



U.S. SENATE COMMITTEE ON

Finance

SENATOR CHUCK GRASSLEY, OF IOWA - CHAIRMAN

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Opening Statement of Chairman Grassley
Hearing, "A Tune-up on Corporate Tax Issues: What's Going on Under the Hood?"
Tuesday, June 13, 2006

In today's hearing, we will primarily focus on the current state of our corporate tax system. But we'll also touch on basic issues to consider in the context of business tax reform – lowering rates and broadening the base. The continued globalization of our economy and the complexity of business activity present significant challenges to our corporate tax system as a whole, and to the administration of that system. The complexity of the tax code itself creates burdens and inefficiencies for taxpayers and the IRS, although some taxpayers may view complexity as creating opportunities for tax avoidance.

According to the Congressional Budget Office, corporate income tax receipts were a record \$278.3 billion in 2005, up 47 percent over the prior year and representing 2.3 percent of GDP – the highest percentage since 1980. The first 8 months of fiscal year 2006 show the trend continuing with corporate tax receipts up 30 percent over last year. The recent surge in corporate tax receipts is due in large part to the strong performance of our economy. Corporate tax receipts have gone up along with rising corporate profits resulting from a growing economy.

In addition to a growing economy, I think some of that increase is also because of continuing efforts to combat corporate tax abuse and improve corporate tax compliance. For example, in 2004, Congress enacted my package of legislation cracking down on tax shelters and requiring companies to publicly disclose in SEC filings penalties for failing to report a tax shelter, so investors will know whether a company is violating tax shelter laws. These provisions have provided the IRS with tools to combat tax abuse and also work to deter tax shelter activity.

We need to do all we can to ensure tax compliance by corporations and individuals alike to maintain the fairness and integrity of our tax system. To that end, I look forward to hearing from the Honorable Mark Everson, Commissioner of the Internal Revenue Service, and the Honorable David Walker, Comptroller General at the Government Accountability Office, about the current state of play in corporate tax compliance and what is known about the corporate tax gap. Tied in to corporate profits is the taxation of appreciated investments in corporations. In May of 2005, Senator Baucus and I requested the GAO to conduct a study on the capital gains tax gap. Today, Mr. Walker will also discuss the GAO's findings from that study and its recommendations as to how we can close the capital gains tax gap.

The Department of Justice plays a key role in enforcing the tax laws. Eileen O'Connor, Assistant Attorney General in the Tax Division of the Department of Justice will fill us in on the current issues in corporate tax from the Tax Division's perspective. She will also discuss some related matters, including the civil and criminal laws at issue with stock options being backdated for the benefit of

executives.

As promised earlier this year, we will examine the tax policy behind the LIFO method of inventory accounting with the help of Dr. George Plesko, Associate Professor of Accounting at the University of Connecticut School of Business. Dr. Plesko's scholarship in the area of bridging the reporting gap for the many differences between financial accounting standards and the tax code supports recent changes in the IRS form schedule M-3. The IRS recently came out with the new schedule M-3, which will provide IRS examiners much more detail regarding these differences.

One of our panelists, Mr. Edward Kleinbard, a New York partner at the law firm of Cleary, Gottlieb, Steen & Hamilton, has recommended public disclosure of the M-3 to promote transparency in financial reporting. Confidentiality of tax return information is a fundamental part of our self-assessment tax system. It's important to balance taxpayers' interest in privacy with the need for tax law compliance. Commissioner Everson has publicly stated that corporate tax return disclosure is something that merits serious debate. This hearing will provide a forum for having that debate.

In addition to tax compliance and enforcement matters, we will also hear testimony on the basic aspects of our current corporate system – the tax rate and the tax base – that we should consider revisiting in the context of business tax reform. In the global economy, tax policy is not so neatly put into domestic and international categories. Our corporate tax rate is typically thought of as domestic tax policy. But when it ranks at or near the top among OECD countries, it influences international business decisions, like where to build a plant, and gives companies incentives to shift income offshore. As this committee turns to tax reform, a key objective should be to make the system one that is fair and allows businesses to make decisions based more on economic merit and less on distortions generated by the tax code. The recent global trend has been to lower the corporate tax rate and broaden the base. This is no longer an abstract idea. Our last panelist, Dr. Martin Sullivan, economist and contributing editor at Tax Analysts, will discuss this new era in corporate taxation that has arrived in many countries across Europe.

Closing Statement of Chairman Grassley

I just wanted to make a few brief closing comments. I appreciate all the witnesses' time here today. I think this has been very informative for the committee. We have learned about problems with today's tax system and have heard valuable suggestions for ways to improve the current tax code. Some of these may need further thinking but some we should act on sooner rather than later. Beyond trying to improve today's code, the discussion about issues such as tax expenditures and fundamental problems with the tax system point the way for thinking about tomorrow's tax code. The comments we have heard calling for lowering the rates, broadening the base, and simplifying the tax code are good goals that should guide our work as we consider corporate tax reform.

Achieving these goals of tax reform will not only make the code fairer and more efficient, but it will also provide fiscal benefits to the budget. But of perhaps greatest importance, we've heard today that a system of lower rates, broader base and simplification will increase our nation's competitiveness in attracting capital for new and better jobs. We have to recognize that we live in a global economy that requires us to be competitive in securing capital investment if we want to improve the standard of living for our children and grandchildren. This hearing has been a good beginning for exploring further the issues of tax reform. It is my hope to have a hearing on tax reform and simplification focusing on individuals later this summer and to explore in more detail corporate tax reform this fall.

