How to make America's corporate tax system the most competitive in the world

Many economists have shown that the burden of the corporate tax is borne by employees and consumers in the form of lower wages and higher prices. Instead of making employees and consumers pay the corporate tax, why not institute a true "Warren Buffet" tax and shift the burden to the owners?

Eighty-one percent of American businesses are Subchapter S or limited liability corporations - they operate as "pass through" entities for tax purposes. Their business income is attributed directly to the owners where it is taxed at the individual level. We should tax domestic C-corporation income at the ownership level as well. There would be a number of issues to resolve, but with modern accounting techniques and computing power, it is certainly possible to attribute C-corp income to their shareholders.

Once income (which I suggest should be defined as operational cash flow) is attributed, businesses would make a back-up withholding payment equal to 25% for owner taxes - similar to what they currently do for payroll taxes. That would cover the vast majority of taxes owed by shareholders. To the extent that an individual's tax rates differ from the withheld rate, those individual taxpayers would claim a refund or pay the remaining tax due.

The required business tax withholding payment is, in effect, a forced dividend that eliminates the economically harmful double taxation of dividends and disincentives to repatriating overseas income. Because corporate income already will have been fully attributed to owners, additional dividend payments to shareholders could be distributed without incurring additional tax. This would dramatically increase the incentive for corporations to stop hoarding cash, to pay more dividends, and thereby to promote more efficient allocation of capital and greater economic growth.

There are many details to be developed, but here are the basic elements of the plan:

- Redefine all domestic business taxable income (whether from a C-corp, an S-corp or an LLC) to allow 100% expensing of capital investments. In effect, we would be taxing net operating cash flow.
- Worldwide cash flow will be included in taxable cash flow. Companies would continue to claim a foreign tax credit for taxes remitted to foreign governments; this credit would be passed through to shareholders proportionally.
- Corporations would establish a method to attribute taxable cash flow to shareholders. I would suggest using a # shareholders' days metric -- the number of shares owned divided by portion of the year they are owned.
- Taxable cash flow would be attributed to each owner holding shares.
- C-corps would make a back-up withholding tax payment on behalf of the owners to the IRS equal to 25% of taxable cash flow on a quarterly basis.
- C-corp owners would receive an annual form, similar to a K-1, showing attributable cash flow and the 25% back-up withholding tax payment made on their behalf.
- C-corp owners would include attributable cash flow in their individual taxable income -- and would be able to claim the full back-up withholding as a credit against their tax liability.
- Tax exempt shareholders, pension plans, and foreign shareholders would not be allowed to claim back-up withholding as a tax credit.
- Because taxable cash flow would be fully attributed and taxes would be paid by owners, no additional tax would be due on dividends paid to shareholders.
- Dividend payments made would not be deducted from taxable cash flow.

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