afford my services with less strain on their budgets and more say in the type and extent of treatment available to them. Market forces would bring greater efficiencies to the delivery of healthcare, and more restraint to consumption of those services, further bringing down the cost without interfering in the choices which should be made by our patients, in consultation with their doctor, and not by government or a distant insurance company.

That is how the free market is supposed to work, and will, if we just get our Byzantine income tax code out of the way. The FairTax will remove distortions from the marketplace in healthcare and elsewhere in the economy, grow our economy and individual incomes, bring back the manufacturing jobs we have lost, and fund our necessary government services with a fair and transparent system of taxation more consistent with our national embrace of the free market, and freedom in general, than any other system under consideration. I ask you to join me in working for this important change for the better.

Thank you for your time and consideration.

Sincerely,

Wm. Donald Tabor Jr., DDS

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### Statement of Paul Tadros, Kirland, Quebec, Canada

#### INTRODUCTION

Invariably, some of the proposals herein may have been presented by others but, in many aspects, may be different and more controversial but pragmatic. Of course, they constitute broad concepts.

The proposals being presented aim to (1) avoid complexity and (2) be equitable. While a certain degree of complexity may be necessary, it should not be the norm. Currently, complexity in the Code is the norm rather than the exception.

The key element to drafting and implementing sound pragmatic fiscal policy is the existence of the political will. Does Congress and the Administration have the will to curb self-interests groups? Sound tax policy implies equitable treatment, not equality—not everyone can be satisfied.

At this point, some background and insight may be warranted. I have been practicing U.S. international taxation for over 25 years and have worked in numerous countries. Until two years ago, I was a Partner—U.S. International Tax Services with a Big 4 Firm.

In 1980, I was part of a small group which was contracted by a foreign national government to make recommendations on a complete overhaul of its income tax regime. This national government provided us with extensive data of its taxpayers over a fifteen (15) year period. Of course, identities were not disclosed but groupings, as we thought to be necessary for the analyses and basis for our recommendations, were provided. In conducting our in-depth analysis, no element nor any group were “sacrosanct.” The “bottom line” shock to this government was that, over the fifteen-year period, its revenues would have been 30% higher if:

1. There was no corporate income tax; and,
2. The basic rate for individuals was 17% with a basic exemption, at that time, of \$10,000.

Of course, the final document was substantive. To the surprise of that government, the public hearings produced wide acceptance for the proposals. Unfortunately, it succumbed to the pressures of interest groups and lacked the political will to tell these groups to “get lost.” Needless to say, the continuation of the status quo resulted, in the long term, in large fiscal deficits.

#### PRINCIPLES BEHIND THE SUGGESTED PROPOSALS

1. We must start with the principle that the concepts of capital export neutrality (“CEN”) and capital import neutrality (“CIN”) are no longer valid in today’s global economic environment. In fact, they are contradictory. For example, we see this in the portfolio interest exception in section 871(h). Therefore, where is the “neutrality”? To retain these principles in formulating tax policy will cause meaningful tax reform to remain elusive;

2. Encouraging compliance. A disincentive to avoid taxes is introduced;
3. Protecting and even increasing revenue flows to the Treasury;
4. Encouraging investment in human resources and plant and equipment;
5. Increasing productivity and making U.S.-based multinationals more competitive;
6. Increasing savings thereby putting less pressure on the Social Security system; and,
7. Keeping inflationary pressures at bay.

#### **INDIVIDUALS**

1. The four categories of filing status should be eliminated. These categories produce bias and complexity. Each taxpayer files separately and becomes solely responsible for his/her own tax liabilities;
2. In the areas of employment and investment income, the number of deductions should be significantly reduced (see points 3 and 4 below). Normal expenses for business (self-employed) income continue to be available;
3. Deductions for items such as mortgage interest, property and state taxes should be eliminated. At the same time, the deferral rules, etc. related to the sale of a principal residence should be eliminated. The gain on sale of a principal residence (subject to built-in safeguards) should not be taxable. Of course, losses are not deductible;
4. Dividend income from U.S. sources should be exempt. Therefore, any expenses attributable thereto would not be deductible. Foreign-source dividends would be taxable at the full proposed rate (of course, subject to any foreign tax credit);
5. There should not be any distinction between capital gains and other investment income;
6. The PFIC (personal foreign investment company) rules should be retained;
7. All taxpayers will have a basic exemption of an amount equal to the minimum wage. In essence, this protects the most disadvantaged in our society while creating an equitable situation;
8. In relation to (7) above, a refundable child tax credit of \$3,000 for each child under 18 years of age if and only if the total annual family income is less than \$30,000 (basically, twice the minimum wage); and,
9. Based on the preceding, the rate of tax applicable to everyone should be 20%.

#### **Some of the effects from the preceding proposals should be:**

1. Given that \$0.80 for every \$1.00 earned is retained by a taxpayer, an incentive to earn more is created and a disincentive to not report is also created. A progressive system, although the principle is to create "fairness," actually: (1) creates a disincentive to increase earnings because every additional dollar earned in "moving to another higher bracket" results in lower returns; and, (2) creates an incentive to "avoid."
2. Pressures on salaries and wages should be substantially reduced. This, in turn, enables U.S.-based companies to be more competitive while reducing inflationary pressures;
3. By making domestic dividends exempt from taxation, the so-called "Wall Street" biases should be lessened. Companies with a good history of paying dividends would be rewarded by investors. More importantly, the investments become more of a long-term nature rather than "selling" because someone on Wall Street placed an earnings target on a company which was not met. In addition, this should lead to stronger balance sheets because it is worthwhile to raise funding through equity rather than debt.

#### **CORPORATIONS**

**This area would, most likely, constitute the largest overhaul. However, it's also the area which is prone to self-interest groups. This must be avoided at all costs.**

Some of the areas which should be retained include, in an international context, sections 367; 163(j); and 482. Nevertheless, updating the applicable regulations to ensure that they are in line with today's economic environment becomes crucial.

Since my forte is in the international area, most of the proposals address this aspect. A good start was made in some of the changes in the American Jobs Creation Act of 2004 ("AJCA"). For example, the reduction of the foreign tax credit baskets to two and the recharacterization of overall foreign loss to domestic loss. However, one of the negatives was the various effective dates. This type of action contributes to and promotes built-in complexity which must be minimized.

With regards to the controlled foreign corporation (“CFC”) rules, the only aspect which should be retained is that related to “pure investment income.” The following paragraphs address the draconian aspects of the CFC rules.

The Subpart F provisions constitute one of the most complex set of rules in the Code. These were introduced in 1962 when the so-called principles of CEN and CIN were, perhaps, valid. Forty-three years later, CEN and CIN, as stated earlier, are no longer valid. To maintain the CFC rules to force “neutrality” is not appropriate. Other factors such as labor, country risk, etc. play major roles in investment decisions. All of these are not the “same” in all countries. In other words, “neutrality,” in this context, is no longer valid. This goes beyond the basis on which taxation should be imposed, i.e., residence or source but do illustrate that we should not be holding fast to CEN and CIN, depending on one’s point of view, as the foundation for tax policy.

When the entity classification rules [commonly referred to as “check-the-box” regulations (“CTB”)] were introduced in 1997, it is common knowledge that various companies took the opportunity to minimize the excessive draconian provisions of Subpart F. Not surprisingly, some of these companies found themselves having to deal with two old Subpart F provisions, i.e., the sales and manufacturing branch rules. Why these even existed in the first place defies logic. Companies which are based in the developed countries (primarily, the OECD members) do not have to contend with such antiquated and stifling provisions. Not content with outdated and draconian provisions, once more Treasury tried to curtail the positive aspects of the CTB rules. End result, more complexity, more litigation, additional costs and waste of resources.

Let us examine two areas to illustrate the “folly” thereof: one in Subpart F and one dealing with a particular sourcing rule.

Absent the so-called “same country exception” and any CTB opportunities, interest paid between two CFCs is taxed on a current basis in the hands of the U.S. parent (“USP”). The following is a typical scenario: USP has two wholly-owned subsidiaries (“A” and “B”) in Country A and Country B, respectively. A and B are brother-sister and are corporations for all U.S. tax purposes. Both A and B conduct an active trade or business. However, A is extremely profitable and has excess cash on hand. B needs funding to modernize to become competitive. If A lends the funds to B, USP has Subpart F income taxable on a current basis. Therefore, B turns to a third-party bank to borrow the funds. Is this an economically efficient way to use of the funds of the group? Does anyone in Congress not see why “inversions” took place? For portfolio-type of investments, we already have the PFIC rules to address this issue. However, that should be the sole exception. Subjecting sound efficient allocation of resources were needed to current taxation is pure folly.

What was Congress’ answer? Section 7874 of the AJCA. Instead of repealing the draconian provisions of Subpart F which were the “root” of the problem, section 7874 was introduced. What did section 7874 do? Firstly, it created more complexity and, secondly, it caught transactions which had absolutely nothing to do with inversions. If another country applied a similar provision, Congress would be livid. To illustrate: USP owns A and B. If USP decides to form a holding company (“C”) in Country C and transfers the shares of A and B to C in a stock-for-stock exchange, would Congress accept, for example, Country A’s position that C is now a tax resident of Country A?

The other area deals with the sourcing rules in the telecommunications sector. Many countries around the world have opened their telecom industry to competition (previously, a monopolistic situation). The following is a typical scenario and one which was encountered:

USCo is in the wireless telecommunications business. It wanted to expand outside the U.S. and saw an economic opportunity to so do. Under the foreign country’s requirements, USCo was required to form a local company (“LoCo”) to apply for the license and, if granted, to operate the cellular business in that country. LoCo was granted a license and signed a significant number of subscribers in that country. **All** of its customers are “locals.” Its competitor was the previous monopoly which was **not** U.S.-owned (“MCo”). MCo does not have a fixed place of business in the U.S. and, like LoCo, all of its customers are “locals.” Where does the “idiocy” arise? If LoCo’s customer makes a call from his home to, say, someone in California, to LoCo, for U.S. tax purposes, the revenue therefrom becomes U.S. source income. At the same time, MCo and its non-U.S. owner do not have to contend with this issue. Does one see a theme emanating throughout this discussion? Stifling the ability of U.S.-owned enterprises to compete. Why? Because *“we believe CEN and CIN are very valid principles on which fiscal policy should be based.”*

**As to the corporate area, the following are proposed:**

1. Except for income from pure portfolio-type of investments (which should be addressed in the PFIC provisions), repeal Subpart F in its entirety;
2. Amend the provisions of section 7874 to ensure that true “non-inversions” are not caught. The “fix” in the “Tax Technical Corrections Act of 2005” does not solve this problem. Since the original provision was retroactive to March 2003, this amendment should also be retroactive to March 2003;
3. Eliminate all “preference” items. This, then negates the need for AMT and reduces the need for all the associated reporting on large book-to-tax differences. For example, there would not be a need to expense stock options. Given that employment income and capital gains are taxed at the same rate, the adjusted basis to the employee is simply the price paid for the stock on exercise thereof;
4. Dividends received from CFCs in an active trade or business should be exempt under strict reinvestment provisions. Included in the definition of an active trade or business would be intragroup financing provided the beneficiary of the funding is in an active trade or business; and,
5. Non-manufacturing income to be taxed at 20% while manufacturing income (as envisioned in section 199) to be taxed at 15%.

**OTHER**

**Due to recent developments, Congress and the Administration must act on “reigning-in” commodity traders, in particular those in the oil sector. In the 1990s, there was a concerted effort globally on putting a “leash” on the currency traders whose actions had wreaked unnecessary havoc.**

Notwithstanding that there are influences which will dictate the price of oil, what is now occurring is that these traders are using every excuse to reap substantial profits at the expense of the global economies. For example, storms in the Gulf of Mexico always arose and we never saw spikes in prices. Today, just a “whiff” of a pending storm and these individuals use this as an excuse. If immediate action is not taken, there would be severe disruptions to economies and a vicious circle begins: price pressures fuel inflation which requires an increase in interest rates.

Therefore, it is proposed that a special tax equal to 75% of the gain realized by a trader should be imposed. This may seem harsh but harsh measures are necessary to put back some semblance of order.

**CONCLUSION**

Of course, the preceding are only in broad terms and do not purport to address all aspects of tax reform. They do, however, attempt to address those areas which would achieve the objectives as previously outlined.

To reiterate, it is the belief that the proposals presented herein should result in:

1. Increasing the competitiveness of U.S. persons;
2. Increased revenue flows to the Treasury;
3. Reduced complexity and providing a foundation for fairness and equity;
4. Increased compliance by providing a disincentive to avoid taxes;
5. Protecting and even increasing revenue flows to the Treasury;
6. Increased investment in human resources and plant and equipment;
7. Increased productivity;
8. Increased savings thereby putting less pressure on the Social Security system; and,
9. Keeping inflationary pressures at bay.

Redwood City, California 94062  
August 30, 2005

Dear Honorable Chairman Camp and Ranking Member McNulty:

I have submitted my testimony and shared my story at the President’s Tax Reform Panel in May 2005, as well as for H.R. 5141. I now wish to share my story with you in hopes of garnering your support and leadership of the Honorable Sam Johnson’s H.R. 3385.

My story is simple, and yet so unfair and outlandish that few people outside of government believe it was possible. Quite simply, I paid \$334,000 in AMT taxes for stock I never sold (and therefore never profited from) and which was worth less than \$100,000 at the time. How is it possible to pay more in tax than an asset (stock) is worth? Alternative Minimum Tax, or AMT. I now have a huge AMT “tax

credit” that I can never hope to recover. I understand the logic that was used to originally justify AMT, but the law as created was clearly flawed. Thousands, like me, have been forced to sell everything for a tax bill that is several times the worth of their gains/income, again, phantom profits.

In my own story, I went through both severe financial and emotional strain. The sleepless nights, the new anti-depressants (which I never took before), the new 2nd mortgage was almost overwhelming. I hold on as an optimist to this day that this injustice will someday be corrected. I know of others that were not able to hold on, and who have taken their own lives.

I respectfully and urgently request your support of H.R. 3385.

Ed Terpening

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Atascadero, California 93422  
August 31, 2005

Dear Honorable Chairman Camp and Ranking Member McNulty:

I wish to share my story with you in hopes of garnering your support and leadership of the Honorable Sam Johnson's H.R. 3385.

I am a technical support engineer and I work for a tech company located in San Luis Obispo, California and live nearby in Atascadero with my husband and two young children (10 months and 3 years). Although I make a decent salary, I'm not only the primary breadwinner in our household, but I pretty much support the family right now. My husband is a part-time student, part-time stay at home dad and part-time auto mechanic. He is back in school to earn a degree and change careers not only for his fulfillment, but also so that we may provide a better life for our children. We drive used cars and don't take fancy vacations. We are definitely your everyday people.

Several years ago, I was offered stock options through my company. My husband and I were anxious to exercise these to hopefully have a long-term investment that might help in the future with college funds or retirement. We knew there would be tax implications and were aware of AMT, but felt the investment was the smart thing to do. We purchased those options through the years 2000 to 2002. When filing our taxes the following April each of those years, we were shocked at how much of our calculated taxes for the previous year was from AMT. It may not sound like much to some people, but thousands of dollars to this family is at least a month's expenses, maybe two. This is something we can't afford to be paying when we are struggling to make our mortgage each month. And now, being faced with more stock options offered at my new company, I am terrified to purchase them until I sit down and compute to see if we can afford to do it this time around. I'm sad to say that I predict we will not be able to take advantage of this opportunity.

I respectfully and urgently request your support of H.R. 3385.

Heather Thayer

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Shoreview, Minnesota 55126  
August 30, 2005

House Ways and Means Committee

Dear Members of the House Ways & Means Committee:

My name is Phil Thompson, and I have submitted my testimony and shared my story at these past events:

- 6-15-2004, Hearing on Tax Simplification, Oversight Subcommittee
- 6-08-2005, Hearing on Tax Reform, Full Committee
- April/May 2005, Senate Finance Committee Chairman Grassley
- Spring/Summer 2005, President's Tax Reform Advisory Panel

I now wish to share my story directly with you in hopes of garnering your support and leadership of the Honorable Sam Johnson's **H.R. 3385**.

I am 44 years old. In 1997 I accepted a position as a software engineer with a software company located in Roseville, Minnesota. In addition to salary, I was given

a one-time grant of 3,000 incentive stock options (ISOs) when I started. **This was the first time I had ever received stock options in my life.** Between 1997 and 2000, the company grew rapidly, and the stock split a few times, and the increasing stock price ended up making those options very valuable. Before the year 2000, I had exercised and sold some of the options that had vested, mainly to get a down-payment for my first house. But in the year 2000, because more than half of my options had vested, I decided to accelerate exercising many of these options.

I knew very little about the tax ramifications of exercising and holding ISOs, so I hired a professional tax advisor who had been recommended to me by several co-workers (who were in situations similar to mine). My tax advisor recommended an ongoing, well-timed exercise-and-hold strategy, which would allow me to best benefit from the tax laws over the next several years. This seemed logical to me. **Unfortunately, he did not warn me of the risks involved with exercising and holding ISOs, should the stock price decline dramatically.** And because until that point I had only done same-day sales of my options, I was not familiar with the different tax treatments.

During the year 2000, I exercised and held approximately 4,500 options, worth approximately \$470,000 on the purchase date. And for most of the year 2000, the stock price continued to trade considerably higher than my purchase price. My trading window for the year closed in mid-December of 2000, and even in early December the stock price was still above my purchase price. Of course, the stock price declined dramatically thereafter. I didn't realize there was a problem until **my tax advisor told me in March of 2001 that I owed approximately \$165,000 in combined federal and state tax. I was shocked and amazed, because my gross annual salary at that time was only about \$85,000.** Frankly, I didn't think it was possible that a taxpayer could be required to pay more in taxes than he/she actually earned.

After my tax advisor explained that I would not be able to discharge the AMT by selling the shares (because the AMT is an immediate tax on **potential** earnings, not on real money), I was forced to exercise and sell even more options in order to cover my tax liability. I was luckier than most, in that my company's stock price decline was less rapid than most tech stocks at that time.

**As of this writing in June 2005, the federal and state governments still hold over \$108,000 of my money in so-called "AMT credits."** This is money that I could use to pay off my house, invest in my future, and prepare for retirement.

After being victimized by the AMT treatment of incentive stock options, I have the following observations:

1. **The alternative minimum tax can be an unfair tax on phantom gains that may never be realized.** For incentive stock options, because the AMT is based on the tax that would be owed on the day of exercise, it does not take into account the possibility of a dramatic drop in the stock price. It also does not seem to take into account that for various reasons (holding periods, black-outs, complexity of the rules, etc.) a taxpayer may be unable to sell the shares in response to such a dramatic drop.
2. **The AMT rules are very difficult to understand.** Even with the assistance of a professional tax advisor, I encountered a situation that could have easily bankrupted me. And since the year 2000, I have read 2 books on the AMT, and done much Internet research on the AMT. I still don't feel like I understand the AMT rules very well. Each rule seems to have multiple "except if" clauses. Thanks to the complexity of the AMT rules, I am forced to hire a professional tax advisor every year to prepare my tax return. I also find it very difficult to plan future financial moves because I am unsure of how they will affect my tax liability and the return of my AMT "credits."
3. **Current tax laws allow no solution to easily recovering the AMT taxes pre-paid on phantom profits.** Even if a citizen like me is able to meet the tremendous burden of the AMT, the rules for returning the AMT "credits" are designed to make it a very long and arduous process, in some cases requiring many decades. Recovery of "credit" is hastened only by dramatically increasing your earnings and/or by creating capital gains. And both of those solutions are not generally easy to do! **In my personal opinion, speeding up the return of the AMT "credits" is the most important part of AMT reform.**
4. **AMT "credits" (prepaid taxes) are lost forever if the citizen dies.** If I was to die in an accident tomorrow, the \$108,000 of mine that the government holds in AMT "credits" would be lost to me and my heirs forever.

Although the tax rules claim to provide a benefit for investors who exercise stock options and hold onto the stock, **I will never again exercise and hold any in-**



**centive stock options. Because of the AMT treatment of ISOs, it's just too much of a gamble.**

**I respectfully and urgently request your support of H.R. 3385.**

Thank you for your attention.

Phillip Thompson

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Tewksbury, Massachusetts 01876  
*June 20, 2005*

To Honorable Chairman William M. Thomas and House Ways and Means Committee

Dear Chairman Thomas and Committee Members:

In 2000 my husband and I purchased some of my options from Nortel Networks. I had been there for over 8 years so the options were fairly low priced. Our goal was to start acquiring shares to sell at some point to put towards our kids education, we figured if we bought and held for a year we would have 20% more to put down, but not having to pay the short-term capital gains. Logical, until we learned that next April 15th that we owed the government approximately \$75,000 for shares that we paid approximately \$8,000 for.

I left my accountants office in tears. And since my accountant is my Dad, he felt pretty bad about it. We didn't have \$75,000 available; we had to take it out of our home equity loan. I was physically sick for a month thinking about it.

It is now 2005 and we finally did get to recuperate some of our AMT tax when we sold some shares in 2003, but it is going to take us 3-4 years to get it all back. So our kids got whacked in the end with us not being able to put as much money into their college savings funds. I am lucky that my husband makes over \$100,000 a year and it won't take us 20 years to get back all the money. I can't imagine all of the people out there that don't make a lot of money and were just trying to get ahead and their lives were ruined financially.

Some of the stories of the people who are members of ReformAMT are heart wrenching. People lost their homes, declared bankruptcy . . . etc. I am only thankful that I was not one of those people and was fortunate enough to have the financial means to deal with the loss.

Please contact me if you need any more information.

Susan Timmons

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Batavia, Illinois 60510  
*August 26, 2005*

Dear Honorable Chairman Camp and Ranking Member McNulty:

I have not previously submitted my testimony to any previous Ways and Means Committee proceedings.

I now wish to share my story directly with you in hopes of garnering your support and leadership of the Honorable Sam Johnson's H.R. 3385.

I am writing for myself and others in a similar position who have suffered financial hardships as a result of the Alternative Minimum Tax.

I work for a small technology consulting firm that used incentive stock options as part of its compensation. Believing in the company and its future and being hamstrung by rules that dictated when I had to exercise and when I could sell, I exercised and held good portions of the stock granted to me as ISOs. However, the antiquated and complex rules of the AMT, as I understand were created to catch the wealthiest individuals in the U.S. from sheltering gains from the government, have now caught unaware many middle and upper middle class Americans who have worked hard for what they have earned. Since the AMT requires the gains to be calculated at the time of exercise not at the time of sale, I owed nearly \$250,000 in taxes based on paper profits not on actual gains. Calculating tax on paper gains is wrong and unfair. While I did not suffer as badly as others, at the time the \$250,000 was twice my annual income. While I continue to work for the same company today and I continue to hold its stock, I am very disenfranchised with the tax

policy and urge you to take a stand and retroactively eliminate the AMT. Demonstrate to the people that you represent, that you believe the government should not continue to support unfair tax policies and now tax policies that discourage individuals from taking chances with small businesses.

Thank you for your time and consideration.

I respectfully and urgently request your support of H.R. 3385.

Daniel Toth

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Winnetka, Illinois 60093  
August 22, 2005

Dear Honorable Chairman Camp and Ranking Member McNulty:

I have submitted my testimony and shared my family's story at these events:

- 6-15-2004 Hearing on Tax Simplification, Oversight Subcommittee
- Spring/Summer 2005, President's Tax Reform Advisory Panel

I now wish to share my story directly with you in hopes of garnering your support and leadership of the Honorable Sam Johnson's H.R. 3385, the AMT Credit Fairness Act.

My name is Ron Vasaturo and I am writing on behalf of the Vasaturo family. We're writing to ask that you help change the Alternative Minimum Tax (AMT) provisions which have caused a great hardship to our family, unfairly. We ask that you recommend reform to the Alternative Minimum Tax provisions to allow the AMT credit for the Prior Year Minimum Tax to be applied up to 100% of the taxpayer's ordinary income tax. We are middle income taxpayers in our 50's that have a large AMT credit we will take to our grave unless the AMT provisions are revised to allow use of the credit towards ordinary income tax.

In 2001 we had to pay an extremely large alternative minimum tax—\$250,000—for money we never received and never will receive. The \$250,000 AMT tax was on top of the taxes we paid on our earned income. In 2000, I worked for a high technology company that provided me with incentive stock options each month, in lieu of any annual salary increases. Because my wife and I were in our 50's we decided to exercise the stock options each month and set aside the stock for retirement purposes. The company encouraged this, emphasizing the benefit of long-term capital gains if we held onto the stock. We had no idea that the difference between the exercise price and the market value of the stock at the time of exercise would be considered income for alternative minimum tax purposes. We had never experienced stock options before. We thought we were to pay any taxes owed when we sold the stock, if we realized a gain. Having worked hard our entire lives and saved conservatively for a hoped-for retirement, we have always paid our fair share of taxes as part of what it means to be citizens of this country. So we expected that any real gain from stock options would be appropriately taxed. However, in 2001, when we prepared our tax return, we learned of our mistake and our whole world turned upside down.

By 2001 the stock had dropped precipitously in value (the tech bubble burst), and, within a few months, my employer went bankrupt and I lost my job. We sold the stock for pennies a share, at a very substantial capital loss. We paid the huge AMT sum we owed in 2001 by liquidating our bank account and retirement mutual funds, funds we held sacrosanct and had never touched before. Understandably, we had spent many years saving towards achieving a retirement that could provide us with at least some dignity in our ability to meet life's future costs (medical expenses, etc.). Because of our ages (now 55 and 57), we are possibly the flip side of what is too commonly, and easily, thought of as the young college graduate who joins the Internet dot-com for fame and quick riches. We simply do not have the earning years left to recoup what the AMT has taken from us as taxes for money that we never received.

As we understand, the AMT we paid because of incentive stock options is supposed to be a pre-paid tax that can be recouped in later years. That is not the way the law is working for us. We don't earn anywhere near enough income to be able to use our AMT credit. (Ironically, President Bush's recent tax cuts exacerbated this situation.) In order to be able to use the credit, one has to have a very high income—otherwise the ordinary tax does not exceed the AMT, and one can't use the credit.

In 2001 and 2002 when we sought assistance and information from the IRS on how incentive stock options, capital losses, and AMT work, we only received incorrect and conflicting information. The IRS staff, and I spoke to several different people at the Service, did not seem to understand how the alternative minimum tax provisions work. When we sought assistance from tax accountants, we discovered the tax accountants did not understand this complex area of the law.

This seems very unfair that we have been victimized so harshly by the unintended consequences of the Alternative Minimum Tax. We ask that the law be revised so that we can fully apply the credit to our ordinary income tax. We are seeking your help in recommending that taxpayers be allowed to apply the AMT credit for the Prior Year Minimum Tax up to 100% of their ordinary income tax.

Thank you very much for the opportunity to provide you these comments and we hope that this Panel will recommend changes to the law that will enable us to fully use our AMT credit so that we can one day pursue a retirement that we have worked so long and hard towards.

I respectfully and urgently request your support of H.R. 3385.

Very Sincerely,

Ronald Vasaturo

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#### **Statement of Mike Wertheim, Oakland, California**

I have submitted this story in previous years. I am submitting my story now to ask you to please support bill H.R. 3385.

I am an average middle class employee. In 2000, I worked for an Internet company called Critical Path. I received incentive stock options as part of my compensation. I exercised the stock and have not sold it. No one ever advised me to sell the stock before the end of the calendar year to avoid certain Alternative Minimum Tax problems. By the time my accountant prepared my income tax bill for 2000, the Alternative Minimum Tax on my stock was \$64,000. This is despite the fact that the current value of the stock at the time was only \$8,000 (and is now worth only \$500). The \$64,000 tax bill far exceeded my net worth.

I paid the entire \$64,000 tax bill on April 15, 2001 and generated a \$64,000 tax credit, by liquidating savings and borrowing money from my family. At this rate, it will take me over 20 years to use up my AMT credit because the tax code allows me to apply only \$3,000 of my AMT credit towards my income tax each year. Essentially, I have been forced to make a \$64,000 20-year loan to the government interest-free.

Some day my wife and I would like to buy a house and send our daughter to college, but both of those plans are on hold until we can regain our financial standing. After my parents loaned me money to pay my tax bill, the rest of the family is feeling the financial pain, too. My parents, who are both in their 60's, no longer feel that they have enough money for their retirement. All of this happened because the AMT laws forced me to pay a large tax on income that I never actually received.

H.R. 3385 will be a great improvement to the tax code. Taxes should not exceed the value of the actual gain being taxed. It will make it possible for people in my situation to make quicker use of AMT credit. I respectfully and urgently request your support for H.R. 3385.