



From the Desk of Dean Zerbe.



America's Destructive Tax Code

Reprinted from Forbes.com

(May 28, 2009)

It's time to reverse tax policy that has helped to cripple American manufacturers.

The country music song "A Little Less Talk and a Lot More Action" sums up what manufacturers need when it comes to D.C. and the new administration. Politicians of all stripes love to pronounce paeans to lunch-pail Joe and Jane, but when it comes to tax policy, there's nothing but cold, weak coffee in the thermos.

The tax provisions in the stimulus bill did almost nothing to help U.S. manufacturers. The Senate had accepted an amendment that would have accomplished a key goal for manufacturers—getting dollars into their hands immediately—by extending the net operating losses (NOLs) carryback and the general business credits carryback for five years. This would have allowed businesses to immediately file refund claims and increase their cash on hand. Not to be. In conference, the administration and congressional leaders stripped out these provisions.

What can the government do to help manufacturing business both today and tomorrow? First, today. More than anything, manufacturing businesses need dollars in hand. The unfulfilled Senate proposal of a five-year carryback for NOLs and general business credits is a good starting point.

Another possibility would be to provide a payroll holiday for business. The new administration has worn out pens writing checks to individuals with no federal income tax liability, citing that they do have payroll liability. But that same logic seems to be forgotten when it comes to the billions of dollars in payroll taxes paid by businesses. A payroll holiday for manufacturers would provide immediate relief and benefit.

Congress could pass legislation to provide

that businesses would not be subject to payroll taxes (social security, Medicare, unemployment) for the rest of the year. This tax relief would immediately help all businesses—small and large. Too often, tax relief proposals for business only help "C" corporations with federal income tax liability. Such payroll tax relief would also serve to remove what effectively is a tax on employees and encourage new hires.

What about for tomorrow? Here are a few Dos:

50% Domestic Production Deduction.

Manufacturers currently get a small break (Section 199) on the corporate tax—effectively a 3% rate reduction from the U.S. corporate tax rate, already one of the highest in the world. You want to help domestic manufacturing? At a stroke, a 50% reduction in the corporate rate for manufacturers would make them more competitive with overseas facilities.

Allow Small and Mid-Sized Manufacturers to Use the Same Tax Incentives as the Big Boys.

The individual alternative minimum tax (AMT) greatly limits the ability of small and medium manufacturers from taking many key business tax credits. Currently, if you are an owner of a manufacturing business (organized as a pass-through entity such as a subchapter S corporation or partnership), and are subject to the individual AMT, you cannot take the Research and Development (R&D) Tax Credit, the Work Opportunity Tax Credit (WOTC), the disabled access credit, the employer-provided child care credit—over 30 credits in all. It is an uneven playing field tilted strongly against small business. Congress should end this unfair treatment—and do so retroactively.

A Competitive Research-and-Development Credit.

Washington thinks the angels should be weeping for the fact they're considering

making the R&D credit permanent. That's fine, but let's keep in mind that the U.S. R&D credit is thin gruel compared to the incentives of other countries. Manufacturers that are seeing the long-term horizon past the current economy recognize that they need to invest aggressively in R&D, and we need a tax code that encourages those investments. If we are going to keep (and grow) manufacturing in this country, the path will be lit by research and development.

And a few Don'ts:

Cap-and-Trade.

Congress needs to be extremely mindful of the burden a cap-and-trade policy on carbon dioxide emissions could and would impose on manufacturing.

Last In, First Out.

Congress and the administration need to revisit the proposed elimination of the LIFO accounting method, in which a company treats the first units sold as the most recently purchased. While Congress' ire with this accounting method is mostly directed at big oil, the current draft legislation will clobber many small and mid-sized manufacturers as well.

More IRS Audits.

The proposed massive increase in IRS audits needs to be rethought. While this has been sold as a focus on offshore tax weasels, I have found that as much as Congress envisions platoons of IRS agents wearing Tommy Bahama shirts in the Caymans, the reality always is more IRS agents in sports coats knocking on doors in Camden, N.J.

This projected big increase in IRS auditors is particularly troubling given that, while there are a good number of trained, qualified IRS agents, there is also a growing



From the Desk of Dean Zerbe.



tendency for a few at the IRS to basically throw out a number for taxes owed without any real review of the taxpayer's facts and application of the law. These "spaghetti-wall-stick" audits are devastating for businesses that lack the time, energy and resources to try to keep their business afloat in this tough economy and fight the tax man at the same time. Congress and the administration should look less at big increases in IRS agents and instead focus on ensuring the IRS hires qualified workers, providing them top training and ensuring quality control and good service.

It is time for Congress to take a lot more action when it comes to tax policy – action that will encourage manufacturing domestically.

Dean Zerbe is former tax counsel for the Senate Finance Committee and is now National Managing Director for alliantgroup, LLC, a provider of tax strategies and services to manufacturers.

*Dean Zerbe
National Managing Director
alliantgroup, LP
dean.zerbe@alliantgroup.com
www.alliantgroup.com*

