



**TESTIMONY OF RICHARD K. ARMEY**

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**before the**

**HOUSE BUDGET COMMITTEE**

**U.S. HOUSE OF REPRESENTATIVES**

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Good morning Mr. Chairman and Members of the committee. I am Dick ArmeY, former House Majority Leader, and currently Co-Chairman of FreedomWorks, a non-partisan, non-profit grassroots organization with more than 360,000 members that works for lower taxes, less government, and more freedom. Thank you for inviting me here today to discuss the issue of fundamental reform of the U.S. tax code.

As you know, Speaker Dennis Hastert has renewed the call for sweeping, fundamental reform, and at the Republican Convention this summer President Bush further revitalized the issue in his acceptance speech when he told the nation, "The American people deserve-- and our economic future demands-- a simpler, fairer, pro-growth system."<sup>1</sup>

This debate is important because America has one of the most outdated and complex tax codes in the industrialized world. Taxpayers are forced to spend many frustrating hours fighting forms and figures, digging for documentation, and checking and rechecking their math to make sure everything is right first to comply with the tax code, and gain to make sure they do not fall prey to the parallel alternative minimum tax (AMT). The code exceeds 60,000 pages<sup>2</sup>, and it takes Americans 6.2 billion hours to complete their taxes every year. Simply complying with the tax code imposes national costs as high as \$194 billion, according to the Tax Foundation.<sup>3</sup>

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<sup>1</sup> "Transcript: George W. Bush", *Fox News*, 9/02/04

<sup>2</sup> "Fiscal Facts and Figures", *The Cato Institute*, 2004

<sup>3</sup> "The Cost of Tax Compliance", *The Tax Foundation*, 2/02

Even worse, these cost of compliance figures do not include the broader economic distortions and inefficiencies caused by the current code that begins with an overly broad definition of income—which has necessitated the creation of any number of “loopholes”, i.e., exemptions, deductions and credits to ameliorate the perverse disincentives to work, save and invest resulting from that overbroad definition of income. For example, Congress taxes savings and investment-- the engines of economic growth-- two, three, and sometimes even four times. This punitive approach puts many American businesses at a competitive disadvantage and even encourages some of them to move offshore. John Kerry may like to scorn "Benedict Arnold companies,"<sup>4</sup> but these corporate inversions are often rational moves in response to anti-business tax, labor, and regulatory policies coming out of Washington, D.C.

Most importantly, I think, is that the current tax code offends our sense of what it means to be an American. This country was founded on the right of everyone to be treated equally before the law, but the current tax system doles out special treatment to those who have the power and money to lobby for it. The code is so complicated and expansive that it now touches nearly every aspect of our lives. Americans can no longer make a decision in the family or in business based simply upon family or financial economic criteria. We have to make decisions based on tax criteria, and it is an undue burden. Politicians, in this way, are using the tax code to expand the reach of government control of our economy and of our lives.

Complete and fundamental tax simplification and reform is the only answer. Other ideas, such as giving more power to the IRS, will fail or even make the problem worse. The IRS assessed nearly 28 million penalties last year<sup>5</sup>, and it wants more power and control.

No, it is time to completely scrap the tax code. We need to get rid of all the code's social engineering and special interest handouts. We need a new tax code that recognizes the goodness of the American people, not the guile of the federal government and crafty tax accountants.

No doubt, fundamental tax reform has been on the Congressional agenda since Republicans first took control of Congress in 1994. At that time, Congress created the National Commission on Economic Growth and Tax Reform, chaired by Jack Kemp, which concluded in 1996 that America needed to completely scrap the tax code.<sup>6</sup>

### **The Kemp Commission produced Six Points of Principle for tax reform:**

#### **1. Economic growth through incentives to work, save, and invest**

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<sup>4</sup> “The Kerry-Edwards Plan to Protect and Expand Automotive Jobs in the United States”, [www.johnkerry.com](http://www.johnkerry.com),

<sup>5</sup> *Internal Revenue Service Data Book 2003*, page 34.

<sup>6</sup> “Unleashing America’s Potential”, *National Commission on Economic Growth and Tax Reform*, 01/96

2. **Fairness for all taxpayers**
3. **Simplicity, so that everyone can figure it out**
4. **Neutrality, so that people and not government make choices**
5. **Visibility, so that people know the cost of government**
6. **Stability, so that people can plan for the future**

It is interesting to note that this past July, Jack Kemp and I helped merge Empower America and Citizens for a Sound Economy (CSE) into a new organization, FreedomWorks, where we both serve as Co-Chairmen. Along with C. Boyden Gray, Jack and I are leading a renewed grassroots effort to educate and mobilize ordinary Americans on the tax code and the urgent need for reform.

No doubt, there is a way forward. Supporters of fundamental tax reform have rallied around five basic principles-- "Five Easy Pieces"-- first put forward by veteran Washington tax lawyer Ernest Christian. They are 1) Lowering and flattening marginal rates, 2) moving towards full expensing of business investment, 3) reducing or eliminating the double taxation of dividends and capital gains, 4) expanding tax-free savings vehicles, and 5) international tax reform.

These five goals will move us towards a simpler, fairer, and flatter tax system. Reducing marginal rates makes the tax burden more equitable and creates incentives for people to work. As both Ronald Reagan and George W. Bush have proved, cutting marginal tax rates creates incentives to work *more*, save *more* and invest *more* resulting in greater economic growth. Allowing corporations to fully expense investments in business plant, equipment and technology will maximize business investment necessary for long-term economic growth. And it's obvious that lowering taxes on dividends and capital gains reduces the penalties on saving and investment, creating economic growth.

Finally, the current code is hostile to U.S.-based firms that have significant operations overseas. The Kerry-Edwards detailed international tax reform plan states, "John Kerry does not believe that we should force a U.S. company that chooses to create jobs in the United States to pay higher taxes and suffer a competitive disadvantage with a company that chooses to move jobs to a tax haven and keep profits there permanently." His solution? Eliminating the tax deferral for foreign-earned income as they earn it rather than being allowed to defer taxes.

In other words, Senator Kerry would create incentives for companies to take not just the jobs overseas, but to move the entire operation overseas as well. The Kerry campaign misses the obvious solution. As is written in their own report, a U.S.-based firm can "expect to pay an average tax rate of 31 percent. When this company invests abroad, it faces an average tax rate of 21 percent." The same Kerry report acknowledges that 80

percent of U.S. manufacturing assets abroad are based in countries with tax rates lower than the rate in the United States.

It seems obvious to most people that if U.S. tax rates are so high and uncompetitive that firms are being encouraged - driven - overseas, the solution is not to punish the firms, but to reduce the tax rates to more competitive levels. Cutting the tax rates by 5 percent, as Kerry wants to do, is a good starting point for debate, but is simply insufficient to make America's tax code more competitive internationally.

The ultimate purpose in all of this is that we need a simple pro-growth tax code that is consistent with our values. A better code would reward hard work, encourage investment, and reflect our fundamental belief that individuals can spend their own money better than Washington can. This new system, by harnessing the power of freedom, would make the American economy stronger and more dynamic. I think that millions of taxpayers agree. Americans deserve a "simpler, fairer, pro-growth system," and we are working hard to that end.

In the past, as you may recall, Citizens for a Sound Economy (CSE) helped organize the Coalition for Fundamental Tax Reform (CFTR), a loose confederation of groups committed to fundamental overhaul of the tax code. One of the group's activities was to promote a set of six principles that were essentially a distillation of the Kemp Commission's Six Points of Policy and Six Points of Principle.

The CFTR principles were incorporated into a "Commitment to Tax Reform" pledge that candidates for public office were asked to sign. As everyone here knows, candidate surveys and pledges of this kind can be a powerful political and policy tool.

Now that Citizens for a Sound Economy has joined with Jack Kemp and Empower America as FreedomWorks, we will again be leading with a tax reform pledge based on core principles that should guide sound tax reform. For the purposes of discussion, I'd like to share our current working draft of a new legislative tax reform pledge:

**COMMITMENT TO TAX REFORM CANDIDATE PLEDGE  
[WORKING DRAFT]**

I pledge to support tax reform legislation that:

**Applies a single, low rate to all Americans**

**Provides tax relief for working Americans**

**Eliminates the bias against savings and investment**

**Requires a supermajority of both chambers of Congress to raise taxes**

**Protects the rights of taxpayers and reduces tax collection abuses**

## **Promotes economic growth and job creation**

I think you'll all agree that these ideas all form an excellent basis from which to build consensus on fundamental reform. And, rest assured, we, at FreedomWorks, are not standing still. FreedomWorks and our 360,000 members nationwide care deeply about our economy and the state of our tax code. On behalf of all of our members, we look forward to working together you to scrap the code, replacing it with a system that is fair, flat, and simple.

Thank you.