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A TAX AGENDA FOR SMALL BUSINESS

JOINT ROUNDTABLE
BEFORE THE
COMMITTEE ON SMALL BUSINESS
UNITED STATES SENATE
AND THE
COMMITTEE ON SMALL BUSINESS
HOUSE OF REPRESENTATIVES
ONE HUNDRED SEVENTH CONGRESS
FIRST SESSION

APRIL 4, 2001

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* Comments (if any) at various points between pages 16–46.

SMALL BUSINESS JOINT ROUNDTABLE: A TAX AGENDA FOR SMALL BUSINESS

WEDNESDAY, APRIL 4, 2001

UNITED STATES SENATE,
COMMITTEE ON SMALL BUSINESS,
Washington, D.C.

The Committees met, pursuant to notice, at 9:32 a.m., in Room SR-428, Russell Senate Office Building, the Honorable Christopher S. Bond, Chairman of the Committee, presiding.

Members present: Senators Bond, Burns, Bennett, and Kerry; Representatives Manzullo, Grucci, Pence, Velázquez, Pascrell, Acevedo-Vilá, Christian-Christensen, and Napolitano.

OPENING STATEMENT OF THE HONORABLE CHRISTOPHER S. BOND, CHAIRMAN, SENATE COMMITTEE ON SMALL BUSI- NESS, AND A UNITED STATES SENATOR FROM THE STATE OF MISSOURI

Chairman BOND. Good morning, and welcome to the first joint roundtable of the House and Senate Committees on Small Business in the 107th Congress. It is a very special pleasure for me to welcome the Chairman of the House Committee, Don Manzullo, as well as Congresswoman Velázquez, and their colleagues from the House.

One of the reasons why we have these sessions is to listen to the voices of small business. When I had the pleasure of assuming the chairmanship of this Committee in 1995, my then-ranking member, Dale Bumpers and I agreed we were going to use the Small Business Committee as the eyes and ears for small business. We have learned a lot just by listening. I think there is a line in there from some great philosopher, like Casey Stengel, that it is amazing how much you can hear if you listen.

We have also tried to be an effective voice for small business, and a lot of times we have found that other committees regard us as officious intermeddlers because we know that there are a lot of issues that are not specifically within the jurisdiction of the Small Business Committees, that are, in fact, the most important things that can happen to small business. By mobilizing a strong bipartisan coalition on both the House and the Senate sides, we have been able to enact into law things that I think are making life a little better for small business.

Today, we have a great cross-section of the small business community represented. I understand that my Ranking Member, Senator Kerry, has another hearing and is going to be coming by later on, and we hope that other members from both the Senate and the

House side will be joining us. The purpose of these roundtables is to provide a record for us, for our staffs, and a basis for further action and activities during the coming session.

This topic today, of course, is a red-hot one. It is taxes. We happen to be having some action on the floor in the Senate today on the budget. I am a member of the Budget Committee and I am supposed to be there, as well, so you are going to have to forgive me if I bail out, because I have some responsibilities there. But, what you tell us here today will be helpful, both in the Budget Committee discussions, on the floor, and in the work that we will do on the tax bill, which I am confident will be coming up in the Senate in the very near future.

With 12 days and counting until the dreaded tax filing date, taxes are on the minds of the men and women who worked tirelessly to run small, successful enterprises, not only because of the high tax bills, but because of the enormous amount of time and energy it takes just to complete all of the tax forms required. For the past several months, the focus of the debate has been on President Bush's proposal, which I personally believe holds great promise for small business, especially in terms of rate reduction.

According to the IRS, nearly 90 percent of small business with gross receipts of less than \$1 million are organized as pass-through entities, sole proprietorships, partnerships and S-corporations, which means that they are taxed at the individual rates, and the individual rate decisions will affect those businesses. If we reduce rates, more money will be left to meet payroll, reduce credit card balances, or invest in new equipment and new technology, which makes the businesses more productive.

The President's proposal for eliminating the death tax can also help small enterprises. One of the things we hear, not only from small businesses, but from farmers in communities throughout my state, is that they are unable to pass along a business or a farm or a ranch to the next generation. They want to keep it in the family, but when the government comes in with a 55 percent bite, it takes away too much of their dollars. They cannot continue and still pay the taxes.

Beyond the President's tax cut, there is still more work to be done for small business tax relief. For my part, I have introduced a Small Business Works Act, which has additional relief in terms of cash accounting, expensing deductions, and lowering the AMT. I understand Chairman Manzullo has introduced a similar bill on the House side.

We still need to hear from you. To start our discussion, we have asked each of you to list your top two or three priorities in the areas of tax relief, tax simplification, and taxpayer rights. We found that tax relief recommendations were among the top items that you have told us are important. I look forward to your comments on these priorities to begin the roundtable. We will hear from the leaders of the House Committee, then we will open the discussion.]

When you want to speak, if you would just put your nameplate up on end, we will call on you, and we would ask you to limit your comments to 2-3 minutes, to keep plenty of time for everybody. We'll ask the Hearing Clerk to turn on the light, signifying the

speaker has one minute left, and we ask that you collect your thoughts, provide as much information as you can. We will, however, keep the record open, and you may feel free to supplement it thereafter. With that, let me turn to Chairman Manzullo.

[The prepared statement of Chairman Bond follows:]

SENATOR CHRISTOPHER S. (Kit) BOND, Chairman
Senate Committee on Small Business
Roundtable: "A Tax Agenda for Small Business"
Opening Statement
April 4, 2001

Good morning. Thank you all for joining us for this first *joint* roundtable of the Senate and House Committees on Small Business in the 107th Congress. It is a special pleasure for me to welcome the new Chairman of the House Committee on Small Business, Don Manzullo, as well as Congresswoman Velazquez, and their colleagues from the House of Representatives. I am also delighted to see such a broad cross section of the small business community represented here this morning.

Today, we are going to focus on topic of on-going concern to small business owners across the nation – taxes! With 12 days and counting until the dreaded tax-filing due date, this issue is on the mind of the men and women who work tirelessly to run successful small enterprises, not only because of their high tax bills but also because of the enormous amount of time and energy it takes just to complete all of the tax forms required.

For the past several months, the focus of the tax debate has been on President Bush's tax cut proposal, which I believe holds great promise for small businesses, especially in terms of rate reductions. According to the IRS, nearly 90% of small businesses with gross receipts of less than \$1 million are organized as pass-through entities – sole proprietorships, partnerships, and S corporations. As a result, these businesses will directly benefit from any cut in the current individual income-tax rates. That means more money left to meet payroll, reduce credit-card balances, or invest in new equipment.

The President's proposal for eliminating the "death tax" will also help small enterprises. Too often we hear of a small business that closed down because of the estate tax. But for most small firms the death tax means thousands of dollars spent on estate planning, lawyers, and life insurance. Just think of the new jobs that small firms could produce without these unproductive expenditures.

While the Bush tax plan is a solid first step, there is much more that can be done to ease the tax burden and tax complexity faced by small businesses. I expect that later in this Congress we'll have additional opportunities to focus specifically on America's entrepreneurs. For my part, I have introduced the Small Business Works Act to complement the Bush tax plan and get that small business debate moving -- and I thank Chairman Manzullo for introducing similar legislation in the House. These bills are based on the comments that we have received from many of you and your members over the past many months.

But we still need your help. What else can the Congress do to reduce taxes for small businesses? How can we simplify the countless pages of tax law, regulations, forms, instructions and other paperwork that small businesses face, often on a daily basis? What steps need to be taken to improve taxpayer rights and protect small business owners in their dealings with the IRS? This morning we will be asking you to offer your suggestions in these areas with the goal of setting priorities for us to address during the 107th Congress.

To start the discussion rolling, we asked each of you to list your top two priorities in each of three areas: tax relief, tax simplification, and taxpayer rights. We have compiled the responses, and each of you should have a copy of the

results. Not surprisingly, the top tax relief recommendations concerns the estate or “death” tax and the alternative-minimum tax, the top tax simplification proposals were clarification of the cash accounting rules and simplification of the depreciation rules, and the top taxpayer protection priorities were improving IRS customer service and adopting the SBREFA review panel amendments that the Senate Small Business Committee approved unanimously in the last Congress.

As we move forward this morning, I look forward to your comments on these priorities. In order to keep the discussion organized, we will focus on the three areas individually, understanding that some proposals fall into more than one category. For instance, increased equipment expensing may be viewed by some as “tax relief,” while others will view it as “tax simplification.” What’s important is that we get the ideas on the table and focus on what actions the small business community can take to help us push as many of these ideas as possible through to the President’s desk.

To begin the roundtable, we will first hear from Chairman Manzullo, Senator Kerry, and Congresswoman Velazquez. Then we’ll open the discussion to everyone. When you want to speak on a topic, please place your nameplate on its end. Given the number of participants this morning and the variety of proposals, we ask that you keep your comments to 2 to 3 minutes. We know from experience that this allows the discussion to proceed in a more orderly manner and lets us come back to a participant for follow-up comments in many cases. If comments begin to run long, we’ll ask our Hearings Clerk to turn on the lights signifying that the speaker has one minute to wrap up. During the roundtable, I expect that other

members of both Committees may stop by to listen and possibly ask a question or two. So, we may need to suspend the discussion to hear from them as well.

In closing, let me say that your participation in today's roundtable is extremely important. The roundtable structure allows us to hear from many more individuals and organizations than a traditional hearing, and we appreciate your interest and participation. Your comments will be given serious consideration, and the record will be held open for two weeks for any additional statements or information that you would like to submit to the Committees.

With that, let's turn to Chairman Manzullo for his opening remarks.

Transitions

Tax Relief Segment

Thank you Congresswoman Velazquez. Again, it's a pleasure to have you and the House Committee on Small Business joining us today. Now, let's turn to our participants and get down to business. Our first topic for discussion is tax relief priorities for small business. As I mentioned, the number 1 recommendation concerns the estate or "death" tax, but I know there are a number of other pressing issues in this area for the small business community. Who would like to open the discussion?

Tax Simplification Segment

Thank you. We have about exhausted the time set aside for tax relief priorities. Let's turn our attention to an area of great concern in recent years – tax simplification. Based on your initial feedback, the clarification of the cash and accrual accounting rules appears to be the leading priority, but I know there are others. Who would like to begin this segment?

Taxpayer Rights and Protections Segment

Thank you. We need to wrap up this discussion on tax simplification and save a few minutes to talk about proposals for improving taxpayer rights and protections. While Congress made some important changes in the 1998 IRS Restructuring and Reform Act, we continue to hear that other improvements are still needed. For some, modifying the SBREFA rules to cover the IRS is one such improvement. Who would like to start in this, our last, issue area this morning?

OPENING STATEMENT OF THE HONORABLE DONALD A. MANZULLO, CHAIRMAN, HOUSE COMMITTEE ON SMALL BUSINESS, AND A REPRESENTATIVE IN CONGRESS FROM ILLINOIS

Chairman MANZULLO. Thank you very much, Senator. It is a real pleasure to be here. This should be a very interesting—I do not want to call it panel; I do not want to call it roundtable, but representatives from various small business industries. Congresswoman Velázquez and I have introduced the Small Employer Tax Relief Act of 2001. I think it is the most far-reaching, bipartisan tax bill that has been introduced in the Congress, and we worked and worked and worked on this to make sure that it is bipartisan.

She and her staff have done an absolutely fantastic job, along with our staff, on getting this bill together. This bill provides for immediate relief for accelerating the health insurance deduction for the self-employed to 100 percent, increasing expensing to \$50,000, repealing individual AMT; increasing the meal deduction 80 percent; allowing small businesses to use the cash method of accounting without limitation; simplified depreciation and higher education reporting rules; providing tax credits for small business investments for new, environmentally friendly technologies and for training highly-skilled workers; and eliminating capital gains and depreciation recapture penalties on home offices.

We introduced this bill to complement, not to compete with, the President's proposals and other proposals out there involving the marginal rates. So we are really looking forward to your testimony, and I would yield to my counterpart, Congresswoman Velázquez.

[The prepared statement of Chairman Manzullo follows:]

OPENING STATEMENT
OF
CHAIRMAN DON MANZULLO
COMMITTEE ON SMALL BUSINESS
U.S. HOUSE OF REPRESENTATIVES

Joint Roundtable Entitled "A Tax Agenda for Small Business"

April 4, 2001

In opening today's Joint Roundtable of the Senate and House Small Business Committees, I wish to thank Chairman Kit Bond and each of the participants here today for their leadership and dedication in representing millions of small business owners, farmers, families, and self-employed taxpayers. While the hard-working entrepreneurs we represent are the number one employers in America, they face high taxes and a highly complex tax code. They need substantial, fair and simple tax relief. Accordingly, this Roundtable will facilitate broad-based discussion of a tax agenda for small business.

As part of this agenda, I recently introduced a bipartisan tax bill, the "Small Employer Tax Relief Act of 2001" (H.R. 1037). I thank my colleague, Ms. Velazquez, for her support of this meaningful legislation. A companion to Chairman Bond's bill (S. 189), SETRA 2001 provides powerful tax relief for small business. Immediate relief includes accelerating the health insurance deduction for the self-employed to 100 percent; increasing expensing to \$50,000; repealing the individual AMT; increasing the meal deduction to 80 percent; allowing small businesses to use the cash method of accounting without limitation; simplifying complex depreciation and higher education reporting rules; providing tax credits for small business investments in new, environmentally-friendly

technologies and for training highly skilled workers; and eliminating the capital gains and depreciation recapture penalties on home offices.

Importantly, I introduced SETRA 2001 to complement, not to compete with, President Bush's proposals to cut marginal tax rates and to eliminate the death tax.

Cutting marginal tax rates will empower small business taxpayers – 85 percent of whom pay individual taxes – to continue to spur economic growth and to avert the looming economic downturn.

In addition, the death tax is draining our economy. A destructive and immoral tax – the death tax stifles growth, kills jobs, discourages savings, drains resources, ruins family businesses and farms, and penalizes small, middle-class entrepreneurs. With a new President and Administration who understand, I trust we will finally protect small businesses and farms and kill the death tax. The House is voting on H.R. 8 to repeal the death tax today, so I may have to come and go for this crucial small business vote.

I am looking forward to the comments of our participants, and to working with each of you to make your small business tax agenda law. Thank you again, Chairman Bond, I am very pleased to be here this morning and will now yield back to you for any comments Senator Kerry or Ms. Velazquez may wish to make.

Chairman BOND. Congresswoman Velázquez, welcome.

OPENING STATEMENT OF THE HONORABLE NYDIA M. VELÁZQUEZ, A REPRESENTATIVE IN CONGRESS FROM NEW YORK

Ms. VELÁZQUEZ. Thank you, Senator Bond, and thank you, Chairman Manzullo. Welcome everyone. It is a great pleasure to be here with you. Everyone here understands one absolute truth about America's economic strength today. It rests squarely on the shoulders of America's small businesses. The last decade has seen record numbers of new businesses being created and interest in owning a small business has skyrocketed. That is why I have been repeating the mantra, small business is big business in America. The fact is small businesses contribute nearly one-half of this Nation's retail sales, and 50 percent of the private gross domestic product. They employ more than half of our workforce while providing over two-thirds of the new jobs created in the last decade's economic boom.

Even with this growing role in the economy, small businesses still do not receive parity when it comes to the issue of tax fairness. By providing targeted tax relief aimed at small businesses, we can offer them the incentive necessary to grow and continue to serve as the engine of the economy. We estimate paperwork costs nearly doubled for this Nation's small businesses. There is no one sector of the economy more in need of tax simplification. As tough as the tax cut is on the rest of us, to the small business owner, it is absolutely brutal.

That is why it is crucial we work together to target those portions of the IRS code that are particularly onerous to small businesses. We need to sit down and work towards transforming our tax code into a system that is fair, simple and more understandable than its current form. In doing so, we will help small businesses focus their attention to running their businesses and away from their accountants. As you know, small businesses come in all shapes and sizes. While we each view them differently, the IRS does not and will not do so. That is why the third pillar of tax relief is taxpayer protection.

By ensuring that small businesses are allowed to take corrective action when honest mistakes happen, we guarantee that entrepreneurs are not unfairly singled out. In doing so, we ensure that a single stumble does not bring the whole business tumbling down. To help small business in facing these challenges, I recently joined Chairman Manzullo in introducing the Small Employers Tax Relief Act. In this bipartisan legislation we provide critical tax relief, simplification and taxpayer protection for small business owners. I felt it was important to introduce this legislation after a view of the President's budget, a proposal that contained no specific tax relief for small businesses. Indeed, this lack of relief is in direct contrast to the President's claim, during the State of the Union, that help for small business means jobs for Americans. Some, including myself and most of my Democratic colleagues, believe that the new fees on SBA loan programs and technical assistance programs are actually a tax increase on small businesses. As the Ranking Democratic Member of the House Small Business Committee, I believe we are fulfilling one of our most important roles as we appear here

today. That role is to help our colleagues on both sides of Congress, and more importantly on both sides of the aisle, understand the unique needs of America's small business community, particularly in the area of tax relief.

While today's roundtable is an important first step, I do not believe this can nor should it replace a hearing. It is my hope that the Committee will begin to hold a comprehensive and formal hearing on tax relief in a forum that will give the issues the due diligence it should be given. In closing, these are without a doubt some of the most important and interesting times we have ever faced in America. We have an economy that clearly has more questions than answers, and we are desperately in need of a serious economic stimulus. I believe that if small businesses are to continue to thrive and push the economy forward, we must not fail to provide them with the same level playing field when it comes to tax relief. To do anything less will be to compromise this Nation's future economic prosperity.

Thank you, Mr. Chairman.

[The Statement of Representative Velázquez follows:]

Congress of the United States
House of Representatives
 107th Congress
Committee on Small Business
 2501 Rayburn House Office Building
 Washington, DC 20515-0515

Congresswoman Nydia M. Velázquez
 Ranking Democratic Member
 Statement Joint House and Senate Tax Roundtable
 April 4, 2001

Everyone here understands one absolute truth about America's economic strength today - - it rests squarely on the shoulders of America's small businesses. The last decade has seen record numbers of new businesses being created and interest in owning a small business has skyrocketed. That is why I have been repeating the mantra - - small business is, and always will be, big business in America. The fact is, small businesses contribute nearly one-half of this nation's retail sales and 50 percent of the private gross domestic product. They employ more than half of our workforce while providing over two-thirds of the new jobs created in the last decade's economic boom. Even with this growing role in the economy, small businesses still do not receive parity when it comes to the issue of tax fairness.

By providing targeted tax relief aimed at small business, we can offer them the incentives necessary to grow and continue to serve as the engine of the economy. With estimated paperwork cost nearly double for this nation's small businesses, there is no one sector of the economy more in need of tax simplification. And as tough as the tax code is on the rest of us - - to the small business owner it is absolutely brutal. That is why it is crucial we work together to target those portions of the IRS code - - that are particularly onerous to small businesses. We need to sit down and work towards transforming our tax code into a system that is fair, simple and more understandable than its current form. In doing so, we will help small businesses focus their attention towards running their businesses - - and away from their accountants.

As you know, small businesses come in all shapes and sizes. While we each view them differently, the IRS does not and will not do so. This is why, the 3rd pillar of tax relief is taxpayer protections. By ensuring that small businesses are allowed to take corrective action when honest mistakes happen, we guarantee that entrepreneurs are not unfairly singled out. In doing so, we ensure that a single stumble does not bring the whole business tumbling down.

To help us assist small business in facing these challenges, I recently joined with Chairman Manzullo in introducing the Small Employers Tax Relief Act. In this bipartisan legislation, we provide critical tax relief, simplification and taxpayer protection for small business owners. I felt it was important to introduce this legislation after a review of the President's budget - - a proposal that contained no specific tax relief for small businesses. Indeed, this lack of relief is in direct contrast to the President's claim during his State of the Union that "help for small business means jobs for Americans." Some, including myself and most of my Democratic colleagues, believe that the new fees on SBA loan programs and technical assistance programs are actually a tax increase on small businesses.

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While today's roundtable is an important first step, I do not believe this can - - - nor should it - - - replace a hearing. It is my hope that the Committee will begin to hold a comprehensive and formal hearing on tax relief in a forum that will give the issues the due diligence it should be given.

This hearing would allow us to deliberate fully on this issue - - - and move prudently, rather than hastily, through the legislative process. In closing, these are, without a doubt, some of the most interesting times we have ever faced in America. We have an economy that clearly has more questions than answers - - - and we are desperately in need of a serious economic stimulus. I believe that if small businesses are to continue to thrive and push the economy forward, we must not fail to provide them with the same level playing field when it comes to tax relief.

To do anything less would be to compromise this nation's future economic security.

Thank you.

Chairman BOND. Thank you very much, Congresswoman Velázquez. It is a pleasure to have you and Chairman Manzullo here from the House side, and we look forward to having you participate with us.

For all present today, this roundtable is formally recorded. We found these roundtables give more people an opportunity to make their case. So, in terms of due diligence, the record will be kept open, including your statements here today, and we expect that this will be a very productive and interesting session.

As a result of the information you provided us prior to the meeting, I see that, in terms of numbers of participants recommending estate tax repeal, it is recommended by 17 as the most important; repealing/reforming the Alternative Minimum Tax is cited by 13; tax-rate reduction, by 8; 100-percent deductibility of health care by 7. That's just to give you a flavor of the scorecard.

With that, let's turn now to comments from the participants, and I would invite you to state your association and identify yourself when you wish to speak. I see our old friend, John Satagaj, was the first one. He has been here before. He knows the game.

Mr. SATAGAJ. I have learned these rules already, Mr. Chairman.

Chairman BOND. He knows the game.

Mr. SATAGAJ. My name is John Satagaj with the Small Business Legislative Council. The first and most important piece of business is for us to recognize that we have one fantastic team of advocates up here, and I think they deserve a round of applause. [Applause.]

Chairman BOND. Thank you, John. We will note that and you may even get called on again.

Mr. SATAGAJ. See, if you are going to get recognized, you have got to know why. Maybe I can set the precedent for brevity here, because all of us are all going to want to talk, so let me hit the first two points as quickly and simply as possible. Number one, there is talk already in the United States Senate about a minimum wage increase, and they're talking about how we are going to offset it with some tax relief. I can think of no better blueprint for small business tax relief than the bills Chairmen Bond and Manzullo have introduced. That, we all should be working for. If there is going to be a minimum wage increase, and I know some do not want it at all, that is what we need.

Item two, and you all know that I am not afraid to speak my mind, today in the House the Democrats are going to offer an alternative to the estate tax bill. That alternative increases the exception or credit, call it what you want, to \$2 million, going up to \$2.5 million. If that doubled to \$5 million, meaning \$10 million for a married couple, we in the small business community are going to be hard pressed to say that is not a good deal for small business. That is going in the right direction now. If it goes to five, combined 10, that is good for small business.

Thank you, Chairman Bond, Chairman Manzullo, and Ranking Minority Member Velázquez.

Chairman BOND. Thank you very much, John. Mr. Grucci has joined us. Any comments you wish to make?

Mr. GRUCCI. Well, I am not sure where we are in the discussion.

Chairman BOND. It is jump ball, and it is scramble time.

Mr. GRUCCI. One of the things I have always held to be very important is the health of small businesses, because we all know they produce the real baseline of our job growth and our economic stability. Anything we can do to help improve the business climate for small business is important. I think the elimination of the estate tax is just what the small business community needs and warrants, and I am eager to vote on that today, and I hope that we get that passed without much of a problem.

I also think that things like capital gains reductions are important to stimulate the economy and to help grow our small businesses and midsize businesses and large businesses. So those are the issues that I hope are important, as well as obviously tax relief, and workplace improvements, so with all that in mind I am eager to hear what you all have to say.

Thank you, Chairman.

Chairman BOND. Thank you.

Chairman Manzullo, we have time for brief comments, and welcome to additional House members who have joined us.

Chairman MANZULLO. They came just to hear the testimony.

Chairman BOND. Okay. Any other comments? The next one I saw with the indicator up is John Cox.

Mr. COX. Well, thank you very much. I just wanted to echo some of the things that John Satagaj said, and for those of us representing small business organizations, lobbying is primarily a function of relationships, and I would like to compliment both Small Business Committees for firming up and establishing a lot better relationships over the years. It is improving every day.

As far as the specifics, I think that the tax code is viewed by small business as the closest thing we have to an industrial policy in this country, so it should be designed to encourage the growth of small business and not to curtail it. I think that is reflected in the priority of the tax relief list that we have here. I was very encouraged to see that number eight is the Skilled Workforce Enhancement Act, H.R. 877, which has been introduced by Chairman Manzullo and Congresswoman Velázquez and about 30 other cosponsors, and it also is in Section 108 of the Small Employer Tax Relief Act of 2001. I am sorry. Excuse me. Is that the right bill? I see staff shaking their heads yes. But it is not in S. 189. We would like to have seen it there. Being limited in our resources and establishing our relationship, sometimes we tend to stress one committee or the other, or the House or the Senate. So if we could have assisted the staffs in coordinating some of these provisions, it would have been a great thing to have these two bills, in fact, as companion bills.

Maybe that can be achieved if they are both passed and we can establish these things in conference. So we think it is right on the money. Small businesses are part of this economy, and anything that can be done to help us grow is appreciated, and we will fight for it, and we appreciate you fighting for us.

Chairman BOND. Well, thank you very much, John, and we are only able to succeed to the extent that all of you and your members are willing and able to make your priorities heard to the people who serve you in Washington. Let's turn now to Paul Hense.

Mr. HENSE. Yes. I am the National Small Business United, chairman of their tax committee, 1995 White House conference on Small Business tax chair, and AICPA member, and the reason I am grouchy is I am a practicing CPA.

Chairman BOND. Our sympathies to you. You always feel much better on April 17 and much wealthier.

Mr. HENSE. It is payday here, but out there, it is a whole other thing. I do this all day, every day. This is what my life revolves around, and there are a couple of issues I would like to discuss. I learned a new term at a conference in Florida a couple of months ago, a BFO, a blinding flash of the obvious. I see so many things here that to me are a BFO, because it is what I do. One of them, the deductibility of health care, while full deductibility of health care is being phased in, it is not deductible against self-employment tax. That is crushing for a new business, for somebody just starting out, particularly if you have a family. You have got to have health insurance, and a little bit of it is deductible against income tax. But none of it is deductible against self-employment tax. That is a killer. So it makes it tough getting in to a health plan.

I tried to figure out what the problem is with small business. Why is the family of the small business owner somehow viewed differently than a UAW member, a government employee, almost anybody else? Why cannot we deduct our health care? Why can't our pension plans be deductible before Social Security, before self-employment tax, like other people? It does not make any sense to me. I have a young woman who works for me. She would like to be an owner, until I explain to her that she loses deductibility of her health care; she loses her fringe benefits. She has a child with cancer, so basically this woman cannot be an owner because of what she loses to become an owner. You are supposed to gain becoming an owner. She actually takes a substantial cut because of the deduction she loses.

People talk about the problems with the income tax. I have carried this around for years. This is the complete and total income tax and all the instructions and explanations for 1926. What has Congress wrought? I mean, you know, how did we get from there to here? I did some rough numbers. What is it worth to have a job as opposed to being self-employed? Figuring \$6,000 a year for health-care tax free, \$10,000 a year for pension tax free for 30 years—that is \$480,000—no Social Security taxes on that, that is \$72,000. So a job over 30 years is worth about \$552,000. So, in closing, when I went to my class reunion last summer, it was not the self-employed people who were retired and had a house in Florida and a house in northern Michigan. They were still working and will be until they are 65 or 70 or 75. It is not just a disadvantage to being self-employed. In some cases, it is crushing. It keeps some people out of business, and it definitely diminishes the life of the people who do own a business. It is not fair and it is not right.

Thank you.

Chairman BOND. You feel strongly about that, I gather, Paul.

Mr. HENSE. Well, I am tired, and I am grouchy.

Chairman BOND. I have been fighting a battle since 1995, and still have to wait until 2003 for deductibility against just the income tax. A lot of small business say we cannot wait until 2003 to

get sick. So thank you very much for your comments. We are going to turn in just a moment to the members here to see if they have any further questions.

Senator BURNS. Paul, I kept getting fired all the time, so I had to go into business for myself.

Mr. HENSE. Well, then, you and I understand each other, and you just heard why.

Mr. BOND. Ben Cooper is next. Let me ask him for his comments.

Mr. COOPER. Thank you, Mr. Chairman, and I join my colleagues here in expressing appreciation for your having all of us here for this important roundtable. My name is Ben Cooper. I am senior vice president for the Printing Industries of America.

I want to relate a statistic to you. We have always been proud of the size of the printing industry as one of the largest manufacturing industries in the United States. Since 1997, we have seen something that we are uncomfortable with, and that is a decline in the total number of printing companies in the United States. We have gone from 52,000 to 47,000. That is still a lot of printers, but what it is telling us and what we know is that people are not going into our business anymore. They are not going into manufacturing, and I believe this is true. If you look throughout the economy, you are going to find that fewer and fewer people are starting businesses, particularly in manufacturing. It is just too expensive. I look down the list of tax priorities here. We have such an array of penalties for going into business, and I support the gentlemen who just spoke. There are so many penalties for going into business and very few opportunities to succeed at it.

The planning that goes in, the amount of money you have to spend to stay in business, is extraordinary. The tax incentives to stay in business are minimal. You cannot buy new equipment under almost any of the opportunities here. I think about Section 179 expensing. Try buying a printing press for under \$200,000. It does not happen. So you buy one piece of equipment, you do not qualify for the expensing provisions. My biggest gripe: you buy a computer system that everybody knows lasts 14–24 months if you are lucky, and the government says you must carry it on your books for five years. That has not been changed. I hate to even talk about 1982 or anything. It has never been changed. We have never updated that rule. As a result, this government right now is doing everything it can to prevent success in small business.

I really do believe this meeting today may be a crossroads. We are going to have to turn this thing around or we are not going to have small business manufacturing in this country.

Thank you again.

Chairman BOND. Thank you very much, Ben. Congressman Velázquez, that is in your bill and in our bill, too; is it not?

Ms. VELÁZQUEZ. Yes. Mr. Chairman, I just would like to ask a question.

Chairman BOND. Please.

Ms. VELÁZQUEZ. Maybe to Mr. Cox, and, John, I care a lot about the printing industry, to the point that I married a printer. So I will try to do my best, you know. But considering that Congress must set priorities, when choosing to pass legislation, what are the top priorities in terms of tax relief for your organizations, either

you or any of the people here that can answer my question, and you can answer my question in light of Chairman Bond and Manzullo and Velázquez legislation, in terms of tax relief aimed at small business.

Mr. COOPER. I will be happy to answer. One priority is an indirect tax—do not pass Patients' Bill of Rights.

Chairman BOND. Do not? In other words, do no harm?

Mr. COOPER. Yes. First, do no harm. The Patients' Bill of Rights may end employer-based health care for small companies in this country if it is passed. The second thing is do some sort of relief on estate tax. It is not the people we worry about who ultimately pay the estate tax. It is the amount of money that has to be spent calculating whether or not you are going to have to pay it. Another very subtle thing, please do something about the AMT. Success is punished by the AMT. If you do really well, you are going to do really poorly when the AMT is applied. For us, those are the three main things. I could go on all day, but I will not.

Chairman BOND. You can submit that for the record. Seriously, we have a lot of people. Let me move onto Steve Anderson.

Mr. ANDERSON. Thank you, Mr. Chairman. My name is Steve Anderson. I am president and chief executive officer of the National Restaurant Association, and I appreciate Paul's comments. I think it was your high school reunion, and I had heard stories about 30-year-old people retiring in this country, little did I know that they were actually doing it.

The National Restaurant Association last year implemented a program called the Cornerstone Initiative, which recognizes that America's restaurants are the cornerstone of America. But if you look at the people represented around this room, small business really is the cornerstone of America.

Restaurants are indeed a cornerstone of America. There are 844,000 restaurant locations in this country employing 11.3 million people. We are the largest private sector employer of the country. This year we will do \$400 billion in annual sales and we have a \$1.2 trillion impact on the total economy. So, we are surely the cornerstone of the Nation's economy.

We are the cornerstone of a rewarding career path. We are trying to encourage people to go into the restaurant industry and tell successful stories about how they can achieve success with not a lot of education. But with an entrepreneurial spirit and hard work, they can truly be successful in this country. I will come back to some of these issues that we are talking about and the impact there. And we are the cornerstone of the local economy and community involvement. Nine out of ten restaurants are involved in some type of philanthropic work. If you can loosen up some of the controls, the taxes, and the mandates that come out of Washington, there is so much that small business can offer to America to do good works within our local communities.

To Congresswoman Velázquez's question and to the many issues that we are exploring, I will highlight our priorities. On the tax relief priorities, the business meal deductibility and permanent extension of the work opportunity tax credit are very important to us. On the tax simplification priorities, we are throwing in that category repeal of the estate tax, full repeal, which is the top priority

of the National Restaurant Association. Additionally, the cut in marginal tax rates and banning employer tip audits and aggregate assessments are very important in the areas of taxpayer rights.

As I mentioned, business meal deductibility is very important to our members. To put a human face to this issue, I have a brother-in-law, and I am probably one of few people in the room that actually likes my inlaws, who is a manufacturer representative for a furniture company out of New Orleans. His territory goes from Louisiana to Florida. Basically what he does is travel in his red pick-up truck, that some of us in the family call the bubba truck, and call on small business people who own furniture stores. For these sales calls his conference rooms are America's restaurants. That is very important, and I think he embodies the essence of why increasing the deductibility of business meals is so critical.

Another important issue is the work opportunity tax credit. The National Restaurant Association has been actively involved in that issue as you well know. Three out of four quick service restaurants have hired employees who are former welfare recipients. One in four restaurants nationwide use the work opportunity tax credit to lure disadvantaged individuals to work for them. Individuals who are eligible for the work opportunity tax credit, when given time and training and the education they need, stay on the job longer than anyone else. Thank you, Mr. Chairman.

Chairman BOND. Thank you very much, Steve. With some fear and trepidation and with hope that he is in a little better mood than his neighbor, I now call on Ed Karl with the AICPA. Is this tax season getting you down, too, sir?

Mr. KARL. I represent the American Institute of CPAs, of which Mr. Hense is a member, and actually the first item I my want to mention has to do with fiscal years. Almost all small businesses must adopt a calendar year for reporting purposes, and what we would like Congress to do is provide some flexibility for small businesses by having a small business exception to allow them to use any fiscal year.

We believe this would allow small businesses to focus on running the business, rather than worrying about filings and financial statements. Let me give one quick example: if you had a fuel-oil distributor in Boston who, right now, is likely to be required to be on a December 31 year end, that is not the time of year when the business wants to have to count their inventory, which is at its highest level.

That distributor does not need to focus on business issues of reporting when he is so busy with the business. The distributor would rather do that at a time of year when he is a lot less busy. We would like to see some kind of an exception for small business to have the flexibility to choose any fiscal year.

The other thing I wanted to mention is a reasonable-compensation standard for calculating tax on self-employment income. For partnerships and entities treated as partnerships, there is a bit of confusion about when you rightfully pay tax on your self-employment income versus calculating a return on your investment in the business, which should not be subject to that tax. We would like to propose a legislative safe harbor that would bring some certainty in that area and reduce potential conflict with IRS. Thank you.

Chairman BOND. Thank you very much, Mr. Karl. Let me stop here a minute. We have been joined by more members. You have already heard from my Chairman-in-waiting, warming up in the bullpen, Conrad Burns. I wonder if Senator Burns or if any of the other members who have joined us would like to make a brief comment on anything that is going on?

Senator BURNS. I have a mad-cow-disease hearing going on downstairs. So I may have to step out shortly.

Chairman BOND. Any other thoughts? Thank you and welcome.

Mrs. CHRISTIAN-CHRISTENSEN. I am Donna Christian-Christensen. I represent the Virgin Islands. I am also a physician, and I was interested in the comment about the Patients' Bill of Rights, because as a physician member, I am really committed to passing a patient Bill of Rights, with an accountability provision in it. I wonder if you would elaborate on your statement that it would prevent employers from providing insurance, because I believe that area of concern had been addressed so that the employer was not going to be, in anyway, accountable unless they made specific decisions regarding the care of the patient. If anyone else had any comments?

Mr. COOPER. I would be happy to do it as briefly as possible.

Chairman BOND. If you could give a brief response, we would invite any others who have comments on that, either pro or con, to respond directly to Congresswoman Christian-Christensen, and also to the Committees for the record. We do not have a lot of time to get into that, but Ben, do you want to expand on it?

Mr. COOPER. We are very concerned about direct employer liability. That is certainly an issue that should be addressed. However, whatever is done under the name of Patients' Bill of Rights that increases the cost of health insurance will decrease the benefits. Employers simply do not have any more money, and that is particularly true for small business. We have already had several members drop coverage under current law and the current health-care situation.

The intentions of this legislation may be good; the results are going to be bad.

Chairman BOND. Thank you very much, Ben. Any other comments from the members here?

All right. We have got a great lineup waiting. Wayne Nelson.

Mr. NELSON. Thank you, Mr. Chairman. My name is Wayne Nelson. I am president of Communicating for Agriculture and the Self-Employed. We are made up of farmers and small business people from throughout the country. Our concern would expand a little bit on what Paul has said earlier. We have long been champions, and we appreciate all the work that both chairmen and other members of the Committee have done, to provide a 100 percent deduction for the self-employed. But we also feel a great need to expand that 100 percent deduction for all individuals who pay for their own health insurance.

What is happening, as Ben has stated, and what I am afraid is going to happen in the future, is there is going to be more and more small businesses dropping their coverage. As of today, that individual who does not have a benefit plan working for a small business has a zero deduction unless he or she itemizes, and as you

all know, a very small number of people are able to itemize. So we encourage Congress to add a 100 percent health-insurance deduction for all individuals. We think that is very important keeping coverage for the people that are now insured and helping to decrease the number that are uninsured.

Additionally, with a lot of farmers as members, we have a lot of ag tax things that are important. Farm, Fisherman and Ranch Risk Management (FFARRM) accounts are very important to us, as they are to others. We think it is a great idea and one that should be passed. In addition, we think that Senator Grassley's tax package, which includes a lot of agricultural tax provisions, is also very important. Of course, your bill, Chairman Bond, and Chairman Manzullo's bill both contain a lot of tax incentives that we think are very important to small business. I appreciate the time to discuss these issues.

Chairman BOND. Thank you very much, Wayne, and let's see, number eight is Robert Anderton.

Mr. ANDERTON. Thank you, Mr. Chairman. I'm Dr. Bob Anderton. I am president of the American Dental Association. I represent 144,000 practicing dentists out there, and I am a practicing dentist myself. Dentistry, of course, is a small business, and even though we are small in numbers, I think dentists contribute a great deal to the health of this country. Over 90 percent of the oral health care in the country is delivered by practicing dentists out there, most of whom are solo practitioners. I want to echo some of the things that have previously been said regarding small business.

First, we, of course, are employers and very much interested in the 100 percent deductibility of health-care insurance. I think it is not reasonable that if you are a corporation, you can deduct health-insurance costs, but if you are a self-employed small business owner, you can only deduct 60 percent of it. So we are very much in favor of allowing the self-employed to deduct 100 percent of these costs.

Another issue I would like to raise in conjunction with the representative from the printing industry involves the difficulties that now exist for a dentist to set up a new practice. When I graduated back in the dark ages, about 95 percent of the graduating dentists went into private fee-for-service practice. Now, that is just about flip-flopped, and only about five percent are able to go into business because of the prohibitive cost and the tax disincentives that are associated with setting up a practice.

One example of a tax disincentive is Section 179 of the code, which right now will only allow a practitioner to deduct up to \$24,000 of capital expenditures. Today, it costs many, many times that amount to set up just a one-room office today, somewhere in the neighborhood of \$200,000 when a laser unit alone cost \$50,000. So we are very much in favor of expanding the expensing limits.

If I may, I would also like to make a comment on patient protection. I realize and understand the concerns that employers have on the accountability provision, but we are only in favor of holding those employers accountable for treatment decisions that they make, and our studies show, at least, that that would not appreciably increase the cost to the employer.

Thank you, Mr. Chairman.

Chairman BOND. Thank you very much, Dr. Anderton.

Ms. Terri Neese.

Ms. NEESE. Good morning, Mr. Chairman and other members of the Committees. Thank you very much for hosting this event today, and I would have to join with John Satagaj to say that I think we could not find better small business advocates than these men and women at the head of this table. They are really tremendous people and have helped us a lot. My own company is a human resources company in Oklahoma, and I am representing the National Association of Women Business Owners and also the National Business Association. I would also like to introduce Sheila Brooks who is here with me today. Ms. Brooks is vice president of public policy for the National Association of Women Business Owners.

I would have to concur that many of these tax issues are important to women and minorities. Certainly, for me in human resources field, finding good talent to hire today is extremely difficult. That is a whole other issue, one that we will not touch on today, but certainly something out there that many small business owners are having to deal with right now. Certainly 100 percent deductibility of health insurance is important to our members, but no issue is more important than repealing the death tax.

For and for women and minorities, in most cases we are first-generation business owners. So reality has just hit, and we are beginning to understand that we will not be here forever. The question keeps coming up: And what are we going to do with this business? So, as we look at that, we are trying to figure out: how do we take the money out of the business to spend, how do we make sure we put all of our assets in trust, or how do we protect ourselves so we can pass our business on to our children so they would not have to sell that business in order to pay the estate taxes? We realize also that we pay payroll taxes, income taxes, property taxes, sales taxes, and some of us pay State income tax. But, if we are successful enough, then we pay the death tax. So eliminating the death tax totally is where our industry stands, and raising the unified credit now will only be a band-aid for the future.

Ms. VELÁZQUEZ. Mr. Chairman, if I may?

Chairman BOND. Ms. Velázquez.

Ms. VELÁZQUEZ. Terri, I would like to follow up on the estate tax issue. Last year, I was a supporter and co-sponsor of the Dunn-Tanner bill. I supported it after I did a lot of research. I listened to so many small business groups coming into my office, and coming to the realization that it was a burden against small businesses. So not only I supported it, I voted for it, but I wrote an op-ed piece in the New York Times. So I want you to react to the fact that the legislation that we will be voting on today leaves small businesses to be the last in line to reap the benefits of estate tax repeal. How do you feel about that?

Are we here discussing issues that are important to small businesses? How do you feel about that?

Ms. NEESE. For our members, of course, I understand about revenues, and that you have to have the revenues. But our members are saying we should look at total repeal, and not raising the unified credit to \$5 million or \$6 million.

Ms. VELÁZQUEZ. Terri, I understand that. My question is small business will have to wait until the year 2011. By that time, many small business are going to be selling their businesses because they cannot restructure it. So do you think that the legislation we are passing today is a fair legislation when it comes to small businesses, that is my question? I know that it would be great. It's a great legislation for those who are on the top.

Ms. NEESE. For me personally, I would say no. I would say a lot of our members would say no, too, because it is very important that we have some relief on this now, not 2011.

Ms. VELÁZQUEZ. That is why I am voting against it, because it is leaving some of the Democrats, and we want to work in a bipartisan way to help small businesses. But that legislation cannot give me any coverage when I go back into my district and I say to small business, sit down, you have to wait 10 years from now.

Mr. PASCARELL. Mr. Chairman, I want to continue on this, because this is a priority to a great number of people in this room, and 98 percent of American families do not pay any estate tax, so we are talking about focusing in on—we know what our focus group is. It seems to me, we look at the Wall Street Journal today, very interesting article right on the front page, that the Bush plan relief would be phased in slowly and repeal would not occur for 10 years. When you look at the graph as to who is going to benefit over the next five years, and we talk about trying to get relief to those people who need it, it makes absolutely no sense. What I am suggesting here is we ought to read what we are voting on, including us on this side of the table.

Chairman BOND. Thank you very much. We have a lot of folks who have asked to respond, and I am going to ask all the people, if you have comments, as I call on you, to respond.

Apparently, our House colleagues have some votes coming up. The nice thing about these roundtables is they can operate without us. So we have votes at 10:30, and as soon as we leave, my staff will take over, and we will continue to get a lot of work done. But we will be back as soon as we can. Thank you all very much for coming.

Mrs. CHRISTIAN-CHRISTENSEN. You are fortunate you have two delegates who do not have to go vote.

Chairman BOND. Okay. Moving along, Henry Cole.

Mr. COLE. Thank you very much, Mr. Chairman. I am Dr. Henry Cole, and I am here representing the Center for Environmentally Advanced Technologies. It is a non-profit organization that promotes technologies that prevent pollution, conserve resources and create new economic opportunities. I would like to say that Congress has a wonderful opportunity before it to help tens of thousands of small business dry cleaners across the nation, and at the same time improve the environment. Chairman Manzullo introduced H.R. 978, which provides a tax credit to cleaners who purchase safe, nonhazardous cleaning processes, and those who do would get a tax credit of 20 percent, and if they are in an empowerment zone, enterprise or renewal community, they would get a 40 percent tax credit.

This bill would help cleaners shift from a dangerous technology, perchlorethylene, to safe technologies, including wet cleaning and

liquid carbon dioxide. If you have been watching the news, you know that there is increasing evidence that this chemical, which is exposing millions of Americans and hundreds of thousands of dry cleaners, is a probable human carcinogen. It also has caused billions of dollars worth of cleanup costs from the releases of this chemical from dry cleaners. That is something that businesses are paying the price tag on, and so are the taxpayers.

Now, not surprisingly, dry cleaners face a host of financial pressures associated with this problem. These include cleanup costs, hazardous waste fees, tougher regulations, bans by shopping center owners, local zoning restrictions, and a shutoff of loans from banks. Talk about problems. It is bad enough to have all the problems of small businesses. When you add those industry-specific ones, you can imagine the pressure.

This bill, H.R. 978, would provide a tax credit and would therefore help these cleaners shift to a technology that eliminates those problems. This legislation last year received bipartisan support. It is beginning to receive strong bipartisan support this year, and it is being supported by cleaners and by environmental organizations. We have 50 environmental organizations that have signed a letter supporting last year's bill. These include large organizations like Environmental Defense, Natural Resources Defense Council, Clean Water Action, representing millions of Americans. So here you have a bill that can both help the environment, help the health and safety of people working in dry cleaning establishments, and at the same time promote technologies and help these dry cleaners avoid these kinds of problems.

We think this is a win-win bill, and it would be wonderful if the leadership of your Committee, the Small Business Committee in the Senate, would join with Congressman Manzullo and introduce this legislation, that would help dry cleaners. It would help create economic opportunities with new technologies, and it would certainly help the environment. Thank you very much.

Senator BOND. Thank you very much, and we will have our environmental staff look at that legislation.

Michael Wolyn.

Mr. WOLYN. Good morning. Thank you very much for the opportunity to speak, and thank you for introducing the small business bills that you have authored this year. I would like to dovetail on something that Steve Anderson mentioned with the restaurants. I happen to represent over 11,000 independent-contractor selling agents across North America in the finished products industry, who happen to use your restaurants as their place of business, and I want to thank you for your comments.

We are in the process of doing an online survey with our 11,000 members, and I will submit that for the record when it is complete. One of the things that we have found is the average dollar amount committed by our folks in meals averages about \$5,200, not \$52,000. We went further to find out what exactly we are spending money on. As we testified last year, if you accept that sugar and caffeine are part of the four food groups, a lot of our people are quite frankly going in and out of these small restaurants, working with their people, and consuming hot dogs, hamburgers, coffee and the occasional doughnut.

So it is terribly important for us to get this meal deduction under consideration. I realize we are moving from 50 percent to 80 percent, but I will submit to you that if it is a business meal, it should be completely deductible. If it is not, it should not be deductible. I do not want to mince any words about whether it is half-deductible or two-thirds deductible. If it is a business meal, it should be deductible.

The other areas we are very concerned about again is health-care deductibility. The average person in our association spent in excess of \$6,000 a year on health care. Obviously, they are not able to deduct those costs. It is a very big issue and again, we will submit that for the record.

The last thing that I would like to talk about is the vehicle depreciation. I thought the comment Ben Cooper made regarding computers was brilliant. We have been talking about this on the Hill now for four or five years. How you can take a piece of hardware and depreciate it over five years when it has a shelf life of maybe 12 months is silly. Further to the point, when you bundle hardware and software, you can deduct it. Most of our people are buying software independent of the hardware and are not getting the benefit of the depreciation, and I appreciate that being discussed.

But the other thing we want to talk about is vehicle depreciation. I see that is part of Chairman Bond's and Manzullo's bills. Most of our people are buying vehicles for the size of the trunk, not for the price of the vehicle. They are carrying product, and I defy you to find a vehicle in the United States today under \$25,000 that has a trunk large enough to put anything in it.

Thank you, Mr. Chairman.

Chairman BOND. Thank you very much. We have a vote coming up in the Senate. So I am going to have to vote. I am going to leave you to the tender mercies of Senator Burns. Good luck, and we wish you the best. I will be back later on, but thank you all very much for being here.

Senator BURNS. If there are any automobile dealers here, I am going to make them very mad, because I buy all my cars at garage sales. The other day, I bought a new Lincoln because it has got a big trunk. You can almost haul cattle in the thing, but it only has 60,000 miles on it. It is a 1993. It doesn't have a pimple or a dimple on it, and I gave them \$7,000 for it. It gets me from point A to point B.

Mark Heesen, president, National Venture Capital Association is next.

Mr. HEESSEN. Thank you. Just two points I want to make. First, on the list that you handed out today, I find it interesting that things have actually been put into three areas, because my view is that if you do not do tax relief properly, you necessarily do not simplify the code, which then, in fact, affects how taxpayers' rights are affected. Our belief is that estate tax repeal is tax simplification, as is AMT repeal, which directly affects the ability of taxpayers before the IRS. It becomes very important when you are looking at revising things instead of repealing things, that you necessarily complicate the code.

This little document from 1926 is going to be twice the size of what it is today, that many times over, if you are going to simply look at tinkering around with estate tax relief and tinkering around with the AMT. I think it is very important that we look at these things and say repeal is tax simplification, and it also is relief for the American taxpayer. You cannot really divide up these issues, in my view. Second of all, for every person around this table, for small business in general, capital formation is the key. We can talk about meal deduction and everything else, but without the capital formation to start the business, you are never going to have a business. So things like capital gains for individuals is critically important as we move forward.

You know, your angel investors, your original investors in companies, are very tax sensitive. Your institutional investors are not as tax sensitive, but for your aunts and uncles who want to help you create a business, they are going to look at the tax consequences. Capital gains is an integral part of that. I think any time you look at change in the tax code and look at tax relief, capital gains really should be an integral part of that relief. Thank you very much.

Senator BURNS. Thank you. Now we will hear from Dorothy Coleman, Vice President, Tax Policy, National Association of Manufacturers. There you are, right there.

Ms. COLEMAN. Thank you, Senator Burns. The NAM's 14,000 members include 10,000 small and mid-sized members, and for them an estate tax repeal is the number one tax priority. Needless to say, we are thrilled that the estate tax repeal bill is coming to a vote on the House floor today. To answer the earlier question, reform just does not work, particularly for our members. They tend to be capital intensive. The value of the business is high. Something like an exemption is just a band-aid. It will have to be revisited. Repeal is what our members are strongly behind, and we are glad this is coming to the House floor today.

The other two top issues on your list are actually very top priorities for our members as well. Rate deduction, particularly for our S-corporation members, is particularly important. Forty-three hundred of our 10,000 small businesses are organized as S-corporations, and for them the reduction in the top individual tax rates to 33 percent would be a real boon to their businesses. One of our members told me other day, when the rate hikes were enacted in 1993, her tax bill jumped by \$50,000 in one year. It is not a huge company, but that is money that she would reinvest in her business.

The other top issue here, repeal or reform of the AMT, both for corporations and individuals, is an important issue for the NAM. Particularly in an economic downturn, the AMT becomes a real problem for our members. During the last economic downturn about 50 percent of American corporations found themselves subject to an alternative minimum tax, actually paying a higher tax bill than they would otherwise under the regular tax system. Thank you very much for having us here today.

Senator BURNS. We thank you. I can remember, we sort of tackled AMT about two or three years ago, and we almost got some reform done. Now we are finding a lot more people qualify for AMT

than they did two or three years ago, and it has got a little bite to it.

We will hear now from Donna Fisher. She is with Tax and Accounting, American Bankers Association.

Ms. FISHER. Thank you for holding this roundtable. I am Donna Fisher with the American Bankers Association, and it might surprise you to know that 95 percent of banks are community banks, and those banks are small businesses that are serving small businesses. So this is a very important roundtable for us as well. I have to kind of argue a little bit with the restaurant folks down the way here. We like to think we are the cornerstone of America's communities.

One of the things I will share with you and leave with the staff is that we do have a book called Compliance, Competition, and the Community Bank Tax Burden, which is a blueprint for tax reform, and we can leave that with your staff. Probably our biggest issues that we have raised with this group are the estate taxes. We are very concerned, though, about the carryover basis versus step-up basis.

That is an issue that has been an ongoing issue for years and years. Carryover was tried before, and it really did not work. I think someone who has a coin collection is probably the best example to use. Over the years, Aunt Mary has added to her coin collection and what is the original basis of all those coins, and how do you determine what the original basis is? So the step-up basis is really important to us as well as for our customers.

The second issue is what we like to refer to as a funding issue, and that is a big issue both for small businesses as well as for small banks. There are also lots of ways to address that issue, but two that we would raise here are farm accounts, which would be good for farmers, ranchers and fishermen, as well as strengthening the agriculture bonds, with which I think some of you are familiar.

The last issue would be Subchapter S reform. We view that as a simplification issue. You may not be aware of this, but for the first time in 1997, small banks could use Subchapter S or elect Subchapter S status. There are a number of issues we would suggest as simplification issues, including the expansion of the types of shareholders, expansion of the number of shareholders, issuance of a second class of stock, which is unique to community banks, modernizing the passive-income rules, and liberalizing the unanimous shareholder-consent rules. All of these, we think, would be beneficial not only for small banks, but for the small businesses they serve in their communities. Thank you very much.

Senator BURNS. Thank you. By the way, I want to remark. Delegate Christian-Christensen, you are a physician. I have a daughter who is in her first year of practice. She has a little tax education, too. I found that out. I think it is wonderful, though. She can start paying me back.

Mrs. CHRISTIAN-CHRISTENSEN. It is going to be a long time. Trust me.

Senator BURNS. Mr. Bond and I were raised in the same state of Missouri, and both of us write alike. Frank—is this Brost.

Mr. BROST. Thank you, Mr. Chairman, I am Frank Brost. I am from the beef-is-what's-for-dinner group, the National Cattlemen's

Beef Association. I am also from your neighboring state of South Dakota.

Senator BURNS. You guys have to learn how to vote down there.

Mr. BROST. I will comment on that later, sir. I am the chairman of our tax committee, on the NCBA. I am also a rancher, and I practiced law for 20 years in a little community in south-central South Dakota. So some of the issues that we are concerned with, I am not only sitting here talking the talk, but I have walked the walk on those issues and dealt with them with the people that suffered from them.

We have five issues, Mr. Chairman, that are a major concern to us. Number one is the elimination of the death tax. That is the leading issue for the NCBA because of the breakup of our multi-generation family farms. As you know, all folks know that are connected with that business, we are capital intensive. We are, as I always say, asset rich, cash poor. We rely heavily on debt because of the increasing capital needs in our businesses. We are in a business that makes three, four, five percent return on our assets, and when you tax us at 55 percent, my little math says that is 11 years, not counting interest, to pay it off. That is a huge issue for us. It has driven many, many young people and ranchers and farmers in business out of business. It is our number one issue.

The reduction of the capital gains, again, is a big issue for us. As you know, we own a lot of assets in our business. The capital gains tax is a big issue for us. Another issue of major importance is the full deductibility of health insurance for our people.

The farm account issues are also important because of the ability to do a better job in averaging our income. Because we are a cyclical income business, we sometimes hold assets or products because of prices and drought and different things, and we sell them later. So it is important for us to be able to take the peaks and valleys out of our income, because our expenses just keep going up. That is a key issue. I think the idea of creating a fund, an account for a rainy day fund in the FFARRM legislation would be helpful for us.

The AMT, as you correctly stated, is kind of like high blood pressure. It is a silent deal, and someday it is going to start killing people. That thing needs to be really worked on because it is going to hit us in our business. Those are the main issues, Mr. Chairman, that we think need to be addressed in this Congress. I appreciate the opportunity on behalf of NCBA to address those issues and present our views to you. Thank you, sir.

Senator BURNS. What is your town in South Dakota?

Mr. BROST. Merdo is where my ranch is located; it is in South Central South Dakota. I now live in the Black Hills and run my ranch from here.

Senator BURNS. I tell you, it is pretty easy to get a ticket in Merdo, isn't it?

Mr. BROST. It surely is, yes. Next time through, give me a call. I can give you some help maybe.

Senator BURNS. I left a lot of checks there. You could not get through there. From Merdo clear to Rapids, you just could not make it.

Mr. BROST. See, that is part of the economic development system of that state.

Senator BURNS. You guys think it is funny. Linda Goold, who has to be smiling, because we just sold our house, and we are trying to buy another one. I will tell you what, my wife has not gotten me back in another house, but I have my drapes picked out. Linda Goold, Tax Counsel, National Realtors.

Ms. GOOLD. I am with the National Association of Realtors, where we are fond of saying that America was built on real estate. I actually want to go back into ancient history. I have been involved with the tax-legislative process for 25 years, working a number of years ago for a senior member of the Senate Finance Committee.

In 1978, we reduced the capital gains rate from 49 percent down to 28 percent. President Carter had proposed raising it to 54 percent a year. That was the beginning of the long string of capital gains reductions. That remains an important issue, but right after we did that reduction down to 28 percent, the Finance Committee held a hearing not dissimilar from this roundtable, asking: what do we do next?

One the most dramatic things that has stayed in my mind all these years came from Secretary Michael Blumenthal. He came up to the Finance Committee and said the single most important issue for helping the economy as we had it then, and if you can remember that was a pretty bad economy in 1978, would be to reduce the depreciable lives of all assets.

A number of the concerns that you have heard today, about computers, about dry cleaning equipment, about capital formation, all of those could be cured significantly if we shortened the lives of all depreciable assets, including real estate. Why? Because for every dollar of depreciation benefits that you get goes straight your bottom line. They improve your rate of return. They expand the amount of income you can keep in your business.

Those issues apply across the board to all equipment and to all real estate. I would wager that if we went around the table here, many of the businesses represented have owners who own their own buildings. They have to recover those costs today over 39 years. If they also have some rental property and they make some improvements for their tenants, who might only stay for six or eight or 10 years, they have to recover those costs over 39 years.

Last summer, the Treasury Department released a study on depreciation, which said there is an across the board need to review depreciation and to consider depreciable lives. In that study, the Treasury Department said that the most imbalanced of all of the assets in terms of depreciation lives and capital recovery was real estate and that 39-year life that applies to real estate does not reflect economic reality in any respect.

Under current law there is also a 27.5-year life for apartment buildings. We are facing a substantial shortage of rental housing in this country, and so that, again, underscores the need to improve the rate of return for those owners. The most significant and substantial way that can be done is to shorten depreciable lives and to revise the depreciation system.

I might add just a word on capital gains. Any time you reduce capital gains rates, it is critical that you also reduce the depreciation recapture rates, or better yet restore the depreciation recapture rates to the 35-year rule that existed before, in which depreciation allowances are treated as capital gains. If you fail to reduce the depreciation recapture rates, every time you reduce capital gains rates, you will be increasing the tax burden for real estate relative to all other assets. Thank you very much, Mr. Chairman.

Senator BURNS. Thank you. We are going to change topics here. I am going to start with Bob Stallman, and of course we have been joined by our colleague, Senator Kerry. I want to move to tax simplification, which Mark Heesen touched on previously. With that, do you have a statement?

Senator KERRY. I do have some comments I would like to make, if I may. Unfortunately, we have Alan Greenspan over in the Finance Committee, too, and my Governor in front of the Foreign Relations Committee, to be confirmed to go to Canada. So I am being tugged in a number of directions. I should have known when I walked in here and everybody was rolling in the aisles, that my friend, Conrad, was presiding.

I am delighted to welcome Nydia over here. We are happy to have her cooperation, and the Chairman also. Thank you very much. First of all, I want to thank everybody for being part of this. These roundtables are the most productive efforts that we have in the Committee in our judgment, that is why we have kept them going this way. We are very appreciative for your participation.

The record that is created out of this, the dialog that takes place is so much more productive in many ways than the standard hearing process. I think the Committee has worked very effectively as a result of that. I gather a few folks have talked about the rate cut and the proposal that is on the table here that is being voted on this week, but I personally am deeply concerned about the President's tax and his budget plans, particularly with respect to small business.

All of you are better validators than we are these days here in Washington, as to the real meaning and impact on some of these choices on your lives as small business people. I am pleading with you to try to weigh in with some of our colleagues on the other side of the aisle, because they would listen to you. Where they may see something that we say as partisan, rather than purely substantive, I suspect they will be much more ready to hear what the practical applications are on your lives, of some these things that are being proposed.

The fact is that the Bush tax plan assists only those small businesses who file individual tax returns. That, as we know, leaves behind millions of small businesses. They have been the most critical component of economic growth in this country in the last years. Those small businesses get no tax reduction from the plan. Notwithstanding, they provide the majority of small business revenue in the country.

Second, the budget proposal actually winds up increasing the burden of what one might call taxation on small businesses, because it increases the interest rates by 50 percent on those that are victims of disasters or get disaster loans. It increases the fees on

small businesses which apply for 7(A) guaranteed business loan. In addition, I think that with what the Federal Reserve report has said about banks tightening credit for small businesses, this is exactly the opposite direction to be moving in.

Forty-three percent of financial institutions put a stricter standard on small business lending, and a lot of them have forced small businesses to provide additional collateral in order to obtain a loan. I am not suggesting that that is necessarily inappropriate as a banking practice or as a business practice, but it obviously makes things tougher and tighter and, therefore, whatever else you do becomes cumulative.

In addition, not one bank reported an easing of the lending standards for small businesses in this survey. Obviously, whatever is happening in the economy at large is having an impact on business practices now.

Last week before the Finance Committee, Dr. Robert Berney, the chief economist at the Office of Advocacy at SBA, said that small businesses suffered more severely than other businesses during the early part of this downturn, and generally speaking, do in any kind of downturn. He believes a strong counter-cyclical public policy of reducing interest rates, lowering taxes and increasing Federal expenditures is appropriate.

Instead, what we see, what the administration is proposing, is an increase in interest rates, an increase in taxes by increasing fees and a cut in federal expenditures for the small businesses. There are other areas where I think we can have a positive impact for small business. I am going to be introducing the Single Point Tax Filing Act, which will make tax filing simpler and easier if you choose to allow the Internal Revenue Service and State agencies to combine on one form both State and Federal employment tax returns. I hope that will ease the bureaucratic burden on small businesses, eliminating unnecessary duplication that many of you face.

Secondly, we know that you are not always treated equally by the tax code. So, for instance, self-employed only have 60 percent of their health-care costs deductible. I know we are trying to get to the 100 percent by 2003, but I hope we can resolve that disparity even sooner during the 107th Congress, because that would enormously help lift a burden on the self-employed.

In addition to that, in 1993 I introduced legislation with Dale Bumpers, where we enacted a targeted capital gains reduction for shareholders investing in a qualified business stock, who had got a 50 percent exclusion on the capital gains tax. I would like to see that go further, personally, by eliminating, altogether, the capital gains tax on qualified investments, particularly the so-called critical technologies. I believe if we did that, we would greatly excite investment in the high-value added job sector, which is the fastest and best lifter of all boats, if you will. So I would like to see us do that.

Lastly, with respect to pension plans, in 1999 employer-sponsored pension plans covered only 33 percent of workers in firms with fewer than 25 employees, and only 57 percent in firms with 25 to 99 employees. That compares with an average of 81 percent in firms with more than 100 employees. I believe we ought to make it a major target of the Small Business Committee, to try to per-

suade our colleagues to provide workers in small businesses the same access to retirement plans and to pensions that counterparts in big business have. I think we ought to undertake to do that.

I think we have a big mission ahead of us, notwithstanding all that we have accomplished. I hope in the course of this morning's dialogue, even though we have to go vote in the Senate now, many of you will pick up on this and put your comments before the staff. Thank you very much, Mr. Chairman.

Senator BURNS. Thank you. In tax simplification, we will start with Bob Stallman from the American Farm Bureau.

Mr. STALLMAN. Thank you, Mr. Chairman. I am Bob Stallman, President of the American Farm Bureau Federation and represent our 5 million-member families across our country today.

I am going to state the obvious and that is America's farms and ranches are small businesses, too. I sometimes think the public does not realize that, but we have many of the same issues that we have discussed here today. We are a subset of the small business community, to the extent that the capital intensive nature of our industry means we obviously have a lot of capital assets tied up, most often in the nature of land, some of which is becoming really highly valued now, given what is happening with the economy and the abilities of others to affect the market value.

We also have extreme volatility due to the nature of our business and effects of international markets and also the weather. With that in mind and in keeping in the context of simplification, our number one tax priority is death tax repeal, on which we have already had some discussion here. There are some reasons that we want repeal, rather than increasing the exemption. The primary one is that at death, if you have one family farm that is just a little under the exemption, they have all the emotional upheaval, but do not have a visit by the IRS. If you increase the value of that operation just little bit, they have the same emotional upheaval and have a visit from the IRS. We are picking winners and losers.

The other issue is the appropriate level in terms of value at which the estate tax should apply. Tell me what land prices will do in 10 years, and I can answer that question. Without knowing, the uncertainty still creates the need for extensive planning and the extensive cost associated with that estate planning. As long as the estate tax is in place, the need for planning will exist.

I know of one instance with a family farm that worked very hard with professionals, such as CPAs and attorneys, to come up with a plan, and even then you do not have certainty, because that is now being challenged by the Internal Revenue Service. So, no matter how much you pay, no matter what professionals you get, you still do not have certainty, and that is why we favor repeal.

The other issue I would like to address involves the volatility of farm income and the benefits of FFARRM accounts, which has been mentioned here. FFARRM accounts will allow us to plan, to do some financial risk management as producers, and that is critical. One other tax priority, and I will mention it briefly before going to some others, is the need for capital gains relief. The capital-intensive nature of our business means that lower capital-gains taxes would be very important to us.

The other small business issues that we have talked about, whether it be greater expensing under Section 179, deductibility of health insurance, or the alternative minimum tax, in terms of real simplification these are issues that need to be addressed.

Lastly, with respect to deductibility of meals, most farmers have their business conferences on the tailgates of pickups. We are eternal optimists, however, and hope one day to be able to go into the restaurants that Mr. Anderson represents and have our meals and therefore deduct the costs. Maybe we can work out field delivery.

Chairman MANZULLO. If I recall, President Clinton's tax increase in 1993 increased the marginal rates of most of the business people who have Sub-S corporations. That was not mentioned by Senator Kerry. I do not have the opportunity to do that, but I find that that was a huge tax increase on small businesses. Very few numbers of small businesses have small Sub-S corporations, so that is where the taxes went up. Perhaps, Mr. Regalia, you want to embellish on that.

Mr. REGALIA. My name is Marty Regalia and I represent the U.S. Chamber of Commerce. On behalf of our three million extended members, 96 percent of which are small businesses, I want to thank you for having this roundtable discussion. Representing the Chamber and its myriad member businesses is often times a little bit daunting. As I look at this list of small business tax priorities, I find very little on this list that I would not support or that our members would not support. Very specifically, I think in terms of the broad-based issues of estate tax reform, rate deduction, AMT repeal, these are things that the economy needs to continue to grow and to prosper.

We look at the deduction area, and we see things like the health-care deduction for self-employed and the meal deduction as being imperative for a continuing vibrant small business sector. As an economist, I know the importance of investment and capital formation, and clearly, our taxes on capital in this economy are onerous and are counterproductive. Proposals like expanding the Section 179 expensing and really going beyond that to address the entire area of accelerated cost recovery for assets, I think, are highly important.

In addition, the R&E credit should be made permanent. While it is effective already, it would be more effective if it was made permanent. Moreover, regulatory reforms like the cash-method of accounting are also issues that we support.

I think that one of things we have to remember right now is that there is a tax package in play that includes three of these major proposals: the estate tax reform, broad-based rate deduction, and permanent extension of the R&E. I would urge the Congress and the Senate to pass this particular tax package, and do it now, because, as an economist, I know that people behave rationally. They form opinions rationally. If we give a tax cut to the American people that is a permanent tax cut, they will respond very quickly in terms of renewed confidence and renewed spending, and they will keep the economy growing. So the most important tax cut is the one we can do right now. Thank you.

Chairman MANZULLO. Thank you very much.

Ms. VELÁZQUEZ. Mr. Chairman, if I may?

Chairman MANZULLO. Of course.

Ms. VELÁZQUEZ. Mr. Regalia, you said that you represent the U.S. Chamber of Commerce and 83 percent of the members are small businesses.

Mr. REGALIA. Ninety-six percent.

Ms. VELÁZQUEZ. Ninety-six percent of your members will support the estate tax repeal that we are passing today.

Mr. REGALIA. Absolutely, they would.

Ms. VELÁZQUEZ. Even though it will not affect them until 11 years from now.

Mr. REGALIA. It does affect them. It affects them immediately because by passing a repeal, they begin to plan for that today. It is not just the estate taxes that are paid today. It is the planning for the estate tax. If you do not repeal it, the planning costs, the compliance cost continue. My father-in-law, before he passed away, was a certified life underwriter and estate planner. That is what he did for a living. While I am happy and my wife is very happy that he was very successful at that, we would like to see that particular cottage industry done away with. It is not a productive use of resources.

Ms. VELÁZQUEZ. Sir, I support repealing of the estate tax for small businesses. I do not support for them to have to wait 11 years.

Mr. REGALIA. Anything that you could do to accelerate the entire repeal, we would support and welcome.

Ms. VELÁZQUEZ. I would welcome you to go and talk to Chairman Thomas of the Ways and Means Committee. He is the one to introduce this for scoring purposes. It will cost too much. So they decided if they would go with a today, it would cost too much in terms of small businesses.

Mr. REGALIA. We believe that the fastest repeal of the estate tax would be the best of all solutions. In a world where we cannot have the best, we do not want the perfect to stand in the way of what we see as the good. So we support the House package wholeheartedly.

Ms. VELÁZQUEZ. Four percent of your members will benefit today from the estate repeal, not 96.

Mr. REGALIA. No, 96 percent will benefit and 100 percent of our members support repeal of the estate tax.

Ms. VELÁZQUEZ. Thank you, Mr. Chairman.

Chairman MANZULLO. You have an opinion on that; don't you?

Ms. VELÁZQUEZ. Very strong. You can come to me and talk about bipartisanship. We have demonstrated that in our Committee. I supported repeal of the estate tax last year, but I supported it on behalf of small business, not just two percent.

Chairman MANZULLO. Do you know what I support? It is 100 percent repeal of the death tax on a 100 percent stepped-up basis. Let's get on with it, folks. This is a bunch of crap that is going on here. I had the horrible job of having to counsel a family who had to half of 640 in order to keep the 320 and pay the damn death tax. We have all these reasons and all this stuff, that is good for insurance people—let's just get rid of the damn thing, have a 100 percent stepped-up basis.

Ms. VELÁZQUEZ. Mr. Chairman, I welcome for you today to go to the House floor and make that comment today.

Chairman MANZULLO. Do you know what stops that? The budget rules—Mr. Alford, you are next. Maybe we can repeal those budget rules, too.

Ms. VELÁZQUEZ. I am not in control, Mr. Chairman. You are.

Chairman MANZULLO. Together, we can conquer Washington.

Ms. VELÁZQUEZ. Sure.

Mr. ALFORD. Thank you, Mr. Chairman. We are a federation of 197 chapters, located in 39 States and nations, and we proudly represent the 820,000 black businesses in the United States. Since the beginning of time, in every society and every government people would tithe 10 percent to the Lord and then expect to give another 10 percent to the king. Here we are in 2001, and we have a king, i.e., the government, that is just totally out of hand.

Our tax system is oppressive and it is anti-small business. I would like to think, as we talk about tax relief and tax simplification, that we look at this in the mindset of creating capital access. With fewer taxes to pay or withhold, there will be, more money to infuse into the business. So, tax relief and tax simplification are increasing capital access, which will create business growth and also create jobs. With business growth and job creations, you have established a broader base of tax revenue coming into the Federal government. In regards to H.R. 8, today, Congresswoman Velázquez, we are indeed very proud of your stand last year, your editorial. I was in New York City the day it hit, and reporters were trying to attack you in a very caustic way, but we are very proud of what you have done, and your principles and your courage.

This bill is not as good as the last bill. The last bill did not get through the White House. We think we should not have an all or nothing approach to this. While we certainly could have improvement, we would appreciate and would hold precious every yes vote we get today. Next year, maybe, we can come back and just get rid of the whole thing.

Ms. VELÁZQUEZ. I want to today.

Mr. ALFORD. Good.

Chairman MANZULLO. Go ahead, Mr. Pence.

Mr. PENCE. Mr. Chairman, for those in the room, I am Mike Pence from Indiana. I am a new member and I am chairing the Subcommittee on Regulatory Reform and Oversight. In yesterday's hearing, our first hearing, I wanted to ask Mr. Alford, as you talk about capital formation, I thought about tax cuts today, but there was an interesting suggestion from several of our witnesses to create a vehicle in the tax structure that would allow a rollover of capital gains taxes, the way we do on certain residential properties when those resources are invested in an entrepreneurial way.

I wonder if you could speak to that from a minority business perspective on how wise or unwise that approach might be.

Mr. ALFORD. Let me say, minority business is black business, hispanic business, small business; business is business. If it is good for business, it is good for all business, and we have yet to see an improvement in the tax code or some relief in the tax system with which we do not agree. So we have a high interest in what you are talking about and perhaps support it.

Chairman MANZULLO. Okay. Mr. Gager?

Mr. GAGER. I am president of the Automotive Parts Rebuilders Association, and I want to add my thanks to you for having this roundtable because I think it allows a lot of people have some input into the legislation. There has been a lot of discussion about different changes to the tax code, but one of the things that really hits our industry hard is the nonresponsiveness of the IRS to an issue in our industry that has gone on for over five years. We could fill volumes of paper on everything we have tried to do to overcome this particular issue. The accounting issue is one that had existed for 50–60 years in our industry. But the IRS decided they wanted to work through the industry specialization program, which was supposed to, according to the rules set by Congress, involve the IRS sitting down with industry members and evaluating whatever particular issues were problems with that industry. Unfortunately, the IRS did not do that with our industry. Instead they just went ahead and issued this industry-specific specialization project or program that hurts our industry tremendously.

There are about 73,000 companies involved in our industry with about half a million jobs, covering people that remanufacture automotive parts and a variety of other products. Just about anything that could be manufactured is remanufactured. But this particular issue has been very difficult. So it is a very serious issue for our people. As a result, anything that can be done to get some kind of simplification or protection for our industry in regards to this one specific inventory issue would be deeply welcomed.

Thank you.

Chairman MANZULLO. Appreciate that. The next speaker is Les Shapiro.

Mr. SHAPIRO. Thank you, Mr. Chairman. I appreciate the opportunity to be here along with all my colleagues around the table, and thank you for inviting us. I think this is a good opportunity to commend everyone at this roundtable for the work that they have done in identifying the issues that are most important to their respective industries. I am Les Shapiro, Chairman of the Padgett Business Services Foundation. I am not a lobbyist, which you may find refreshing from time to time. Padgett Business Services is a provider of tax and accounting work to an exclusive client base of small businesses, defined by Padgett to be under 20 employees. As a practical matter, small business means the mom-and-pop type operations, three or four employees, five employees. Padgett has offices throughout the United States, numbering over 300.

I commend Paul Hense for his BFO reference, because I had a blinding flash of the obvious, which comes only after being able to speak toward the very end of this roundtable discussion. Almost everything that can be said probably already has been said, and as Mr. Regalia alluded to during his presentation, I think there is probably not one person at this roundtable who would disagree with anything that has been said. The only contentious issue we have is the Patients' Bill of Rights. I am very pleased that it is not on the priority list at all, so that issue is moot.

Perhaps I speak for everyone, except those who have particular issues to advocate, in stating that the tax priorities identified by the participants are right on target. I think that if you follow the

participants' lead and give a reality check to the issues that have been identified on the sheet of paper that all of us have been provided, you will find those are the sensitive spots, the spots that will touch virtually every small business owner in the nation. That is where the attention should be focused.

I think you will be getting the most bang for your buck in advocating those positions—the AMT, the death tax, the cash versus accrual, and the depreciation rules. Having spent most of my professional career with the Treasury Department and the IRS, I think the taxpayer rights and protections priority section of the priorities list, insofar as they deal with the IRS, always have been real problems and always will be real problems. To the extent that Congress can continue its good oversight of those problems and perhaps even enact legislation that alleviates some of those problems, I think all taxpayers in the Nation, particularly those who are small business owners, will benefit. To the extent that the Padgett Business Foundation can help Congress or any one of the organizations at the table in the work you do, we would be happy to give it a try.

Chairman MANZULLO. We have got requests from seven more. I am going to limit the testimony to two minutes, so if the time-keeper could do that. The next speaker is Amy Angelier.

Ms. ANGELIER. Thank you Mr. Chairman and Ranking Member for hosting this roundtable today, and also to Senator Bond and Senator Burns. I am with Associated Builders and Contractors, and we represent subcontractors, material suppliers and related firms. What I would like to mention under the auspices of simplification today is the issue of cash versus accrual accounting.

The lion's share of our members are small businesses, and many of those members choose to use the cash method of accounting because it is a simple method. They can keep the books themselves, and generally there is no need to bring in an outside practitioner to maintain their books and records on a daily basis, and there is a significant cost savings with that component alone.

However, as you probably know, the IRS strongly favors the accrual method of accounting when merchandise is a factor. That has been a problem for many of our smaller contractors because the IRS, we believe, targets our industry. The IRS came in and audited our members and are converting them involuntarily from cash accounting to accrual. The problem comes with the penalties, fees, back-taxes and assessments associated with that conversion. It is really hard to escape the situation without a penalty approaching six figures. We had a member last year in Michigan who was looking at \$100,000 even and wound up settling, which required taking on a bank loan to settle with the IRS. That is one fewer employee he can hire. It is three less work trucks he can buy.

Chairman MANZULLO. That was the drywall contractor; wasn't it?

Ms. ANGELIER. That was the drywall contractor, yes. I thank you, Chairman Manzullo, for sponsoring the legislation, and we truly appreciate your efforts.

Chairman MANZULLO. We had planned to turn to taxpayer rights and protections at 11:15 a.m. Those who want to join in that, raise up your placards now and we will continue with the list here.

Ms. VELÁZQUEZ. Mr. Chairman, if I may, I would just like to ask Amy, except for cash flow issues, are there significant ongoing problems from the use of the accrual method, and if there are, what are they?

Ms. ANGELIER. From talking to our members, the problem with accrual is all about timing. It is all about when you pay the IRS. So you essentially are giving the IRS an interest-free loan. So if you are a drywall contractor and it takes you three months to be paid, you are responsible for the taxes right away, but you may not receive the taxable income for two, four, six months, until the business pays you.

Chairman MANZULLO. Okay. William Dennis.

Mr. DENNIS. Excuse me. I am going to cheat and not talk about compliance issues.

Chairman MANZULLO. Could you pull the microphone closer?

Mr. DENNIS. I am Bill Dennis. Senior Fellow with NFIB Education Foundation. I would like to point out that when we talk about simplification, there are just so many targets of opportunity and so little time, that you do not know where to begin. I would also point out that some simplification activities cost a lot of money in terms of revenue foregone. For example, with the changes of Section 179, there is a lot of revenue foregone. Nevertheless, there are a lot of things Congress can do to simplify the code that really do not cost much.

For example, the cash versus accrual issue, which has just been mentioned. The IRS made a change earlier this month, but this is an issue that has been going on for one-quarter of a century, and it just needs concerted action. Independent contractors is another thing that can be done relatively easily if we just have the will. It is not a muddy issue for the most part. So let me encourage both committees to begin looking at these kinds of things. Finally, I am sorry Senator Kerry is not here because I believe he made an error in his statement of fact that I think is very important.

He said something to the effect that owners of C-corporations or C-corporations do not benefit from rate cuts. Well, they do. The owners benefit a great deal from rate cuts, and it is important to point out approximately 60 percent of all C-corporations had no taxable income. The reason they have no taxable income is they zeroed out their income by paying themselves salaries for the most part. So the idea that they do not benefit as well is not an accurate one, and I think it is very important for people to understand that point.

Thank you.

Chairman MANZULLO. Nancy Coolidge. I feel like Bob Barker. Come on down.

Ms. COOLIDGE. Thank you very much, Mr. Chairman. I want to thank you particularly for your work on behalf of the 8,000 colleges and universities in this country who are seeking simplification of the tax reporting connected to the HOPE and lifetime tax credits. We are very grateful, particularly for the proposed elimination of the linkage that we were going to be expected to create between the taxpayer and the student.

Since the IRS has this information, it is clearly more appropriate for the agency to do that, than for us to try to retool. It is very im-

portant that all of us be able to use information we currently have available and not have to generate new information. In this regard, another one of your provisions in this bill would eliminate the requirement that we all report the same thing. We do not have accounting systems that are similar. We cannot do it now. It would be expensive and difficult for the entire higher education community to change and generate what is currently required. It is important that the IRS be more flexible than they are currently apparently being in permitting us to report information we have available.

We should all be permitted to have the best information our institution has available, that was sent to the students and that they then have available to use for filing, not to report on students who do not provide or are willing to provide information on their assets. It is inappropriate for the higher education community to try to warn students about penalties that other agencies would impose on them. It is not an appropriate role for the higher education community. The amount of gift aid that is currently required for a reporting condition is not appropriate for us. We have no way of knowing which amounts of gift aid students get, which are deductible from the tax credits and which are not. The basic principle that your bill provides are: if we do not have information and cannot get it easily now, it is not appropriate to require the higher education community to try to change in order to get it.

Chairman MANZULLO. Thank you, and Commissioner Rossotti has been extremely helpful in trying to help us work through this regulation. Ms. Calimafde.

Ms. CALIMAFDE. Two things quickly. The only people who could applaud the estate tax bill that has passed Ways and Means Committee the other day are people who have heard on high that they will live at least 11 years, because if you read that bill, between now and 11 years from now, nothing much happens. In the last year, the rate reduces by 39 percent, which lets you know how slow the rate reduction is in the bill. So basically we are just frozen for 11 years. To me, for most small business owners who are in their older years, this bill does not help them, and we need more help.

In the pension area, there is a terrific bill in the House; it is H.R. 10. In the Senate, it has not been introduced yet. It would definitely help small business owners and their employees be able to save for retirement. As we speak, there is a move in the Senate to take out two of the major small business provisions from this pension bill. One is the family attribution repeal. They want to take that out because they do not think husbands and wives are going to operate fairly in the context of small business. Another is the 401(k) safe harbor match. There is concern that small businesses will not tell their employees they even have a 401(k) plan. Once again, we are getting hit with the bias that small business owners do not treat their employees fairly. These provisions are in the House bill; the move is to take them out of the Senate bill.

In the health care area, we think health-care costs are too high and need to be controlled. It is really important that the Patients' Bill of Rights does not get passed. That legislation would allow small business owners to be sued simply because they are sponsoring health-care plans.

Thanks very much.

Ms. VELÁZQUEZ. I am going to write the leader about the hearing we held last week where we discussed the pension costs, and to detect pension costs.

Ms. CALIMAFDE. Yes, you are talking in terms of the credit?

Ms. VELÁZQUEZ. Yes.

Ms. CALIMAFDE. Yes, there was a credit in the Senate bill last year. I believe it is going to be in the Senate bill this year. That is a very good provision. Hopefully, the conference will take the best of both provisions and end up with a good bill for small business.

Chairman MANZULLO. Thank you. The next speaker is Lee Mercer.

Mr. MERCER. Thank you, Mr. Chairman. I am Lee Mercer representing the National Association of Small Business Investment Companies. Our members are government-licensed, government-regulated, privately-managed venture capital firms that invest in small businesses, generally from about \$250,000 upwards to about \$5 million per investment. These investments are significantly smaller than the typical non-SBIC venture-capital firm. There is a quirk in the tax code that relates to the taxation of unrelated business taxable income for tax-exempt organizations like pension plans, pension funds and other foundations, that serves as a disincentive for investing in small business investment companies, particularly one type of small business investment company that makes subordinated loans, loans that are subordinated to senior bank debt, to growing small businesses.

It does not stop these organizations from investing in venture-capital firms. Indeed, they do make significant investments in venture-capital firms, just not in SBICs, which make these smaller types of investments, particularly the loans to small businesses or to any business that is established really as a pass-through entity, such as a Subchapter S Corporation or an LLC. So we believe there should be an exemption to this restriction that would aid in capital formation.

This change is not going to take revenue away. It does not prevent money from flowing into venture capital. It just reallocates it down more toward the smaller entities that make the smaller loans, which small businesses need.

Thank you.

Chairman MANZULLO. Thank you. The next speaker is Bernard Phillips.

Mr. PHILLIPS. My name is Bernard Phillips, and I am the tax manager for the National Society of Accountants. Our organization consists of CPAs, enrolled agents, tax practitioners, tax attorneys and nonlicensed accountants. I talk to these people on a daily basis. Part of my job is answering tax questions for these people that they cannot solve for themselves, and I am also the liaison for the organization to the IRS.

So the experience that I have is literally in the field, shall we say. The biggest problem that we have come across is with the AMT, and I do not call AMT a bad tax. I call it a disease. I have cases I would like to submit to the Committees that would really prove the point that this is a tax that has to go away. I have a case

right now, in fact, that one of our practitioners called me about yesterday morning. The taxpayer has a \$500,000 net operating loss and owes \$38,000 in AMT. This is sad. We do plan to submit some testimony on this issue to the Committees.

The other thing is that the depreciation rules have to be changed. Again, we are back to simplicity, but it is another problem area for most of the practitioners that we deal with on a daily basis.

There is one more area, and we talked about it earlier, the fact that the attorneys seem to be setting up LLCs instead of S-corporations. These LLCs are treated as a partnership, but because of section 1402, it is unclear who pays self-employment tax. This is an issue that has to be addressed, as well, and I have addressed this with IRS on a number of occasions. We cannot seem to come up with a regulation to handle it. I think it is something that has to be a congressional mandate to IRS to decide who pays self-employment and who does not.

Thank you.

Chairman. MANZULLO. That depreciation is fine. I am putting a \$20,000 rubber roof on my building that is 130 years old, and the cost of the roof is about $\frac{1}{6}$ the value of the building, and what is it for a roof? Thirty-nine years? You tell me that roof is going to last 39 years. I am planning on introducing legislation to do away with all depreciation, expense it out. I am serious. Let the business owner decide, let him or her decide the years they want to depreciate it and offset it against income. That makes life easy. Mr. Shoaf is next.

Mr. SHOAF. I would also like to thank the Small Business Committees for having this event for us. I would like to echo everything I have heard here, even the conflicting feelings about whether it is the bankers or the restaurants that are the cornerstones of America. Every cornerstone that is laid is a job for our members, so we support both. Our members, by and large, believe that the tax code is not fair, it is not simple, and they are looking for ways to simplify and bring fairness to the tax code. Repeal of the death tax is something they have brought to us as a huge unfairness, and a huge complicated mess to figure out in the end. Only full repeal of the death tax is what our members want. They do not want any band-aids. They want to get rid of it. They do not want to have to plan for it. Full repeal is what they need.

In addition, they also want simplification elsewhere. Our members would especially like to see a recognition that construction raw materials should not be counted as inventory, and allow that they be allowed to use the cash method of accounting. Those are things that have been mentioned here today, and I am very glad we have the opportunity to be here to stress that priority as well.

Chairman. MANZULLO. Thank you very much.

Steve Anderson.

Mr. ANDERSON. Thank you very much, Mr. Chairman. Members of Congress love to go to restaurants with members of their families in the campaign.

Chairman. MANZULLO. You know, I chose to be born into a restaurant family.

Mr. ANDERSON. Which we greatly appreciate, and what a strange turn of events, Mr. Chairman. Being a native of the 16th district, I have eaten in one of those fine restaurants, called Manzullo's. I think a lot of people in Congress know that people own the restaurant, but many times they do not really understand the effect public policy has on employees. I am glad everybody is into this cornerstone initiative, and we will franchise that initiative throughout the small business community. While we encourage you to use that and talk about the impact public policy has on employees, as well as employers, we have also launched something called our pro-employee and pro-employer initiative.

I have been in this town for 25 years. I think a lot of times we go before Congress and tell everybody what we are against, and occasionally we have to do that. But I do not think we go up enough and talk about the proposals we favor and what we can do to help employees across this country. One thing I have not heard, and I would like to make sure is on the record, is the association health plan proposal. Labor shortages are hitting all of us, and we are all trying to find ways to add value to the lives of the people that work for our member companies and our member restaurants, in our case. I think the association health plan initiative is a wonderful way to get accessibility to health care coverage to every person in this country.

Also, I think most of us in this room are affected by disposable income. I know restaurants are, and as a result, we are strongly in favor of the cuts in the marginal tax rates. We think it is very important. As a matter of fact, our association has met with President Bush three times in just the last six weeks on this issue, and we think this issue is very important as we go forward. I mentioned our 844,000 restaurants in the country, and the rate cut will have an impact on restaurant sales. But it will also put money in the pockets of people that work in our restaurants.

Chairman MANZULLO. Thank you.

John.

Mr. SATAGAJ. I just wanted to speak briefly on tax compliance issues on a point that has not been raised, but I think it is one that is very important. That issue is to revise the Small Business Regulatory Enforcement Fairness Act to include the IRS under the purview of the act. We need to revise SBREFA, and I think that is a high priority.

On another compliance issue, Les quietly mentioned earlier that he previously worked for the IRS. He was there in the 1990s when they published a penalty handbook. It was a project that pooled all the penalties in one place, but the bad news was that when we saw them all in one place, we realized how many we had in one place. We think Congress should look at those penalties that no longer make any sense and eliminate them. That should be a high priority, as well.

Thank you.

Chairman MANZULLO. I appreciate that. Before we conclude, Congresswoman Velázquez and I have some marching orders for your organizations, and that is we would like you to contact your members and have them get on board H.R. 1037. This is a very far-reaching tax-relief bill for small businesses, cash accrual account-

ing, \$5 million, that is it. You gross under that, you can go on the cash method of accounting. Many of the things we have talked about in terms of reform, there are two complete sections in there that beef up Taxpayer Bill of Rights. This is a powerful bill.

We have worked very, very hard on this bill. Please, you have come here and you gave us advice. Now we are asking you to contact your constituent members and have them contact their members of Congress in order to get on board that bill.

Mrs. NAPOLITANO.

Mrs. NAPOLITANO. I have been in and out, so I did not hear all of the testimony, but I am wondering how many of you have looked at what is being proposed for SBA cuts and how that will affect your companies, those that you deal with, those that you represent. Nobody—

Mr. MERSKI. I could respond to that. Paul Merski, with the Independent Community Bankers of America. One of the major concerns right now in the community banking industry is liquidity and the funding they need to make loans in the community. It has been pointed out here by numerous people around the table that without the funding for small business, both to start small businesses and to expand and to buy the equipment that they need, which primarily comes from community banks, small business would be in very big trouble. We are concerned with a couple of the lending programs that are run through the Small Business Administration, and these are self-financing. We are not looking for subsidies from the Small Business Administration. But the 7(A) loan program in particular, which Senator Kerry mentioned earlier, will be effected by the President's budget through huge fees, both on the lender and the borrower, associated with loans under that program.

I think both the Senate Chairman and the House Chairman of the Small Business Committee have already written in response to that issue asking that these additional burdens not be put on these loan programs, particularly when you have Chairman Greenspan testifying frequently now about the credit crunch in the small business community.

Mrs. NAPOLITANO. The reason I ask is there is a roughly 42-percent cut in SBA, and a lot of them are going to be fee-based, as you are stating the fact. I believe the second-largest amount of loans go to restaurants who are going to be suffering greatly if they are going to have to come up with either 25–75 to get a loan or to get assistance from SBA. They just will not be able to do it. I think it is important we get this message to our members of the Committee, as well as to the Administration, that this is hurtful to small business' ability to survive. No doubt about it. So why are we putting a burden on small business?

Chairman MANZULLO. If the gentlelady would yield, those increases in fees apply to loans in excess of \$150,000.

Mrs. NAPOLITANO. Very few loans, I think, will be below that.

Chairman MANZULLO. It just depends on how you want to keep on refilling the pot, but for people to go into an SBDC, somebody wants to charge them and we have a hearing on it, and people get excited and we say, "Well, you are already paying taxes." When you call the Department of Commerce, do you get charged for every

call? When you call the IRS, do you get the right advice? So why charge people for basic services?

Mrs. NAPOLITANO. Right. I understand. I am a small business person, and I have been. For me to say to my colleagues and others, I am sorry, if you want to increase your business, you are going to have to pay additional money. My small business, in that area, is where we thrive, in that small economy base.

Chairman MANZULLO. Let's just throw it all out. I am upset with Chairman Greenspan. No one talks about the fact—I am from Rockford, Illinois. In 1981, we led the Nation in unemployment at over 25 percent. It reached 27 percent. We lost 100 factories and 10,000 highly-skilled jobs. The one barometer, the one indicator, the Fed, if it looks outside the beltway, all you have to do is call a steel supplier, and you ask the steel supplier how is business, and for nine months he said it is flat. If you do not sell steel, you are not building, but more importantly, you are not building machine tools, and when tools are not being built, that means there are no orders for equipment. That means the wholesalers and the manufacturers are backing up and the retailers are not buying.

So somewhere along the line, Mr. Greenspan needs to understand that when steel suppliers are not selling steel, you do not raise interest rates. Isn't it interesting that when the NASDAQ was at 5,000, that he used words such as an irrational exuberance, saying stock was overvalued, but now the Fed lowers the rates and says the rates have nothing to do with the value of stock.

Let me ask you a question. What is the value of a 1957 Chevy? It is whatever the market brings. Right now, unemployment in Rockford is pushing seven percent. We lost 2,500 employees at Motorola, laid off the first shift at Chrysler Corporation, and no one wants to use the word recession or depression, but I want to tell you something. My brother has a restaurant, and it has been flat now ever since January. I say, "Frankie, just hold on and work through this thing." But I just think that Congress has not gotten it. We sit around here. I mean, we need to pass an immediate tax cut big-time, make it retroactive, get money into everybody's hands.

Anyway, you had a closing statement you wanted to make?

Mrs. CHRISTIAN-CHRISTENSEN. Thank you, Mr. Chairman. I want to thank you and the Ranking Member for holding this hearing, and thank everyone who came here to share information with us. We have heard you, and I know that under the leadership of our Chairman and Ranking Member, we will address many, if not all, of the issues you discussed. I just want to urge everyone, then, on another issue, that I do not think you have heard us clearly on, to look at H.R. 8, the bill that repeals the estate tax, and I have heard that small businesses need relief now. We believe that.

We heard, I think, Mrs. Thurman say when you look at projections, they are really unreliable. H.R. 8 does not give relief to 95 percent or more of businesses for 11 years, almost all of those are small businesses. A 10-year projection—we may just as easily end up with deficits, which on the back end, small businesses and all businesses are going to end up paying for it in the end. I agree we should not sacrifice what is practical and useful for us now for the perfect. Perfect is repeal, but the substitute bill that we also urge you to look at will give small businesses relief within the next year

or two; whereas what is considered the perfect will not give you any for 11 years. I think if you look at it, you will see the sense of what our ranking member said and what I am trying to say to you now.

Chairman MANZULLO. Mrs. Velázquez, did you have a closing statement?

Ms. VELÁZQUEZ. Yes, Mr. Chairman. I just want to thank all of you for being here today, and I do not want to be a pain in the neck, but I hope you understand my passion. That is that I do care about small businesses, and no one can tell me we have not done the right thing because of partisanship. You know, my Committee reported out 27 bills, 20 of which were signed into law, because we work in a bipartisan way. I will ask you to go a step further, go and talk, not only the members, but talk to the leadership, and explain to them what is good for big business is good for small business, too. After all, you are the engine for our economy, and we have to be honest and we have to be serious about the issues that affect small businesses.

When things are not right, we have got to say it. Sir, I expect you to write a letter to the President and to the leadership and say that is not fair that, on the one hand, we claim we are cutting taxes for small business, but on the other hand, we were imposing fees on the 7(A) loan program. How many members of the industry that you represent get 7(A) loans?

So it is important that we say to the Administration it is wrong that you go around and talk about protecting small businesses, when on the other hand, we are cutting the budget of the Small Business Administration by 43 percent. The estate tax we are passing today, well, I do not know, you read the same legislation I read. Maybe they filed another legislation overnight. That is something else. I want to work with you, but we have to work together, because of the budget proposed resolution and on the estate tax and on the tax cut of 1.6 that they claim that I say is more than a trillion dollars, that we passed. There is nothing there that is targeted in terms of actually for small businesses.

So we have got a lot of work to do. I am prepared to do that, but I want you to join with us in doing so.

Thank you.

Chairman MANZULLO. Well, I cannot tell you how much I appreciate working with you.

Ms. VELÁZQUEZ. My passion.

Chairman MANZULLO. It is good. We have a great working relationship, and again, please take a look at our tax bill. What is that number again? I feel like an 800 number. You dial in and we give you a love gift. H.R. 1037. It is a great bill. I want to tell you something. If it were up to Ms. Velázquez and me, we would take care of that estate tax, wouldn't we? But we have to deal with other people in both bodies.

Thank you all for coming. The Small Business Committee is adjourned.

[Whereupon, at 11:47 a.m., the Committee was adjourned.]

APPENDIX MATERIAL SUBMITTED



National Venture Capital Association

**Senate and House Committees on Small Business
A Tax Agenda for Small Business**

Joint Hearing, April 4, 2001

Tax Policies to Stimulate Capital Formation and High Tech-Led Growth

Mark Heesen, President
National Venture Capital Association

Introduction:

A substantial portion of our economy's remarkable growth over the past decade directly can be attributed to our country's venture-backed entrepreneurs. These entrepreneurs have built the high growth companies that have added millions of jobs to our economy. They have also produced innovative new technologies that, when applied to other industries across the spectrum, have vastly increased worker productivity to keep our economy's growth and employment rates high and inflation rate low.

On March 1, I participated in a Senate Small Business Committee round table discussion with industry representatives, academics and policy makers regarding challenges faced by U.S. entrepreneurs and what role the federal government can play in contributing to their success. The discussion generated an indisputable consensus that access to adequate capital is an enabling element to a successful entrepreneurial venture. The formation of that capital is, of course, directly tied to tax policy. As such, I am pleased to offer my recommendations on a tax agenda for small business.

Tax Policies to Stimulate Capital Formation and High Tech-Led Growth:

The number one priority of emerging growth companies is and always has been sufficient and efficient access to capital. This access is enhanced most directly and effectively by lowering the cost of capital via reductions in the capital gains tax rate. In addition, there are several other important tax policy changes that will also contribute to better access to capital by small, entrepreneurial companies.

• ***Broad based individual and corporate capital gains relief:***

Congress has taken important steps in the recent past to help lower the cost of capital, most recently in 1997 when it lowered the capital gains tax rate. But much more needs to be done in this area. Our industry believes that further efforts to lower the tax rate are necessary to the long-term health of our economy and international competitiveness. According to research conducted by the American Council for Capital Formation¹, U.S. investors (who are now half of U.S. households) face capital gains tax rates on both short- and long-term gains, which are

¹ American Council for Capital Formation, "Capital Gains Taxation and U.S. Economic Growth," Testimony of ACCF Senior Vice President and Chief Economist Margo Thornton before the Standing Committee on Banking, Trade and Commerce of the Senate of Canada, December 16, 1999).

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among the highest in the industrial world. While long-term gains for individuals are taxed at a top federal rate of 20 percent in the United States, the average tax rate in the other countries is only 14.8 percent. The short-term capital gains rate differential between the United States and its competitors is even greater: individual U.S. investors face a top federal rate of 39.6 percent compared to an average of only 18.4 percent overseas.

Closing these differentials will significantly enhance the incentive within our country to buy, hold and sell equity instruments for individuals and corporations. In doing so, policy makers will also lower the cost and greatly enhance the pool of capital available to small businesses.

• ***Targeted capital gains relief (IRC Section 1202):***

Congress can more immediately enhance small business access to capital by concentrating on targeted capital gains relief. Focusing on two specific areas under Internal Revenue Code Section 1202 (having to do with qualified small business stock) would not only increase the amount of capital available to small businesses, but it would also restore Congress' original intent of several years ago to provide incentives for investors to fund small, growing firms.

○ ***Eliminate IRC Section 57(a)(7):***

Congress should eliminate Internal Revenue Code Section 57(a)(7), which treats a percentage of capital gains excluded from "regular" taxable income under IRC Section 1202 attributable to the disposition of qualified small business stock (QSBS) as a tax preference item for alternative minimum tax (AMT) purposes. This will ensure that a significant differential exists between overall capital gains rates and the rates applicable to gains realized on dispositions of QSBS and thereby to restore the incentive to invest in such stock that Congress intended to create when it enacted Section 1202 in 1993.

Sen. Susan Collins in early March introduced a bill (S. 455) to amend Section 1202 regarding capital gains exclusion for longer-term investments in small business stocks. Importantly, S. 455 would eliminate Section 57(a)(7) and make other changes that are vital to the venture industry, including reducing the holding period and increasing the permitted rollover period for qualified small business stocks to 180 days.

The Senator's legislation, known as the "Encouraging Investment in Small Business Act," has four Republican and four Democratic original cosponsors. Making the measure even more attractive is the fact that it is estimated to cost the Treasury only \$5 billion over 10 years—an amount that would easily be made up by the tax revenue that the additional small business growth would generate.

○ ***Issue regulations under IRC Section 1045 regarding capital gains "rollover":***

Congress should direct the Treasury Department to issue regulations under IRC Section 1045 addressing how the capital gains "rollover" provisions of that section apply when a partnership disposes of QSBS and reinvests the proceeds in other QSBS.

Section 1045 allows taxpayers other than corporations that dispose of QSBS (as defined in section 1202) held more than six months to defer tax on the sale of those assets if they invest the proceeds in other QSBS within 60 days of that disposition. In 1998, Congress

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amended Section 1045 to make clear that taxpayers holding stock through a partnership could qualify for the benefits of that provision.

Unfortunately, Section 1045 is silent (and the Treasury Department has issued no guidance) regarding how partners can obtain rollover benefits in the context of a variety of very common transactions involving partnerships. For example, virtually all venture managers and most venture investors hold partnership interests in a number of venture capital partnerships. No guidance is available, however, with regard to how a partner's share of gains attributable to one partnership's disposition of QSBS can be rolled over if another partnership, to which that partner has contributed capital, makes a timely investment in other QSBS.

This problem and others could be easily corrected—and at a very low cost—if Congress were to instruct the Treasury Department to issue regulations governing the application of Section 1045 to partnerships. Issuing regulations will fulfill Congress' legislative intent and increase access to capital by our high growth companies.

• ***Alternative Minimum Tax (AMT) Repeal:***

The 30-year-old alternative minimum tax (AMT) system exists separate from, but parallel to, the regular tax system. Under the AMT scheme, taxable income is modified by an intricate series of "adjustments" and by "preference items" to arrive at alternative minimum taxable income. The application of the AMT frequently results in a higher tax payment than required by the regular income tax system.

The AMT is particularly cruel to entrepreneurs. Many of our leading high-tech regions are in high tax states or jurisdictions. As such, many taxpayers are falling into the AMT because the high cost of property taxes and income taxes in these areas, which are not allowed as AMT deductions. Employees who are not reimbursed for their business expenses are injured as well, because these types of miscellaneous deductions are not allowed for AMT. Perhaps worst of all is the fact that incentive stock options are an AMT-tax-preference item. With the dramatic decline in technology stocks, entrepreneurs who exercised these options when the market was at a healthier level are now finding themselves paying taxes on phantom income.

Due to the fact that AMT is not indexed for inflation, the President's plan to cut more than \$1.6 trillion from the regular tax system would cause an estimated 1.5 million more taxpayers to be affected by AMT in 2002, for a total of 4.5 million, according to a Joint Committee on Taxation report. In 2010, the total number subject to the tax is estimated to be 26.9 million, of whom 12.2 million will have been placed into the system by the President's tax plan.

Past research by the prominent economic analysis firm DRI/McGraw-Hill concludes that the repeal of the AMT would, among other things, increase fixed investment, expand the capital stock in the economy, increase labor productivity, and reduce the cost of capital by a significant amount.

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• **Estate Tax Repeat:**

Elimination of the estate tax would have a direct impact on capital formation for entrepreneurs. The tax not only removes equity capital from the economy by taxing venture capitalists and other investors, it also directly affects entrepreneurs themselves. According to a special report prepared for the American Council for Capital Formation Center for Policy Research²:

"...one finds that the estate tax has a disproportionate impact on entrepreneurs as opposed to rich portfolio investors.

To begin, entrepreneurs constitute only 8 percent of the total (weighted) sample. Nevertheless, they hold \$2.4 billion out of the total (weighted) net worth of \$9.9 billion in the sample, or roughly 25 percent. Thus, they are much more exposed to the taxation of wealth accumulation. Put differently, entrepreneurs are three times more likely to be subject to the estate tax than are simple portfolio investors. Or, turning to another perspective, of those liable for the estate tax, 48 percent are entrepreneurs, compared with only 6 percent among those not liable for the estate tax. In short, the estate tax is more likely to tax entrepreneurs and, in doing so, to tax asset accumulation and risk-taking in the economy."

Given this reality, eliminating the estate tax would provide more efficient access to—and a lower cost of—capital for our entrepreneurs. In turn, this would have a profound impact on our economy. According to another recent report by the ACCF Center for Policy Research³, the effects from the immediate elimination or reform of the estate tax, retroactive to January 1, 2001 include:

- o GDP increases a cumulative \$90 billion to \$150 billion over the 2001-2008 period;
- o Job growth ranges from 80,000 to 165,000 per year and the unemployment rate is slightly lower as a result (by 0.1 percent), with essentially no change in the inflation rate;
- o Both consumption and personal saving rise, as does national saving, despite the loss in estate tax receipts to the federal government; and
- o The level of potential output is somewhat higher, by an average \$6 billion to \$9 billion per year.

Conclusion:

America's small, entrepreneurial firms have been the engines of our economy's remarkable growth throughout the past decade. By backing the most innovative ideas and the most skilled and talented entrepreneurs, managers and technical experts, the venture capital community has served as a catalyst to this growth. In order to sustain and build upon this record, the most important tool needed by entrepreneurs is capital. When considering tax policy, the wisest policies are those that lower the cost of this essential tool.

² "The Death Tax: Impact on Investments, Employment, and Entrepreneurs," by Douglas Holtz-Eakin, chair of the Department of Economics at Syracuse University and editor of the National Tax Journal. Published by ACCF Center for Policy Research, August 1999.

³ "Macroeconomic and Revenue Effects of the Elimination of the Estate Tax," special report for the ACCF Center for Policy Research prepared by Dr. Allen Sinai, chief global economist and president, Decision Economics, Inc., March 2001.

**UNIVERSITY OF CALIFORNIA
OFFICE OF THE PRESIDENT**

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from: **DIANA GOURLAY**
Legislative Director
University of California
Office of Federal Government Relations
1523 New Hampshire Avenue, NW
Washington, DC 20036

TO: Mark Warren
Tax Counsel to Senate Committee on Small Business

RE: University of California testimony at Small Business Committee Roundtable

MESSAGE:

For your files, following is our testimony on Hope and Lifetime Learning reporting requirements.

Talking Points for Small Business Tax Committee Roundtable
April 4, 2001

University of California

1. Thanks to Congressman Manzullo for his interest in the improvement of the Taxpayer Relief Act to make it more useful to students and to the institutions that provide information to the federal government. Special thanks from the *entire* higher education community for the inclusion in this bill of the *elimination* of the requirement that colleges link students with their respective taxpayers. The IRS already has the information to link taxpayers with their dependents, while colleges and universities do not. While there has been no attempt to implement this burdensome demand, it is important that the law be changed to reflect the reality that this connection between students and their parent taxpayers can be accomplished most efficiently by the federal government and not by the higher education community. Repeal of this provision would bring the law into conformity with the current IRS position.
2. It is critical that the IRS permit institutions to provide the best information they have available on qualified educational expenses paid by students, *even if this data element is not standardized for all reporting entities*, as would be ideal. The 8000-plus institutions of higher education do *not* have accounting systems that permit them all to provide information to the IRS in a similar manner. This bill will permit institutions that can provide the statutorily required "amount paid" for qualified educational expenses to report it to students and will also permit institutions that *cannot* provide the actual amounts paid to instead report the amounts that they assessed students when that is the best information they have available. *One size does not fit all*, and the IRS must permit the reporting of the best information available and allow reporting institutions to label the data element appropriately. The institution can identify on the 1098-T whether the dollar amount provided

comprises the actual amount paid by or on behalf of the student or the amount that the student was assessed. Because institutions are not similarly equipped with the system capability to provide uniform data, the IRS must accept the best we have to offer. Absent this legislative relief, there is a very serious concern that the IRS will not permit the institutions to provide the best information they have available, but will insist that all schools report "the lowest common denominator" in the interests of uniformity. Such a rigid demand will effectively require schools to spend money to develop systems that will produce data that is misleading to students applying for credits. Students and their families will expect to transfer data off the 1098-T to their tax filing forms, just as they do with information off their W-2's, so it is especially important that the information represent the best information available from each institution and that it be appropriately labeled, to reduce misuse.

3. The higher education community supports the provision in this bill that makes it clear that colleges would not be expected to report on students for whom they do not have taxpayer identification numbers (TINs) or social security numbers (SSNs) or who direct the college *not* to use their TINs/SSNs as part of a 1098-T. As many students are ineligible to claim either the Hope or Lifetime Learning tax credits, 1098-T data that is not associated with an SSN is superfluous. In addition, some students who will not take advantage of these tax benefits are put in the position of being required to provide personal information to the IRS, which could be construed as an unnecessary invasion of privacy. Also, the onus should be on IRS, not colleges, to relay IRS warnings of fines to their students who decline to provide TINs.
4. Most students are not even eligible to claim either the HOPE or the Lifetime tax credits, and 1098-T data that is not associated with an SSN is "noise" in the IRS system. It cannot be used. No citizen should be forced to provide

personal information when they are not seeking a government benefit. Colleges should not be forced to relay IRS warnings of fines to their students who decline to provide TINs.

- 5. Many institutions do not have the system capability to identify “refunds and reimbursements,” nor can many of us calculate what the IRS expect tax filers to report with respect to changes that affect previous year’s tax credits. The costs of retooling all of higher education to provide these “refunds” across tax years, as taxpayers will need them, are simply not warranted by any reasonable cost benefit analysis. This expectation should be dropped, as provided for in this bill.**

- 6. We endorse the bill’s proposal that removes the requirement that colleges provide an “amount” with respect to gift aid. This proposed change in statutory language is justified given the great variation in the ways that colleges identify and account for price discounts and also the variability in the way students and their families determine what they actually pay for with different types of gift aid. These choices make a difference in the taxability of the aid and thus will have an impact on the claiming of educational tax credits. Because discounts offered to offset the qualified educational expenses paid by or assessed of students are complex and varied and because colleges cannot know which are taxable and nontaxable to students, schools should not be required to list or aggregate the grants, scholarships, fellowships, assistantships, waivers, vouchers, remissions, etc. No dollar amounts that we could report would be accurate or useful as “third party verification.” Absent this change in the statute, we are concerned that the IRS will require us to add up dollar amounts that represents very different quantities – apples and oranges and other dissimilar amounts.**

It is critical that the law permit the higher education community to report data already available without additional investment in re-engineering information that is not central to our educational mission.

