History of Tax
A HISTORY OF US TAXES - 10 KEY DATES
27 October 2020 - Slido Questions

Answers to questions for which there was no time on the day:

In the UK currently, there is a transition to the digitalisation tax filing, resulting in business owners no longer able to submit Sales Tax data directly to HMRC, but now only through 3rd party software. Is that likely to happen also in the US?

Since the mid-2000's, the IRS has required corporations with assets of $10 million dollars or more and at least 250 returns (which includes information returns for their employees and shareholders) filing a Form 1120 (the corporate tax return) to file their returns electronically. A corporation, including a non-US corporation filing a Form1120-F (the corporate tax return for non-US filers), can either use an IRS E-file approved third party preparer to do it or it can do it directly itself so long as it has the software it plans to use is pre-approved by the IRS. Individuals can also file their returns electronically through IRS E-file approved third party preparers but they also have the option of filing paper returns as well.

Much of the changes to taxation you've discussed have been driven by global conflicts (Civil war, WW1, WW2), and the same is true in the UK. What changes do you anticipate for the future, particularly in the light of Covid-19?

It is unlikely that Covid-19 or even any future military conflict would have the same impact on our federal tax system as did the conflicts you mention in your question. For example, the Vietnam, Kuwait, Afghanistan, and Iraq conflicts did not result in any significant changes to the tax system. In particular, while during the Vietnam War there was a 10% surtax on individuals for at least on year, there were no major structural changes or dramatic increases in tax rates as happened during the earlier conflicts. Probably one reason for this difference was that because (1) after WW II the tax rates remained very high until the 1980's and (2) the US was running budget deficits for most of that time, the military was able to maintain its forces at what it believed was an appropriate level without large increases in federal taxes. And since 1981 with respect to the defense budget, the Congress and the President have been able to increase it (during the 1980s) then decrease it (during the 1990s) than increase it again (after 9/11) then decrease it again (during Barack Obama's presidency) and finally increase it again (during the Trump Administration) without resorting to tax increases (for example, most of the funding for the war in Kuwait in the early 1990s came from other countries).

Could you please explain the relationship between the federal budget and the calculation of tax rates. Are tax rates determined in light of the federal budget or regardless of it?

The tax rates are set by specific tax legislation rather than as part of the annual budget process. Thus, in 2001, the rates were reduced by a 2001 tax bill and those rates remained in place for 10 years, after which they were supposed to revert back to the rates in place before the 2001 legislation was enacted (in fact, in 2010, Congress acted to make most of the rates "permanent" (permanent in the sense that they would remain in place unless changed by a future Congress and President)). Then in 2017, under a President Trump and the. Republican controlled Congress, they were reduced again. During this time, the budget process worked on a different although somewhat related track than the process for tax legislation. In fact, in general over the past two decades, the details of the spending side of the budgeting process depended heavily on how much revenue is estimated to be raised by the tax rates in effect at the time rather than the tax rates being changed to raise the money needed to fund the spending priorities in the budget. However, if Joe Biden is elected President, that process would have to in essence be reversed to initially take into account his proposed substantial increases in federal spending ($4 trillion over a 10 year period). This means that basically the Congress will have to decide first as part of the overall process exactly how much it needs to raise taxes in order to able to pay for his proposed new spending (Biden's proposals contain over $2 trillion in tax increases—not including additional proposed increases in the payroll taxes which are used to fund Social Security and Medicare—with the $2 trillion shortfall presumably coming from either reducing other spending (a likely candidate would be defense spending) or issuing more government debt which would further substantially increase the federal budget deficit).

Could you please explain the relationship between the federal budget and the calculation of tax rates. Are tax rates determined in light of the federal budget or regardless of it?

Actually, the US Supreme Court hears very few tax cases. In fact, the 1895 case I mentioned during my talk was quite unique in that it dealt with a constitutional issue rather than the more common tax issues which reach the Supreme Court such as issues involving (1) statutory construction of the tax code, (2) whether a particular fact situation should be recharacterized to reflect the economic substance of the transaction rather than the legal form of the transaction, and (2) administrative issues concerning the statute of limitations or the collection of the tax. But every once in a while, there are still constitutional issues involving the extent of the taxing power of of the federal government under the US Constitution which reach the Supreme Court. For example, there was a rather recent case involving whether the so-called "mandate to buy health insurance" in Obamacare, which was included in the law to force every US citizen to purchase health insurance even if they did not need it, where the Supreme Court was asked to decide if the mandate was a "tax," which would be constitutionally permissible under the broad taxing powers of the US Constitution, or instead was an impermissible restraint on the individual liberties of US citizens. Notwithstanding Obama's public statements at the time the law was enacted that it was not a tax, the Supreme Court decided otherwise in an effort to save Obamacare from being overturned. So, yes in the view of many Americans who believed that Obamacare was an unconstitutional law, the Supreme Court is too powerful as evidenced by its use of the taxing power to uphold a healthcare law.

13: If Biden is elected President and the Democrats control both House of Congress, sometime in the next four years it is possible that the Congress will pass and he will sign a major tax bill that will move US tax policy in a fundamentally different direction: huge tax increases—perhaps the highest since WW II; huge increases in estate taxes—including eliminating a provision that has been in the tax law for almost a hundred years which allows beneficiaries who receive appreciated assets as part of a distribution of assets from an estate to sell those assets without paying a capital gains tax on the appreciation in value during the lifetime of the decedent; elimination of capital gains taxes— which would mean a doubling of income tax on the sale of investment and other capital assets; large new minimum taxes on worldwide income of US multinational corporations plus a penalty on such corporations who produce products overseas that are then sold in the US; and possibly, a wealth tax which, although it would be initially focused mainly on wealthy people, would probably over time be imposed on other less wealthy Americans as well. If any of this happens, that will certainly be a new Key Date in US Tax History.

You describe a state sales tax of up to 10% as "very high" and a reason why a federal sales or value-added tax could not be imposed on top, but European VAT rates are already often 20%+, so why could US individuals not also pay a similar combined rate?

The problem is that the states would still need to bring in the revenue now generated by their sales taxes even if the federal government were to enact a VAT. Thus, on a particular product, there would not only be an embedded VAT in the price but there would also be a sales on top of it. The example I suggested in response to a question during my talk was to have a federal VAT replace the income tax for individuals below a certain adjusted gross income (AGI) so that for those individuals, they would only "pay" the VAT to the federal government while for individuals above that threshold, they would "pay" both the VAT and the income tax on their AGI above the threshold. In the late 1990s when I worked on this idea as part of a group advising one of the presidential candidates on ideas for tax reform, our charge was to make any change we suggested "revenue neutral" meaning that the US would raise the same amount of revenues after the change as it did before. What we discovered during our work on the idea was that in order to make the VAT idea revenue neutral, the AGI threshold would have to be $80,000–-which seemed low to us—and the VAT tax rate would have to be 25%—which seemed high, particularly when you add each state's sales tax on top. So, for example, in a state with a 10% sales tax rate, the combined total tax on the purchase would be in the neighborhood of 35%, basically meaning that the cost of every product subject to the VAT would increase by about a third, and as I suggested, even though the taxpayers below the threshold would end up paying no federal income tax at all (meaning importantly no more withholding on their wages by their employers), a trade off of higher take home pay spread over a 52 week period versus paying a third more for a new automobile or refrigerator at the time of purchase would not be particularly appealing.