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Tax Reform: Incentives That Work for All Businesses

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The talk of tax reform has been driven by talk of the 1% and the 99%, but there has been little discussion of the 95% and the 55%: the 95% of businesses that are organized as pass-through entities (S-corps, LLCs, partnerships, etc.) and the 55% of all private-sector workers in this country who work for the 95%.

Far too many policymakers in D.C. are obsessed with only the 5%—companies organized as C-corps. I fear this fixation is because many in D.C. came from big corporations and they look forward to going back and working for a big corporation.

The tax code, unfortunately, reflects this blindered focus on the 5%, with the 95% of pass-through entities often hamstrung or flat-out blocked from taking advantage of the same credits, deductions and incentives that are in the tax code ostensibly for all businesses. It is simple fairness and good policy that small and medium firms should have the same access to tax incentives.

Congress and the administration should consider the common ground that can be realized by addressing tax reform that ensures all businesses are equally eligible to benefit from the credits, deductions and incentives in the tax code.

As an example, the Research and Development Tax Credit is the biggest incentive out there for businesses (roughly \$10 billion a year). Currently, the overwhelming percentage of the R&D Tax Credit goes to large corporations. Small and medium businesses are doing innovative work that qualifies for the R&D Tax Credit, but we see first-hand that the tax laws create a number of bars that translate into a high percentage of these innovative companies in the 95% not being able to take the R&D Tax Credit.

What is the main bar for the 95%? The Alternative Minimum Tax (AMT) that applies not only to individuals but also owners of pass-through entities.

The good news is that the message of creating a level playing field for businesses when it comes to tax credits, incentives and deductions is beginning to be heard. Thanks to Congressman Kevin Brady (R-TX) the House has acted on an extension of the R&D Tax Credit that will remove the AMT bar and on July 21, the Senate Finance Committee cleared tax extenders legislation that, if passed, would retroactively extend the R&D Tax Credit for two years.

The Senate bill would also remove the AMT bar and would essentially make the credit refundable for small businesses by allowing companies that have existed less than five years and have less than \$5 million in annual gross receipts to take a credit of up to \$250,000 against payroll taxes paid on employee wages. Removing the AMT bar for the R&D Tax Credit enjoys bipartisan support in the Senate.

On a similar note, the administration took a step forward on greater fairness for small and medium businesses by allowing the R&D tax—the Alternative Simplified Credit (ASC)—to be taken on amended returns. While this relief was for all businesses, the real beneficiaries were the 95%.

These examples are just the beginning of what can and should be done to ensure fairness for the 95%. Current and future tax incentives should not include adverse effects or disproportionately burden small and medium businesses.

There are a host of provisions that Congress could immediately consider for increased fairness for the 95% and to the benefit of the 55% of private-sector workers. In addition, the tax-writing committees and the small business committees should call on the Joint Committee on Taxation to provide a detailed analysis of all the barriers and limitations for small and medium businesses when it comes to credits, incentives and deductions.

A road map is always helpful when you are navigating tax reform.



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