TAX FOUNDATION

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Compliance Costs of Alternative Tax Systems II
House Ways & Means Committee Testimony

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The following testimony was presented on March 20, 1996, by Dr. Hall before the House Ways & Means Committee.

The Tax Foundation estimates that complying with the entire federal tax system will cost Americans almost $225 billion in 1996. The rules and regulations for the federal income tax alone account for approximately $157 billion of this cost.

The cost of compliance, which adds nothing to national output, is tantamount to a tax surcharge on all taxpayers. One way to comprehend the magnitude — and economic waste — of the $157 billion federal income tax surcharge is to imagine wantonly destroying every vehicle produced by the Ford Motor Company and more than one-third of the vehicles produced by the Chrysler Corporation in 1995.

The complexity of systems that directly tax people and businesses — like the current income tax, the Flat Tax, and the USA Tax System — is almost wholly related to tax base questions, that is, questions or uncertainty about the timing or definition of taxable transactions.

If Congress were to replace the current federal income tax with any one of the three predominant alternatives currently being discussed — the Flat Tax sponsored by Rep. Armey (R-Texas) and Sen. Shelby (R-Ala.), the USA Tax System sponsored in 1995 by Senators Domenici (R-N.M.) and Nunn (D-Ga.), or the National Retail Sales Tax Act recently presented by Reps. Schaefer (R-Colo.) and Tauzin (R-La.) — it could dramatically reduce America's tax-related burden without necessarily sacrificing a dime of federal tax revenue. The Tax Foundation has estimated how much each plan could reduce the current system's $157 billion tax surcharge, assuming a reasonable transition period had ensued.

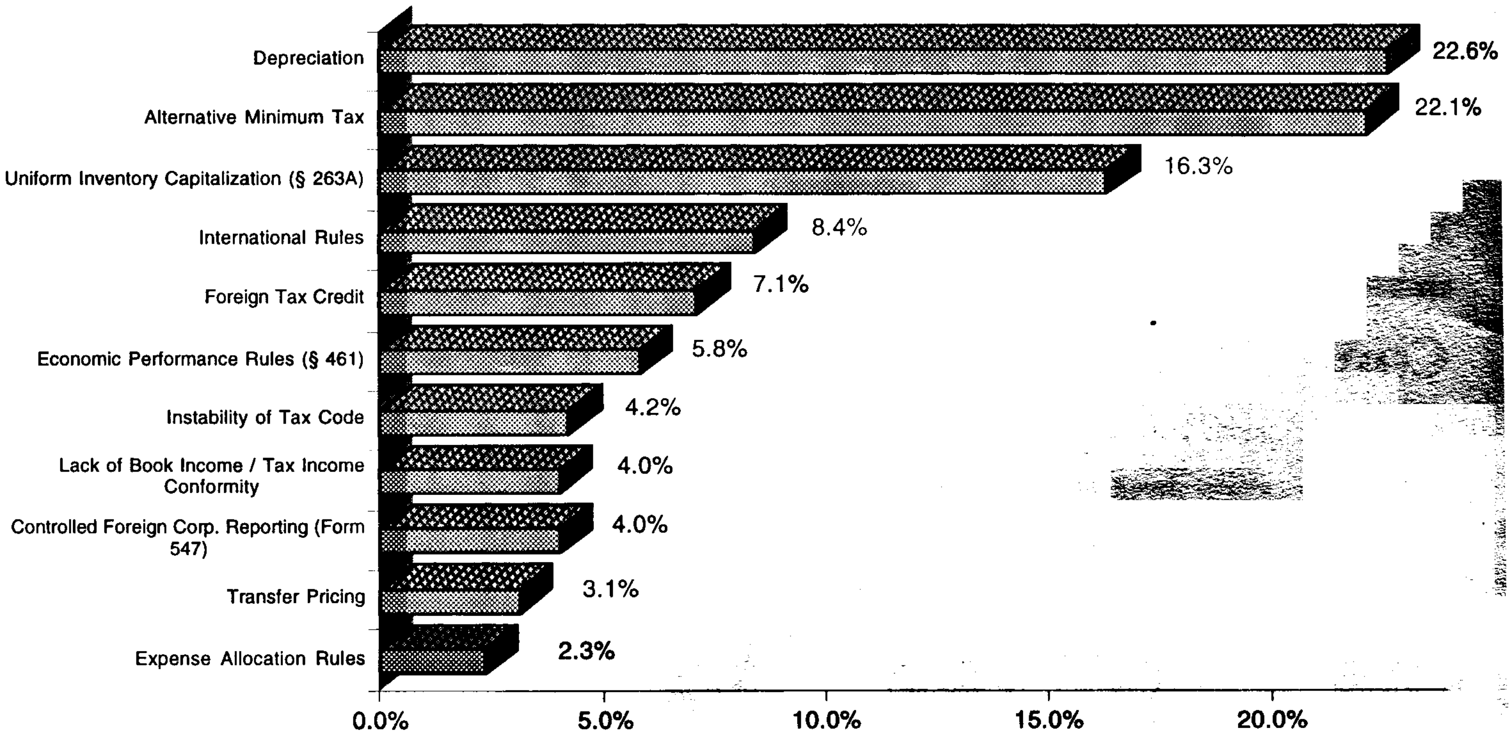
The Armey-Shelby Flat Tax could reduce the surcharge by 94 percent to $9.4 billion. The USA Tax System could reduce the surcharge by 77 percent to $36 billion. The Schaefer-Tauzin sales tax could reduce the surcharge by about 95 percent to $8.2, but the entire burden of this sum would fall on retail and service businesses. However, as currently written, the Schaefer-Tauzin plan would compensate businesses for about one-half of this cost.

These estimates are based on pure versions of the alternative tax systems. It is reasonable to assume that the effect of molding any of the alternative plans into a functioning tax code could increase the complexity, and therefore their associated compliance costs.

Fundamental Sources of Tax Complexity

The cost of complying with a tax system is directly related to the complexity of the system. In terms of complexity, it is fair to say that an income tax — the core of the U.S.

Figure 1
Where the Tax Code is Most Complex (percent of total survey mentions)



Note: 315 of 365 survey respondents answered this question. Many respondents listed more than one aspect. Only the responses receiving at least 10 mentions were included.

Source: Tax Foundation.

government's tax system — ranks among the top of the tax systems currently in operation around the world. Ironically, the term "income" itself accounts for the inherent complexity. Income, particularly business and investment income, is tricky to define, and has, therefore, always added excess complexity to our tax system.

I have discovered complaints about the complexity of the federal income tax system that date back to 1914, the year immediately following the adoption the 16th Amendment to the Constitution which authorized the income tax. Indeed, the 1927 Report of the Joint Committee on Internal Revenue Taxation (Vol. 1, p. 5) states that: "It must be recognized that while a degree of simplification is possible, a simple income tax for complex business is not."

The complexity of systems that directly tax people and businesses — like the current income tax, the Flat Tax, and the USA Tax System — is almost wholly related to tax base questions, that is, questions or uncertainty about the timing or definition of taxable transactions. Multiple statutory tax rates alone do not generate much complexity. On the other hand, the complexity of indirect taxes — like value-added taxes or retail sales taxes — results primarily from the application of multiple tax rates to differentiated products.

The inherent complexity of an income tax base, which bears most predominantly on the income taxation of businesses, results from the difficulty of defining income and determining when to recognize income and expense for tax purposes. Furthermore, a properly constructed income tax (unlike the current federal income tax) also must adopt the added complications associated with adjusting for the effect inflation has on these difficult timing issues.

The Flat Tax and the USA Tax System immediately eliminate these timing-related complexities and, therefore, their attendant compliance costs. Both plans accomplish this objective by moving to a *cashflow* tax base, rather than an accrued income tax base. A

Table 1
Comparison of 1954 Code and 1986 Code (as of 1994)

Subchapter of Income Tax Code	Number of Sections in Subchapter 1954	Number of Sections in Subchapter 1994	Percent Growth
Determination of Tax Liability	4	44	1000%
Computation of Taxable Income	9	145	1511
Corporate Distributions and Adjustments	14	35	150
Deferred Compensation	2	30	1400
Accounting Periods and Methods	6	33	450
Tax-Exempt Organizations	4	17	325
Corporations Used to Avoid Income Tax on Shareholders	4	27	575
Banking Institutions	3	20	567
Natural Resources	3	10	233
Estates, Trusts, Beneficiaries, Etc.	7	29	314
Partners and Partnerships	7	29	314
Insurance Companies	5	29	480
Regulated Investment Companies, Etc.	1	17	1600
Tax Based on Income from Within or Without the United States	9	78	767
Gain/Loss on Disposition of Property	7	42	500
Capital Gains and Losses	4	52	1200
Readjustment of Tax Between Years and Special Limitations	6	5	-17
Tax Treatment of S Corporations	0	14	NA
Other (a)	8	42	425
Total	103	698	578%

(a) Includes all subchapters not explicitly listed as well as Chapters 2-6 of Subtitle A of the Internal Revenue Code.
Source: Tax Foundation computations from Internal Revenue Code.

cashflow tax, as it applies to business, simply calls for the totaling of business receipts and then subtracting off purchases from other businesses. There is no reason to synchronize the timing of income and expenses in such a system.

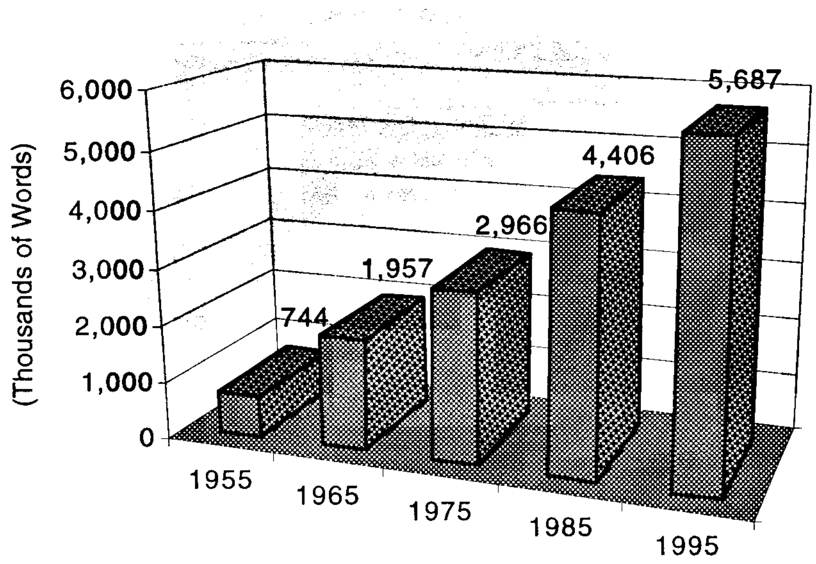
A business cashflow-type tax also eliminates any need for the complexities associated with depreciation and depletion allowances, foreign-source income rules, inventory capitalization, amortization of intangibles, and long-term contracting. This list of items accounts for the bulk of business compliance costs. For example, based on research sponsored by the Tax Foundation, the current rules pertaining to foreign-source income alone account for 45.5 percent of the total federal income tax compliance cost for the firms of the Fortune 500. In fact, adoption of either the Flat Tax or the USA Tax would eliminate virtually every item on *Figure 1*, which illustrates the findings of a Tax Foundation-sponsored survey of senior corporate tax officers about the sources of complexity in the current federal income tax code.

Political Sources of Tax Complexity

Although the Flat Tax, USA Tax System, or a retail sales tax are inherently far less complex than even the most pure income tax system, misguided political tampering can ruin the integrity of any system. Indeed, over time, the political process of give and take has exacerbated the inherent complexities of the federal income tax system. The definition of taxable income has not only expanded dramatically, but it has undergone chronic revision.

Table 1 reveals the dramatic growth in the income tax code over the past 4 decades. In 1954, the federal income tax law comprised

Figure 2
Growth of the Income Tax Code (Laws and Regulations)



Source: Tax Foundation.

103 code sections. Today, that law comprises 698 code sections, a 578 percent increase. Almost all of the growth relates to tax base questions. Note that since 1954 the number of sections dealing with the "Determination of Tax Liability" has grown 1,000 percent; the number of sections dealing with "Capital Gains and Losses," most of which detail "special rules" for calculating capital gains and losses, has grown 1,200 percent; the number of sections dealing with "Deferred Compensation" (e.g., pension plans) has grown 1,400 percent; and the number of sections dealing with the "Computation of Taxable Income" has grown more than 1,500 percent.

Perhaps a more revealing measure of the growth in tax code complexity is the growth in the number of words that comprise the income tax law and its attendant regulations. *Figure 2* charts the growth in the combined number of words that define the body of both the federal income tax laws and their attendant regulations. The Tax Foundation has determined that over the past 4 decades the number of words detailing the income tax laws has grown 370 percent. The words detailing income tax regulations, which provide taxpayers with the "guidance" they need to calculate their taxable income, have grown 753 percent. The combined growth is 664 percent.

The growth in the volume of the income tax laws and regulations has resulted piecemeal from the 31 major tax enactments and the more than 400 other public laws that have amended the Internal Revenue Code since the 1954 Act. Based on a sample of one-fifth of the core sections of the income tax code, these enactments have not only increased the volume of the code but have resulted, on average, in the amendment of each code section once every four years. As *Figure 3* illustrates, this instability has been much more pronounced in the past 20 years than it was during the 20 years immediately following the 1954 Act.

The complexity generated by the growth and constant change of the tax code creates two general types of economic costs. One is the overhead cost associated with the economically sterile exercise of tax planning, compliance, and litigation. The second cost results from the economic opportunities that are foregone because of taxpayer uncertainty.

Because of complexity and instability, despite substantial cost to fund diligent and expert research, taxpayers may not be able to obtain a reasonably certain conclusion about how taxation will affect a business plan or investment. In many businesses, research and development require longer and longer lead times. If taxpayers cannot accurately predict

Table 2
Estimated Cost of Corporate Income Tax Compliance by Amount of Company's Asset Size, 1996

Asset Size/1 ($Thousands)	Compliance Cost as % of Assets	Estimated Compliance Cost
$1,000	0.81%	$8,100
$25,000	0.66%	$165,000
$50,000	0.49%	$245,000
$100,000	0.31%	$310,000
$250,000	0.14%	$350,000
$500,000	0.10%	$500,000
$1,000,000	0.09%	$900,000
$2,000,000	0.08%	$1,600,000
$3,000,000	0.08%	$2,400,000
$4,000,000	0.04%	$1,600,000
$5,000,000	0.04%	$2,000,000
$7,500,000	0.05%	$3,750,000
$10,000,000	0.03%	$3,000,000

1. Excludes financial and life insurance firms.
Source: Tax Foundation.

the tax consequences of a particular economic activity, either because of vagueness, complexity, or instability in the tax code, then tax policy is handicapping the growth and dynamism of the U.S. economy.

Quantifying the Overhead Cost of Tax Compliance

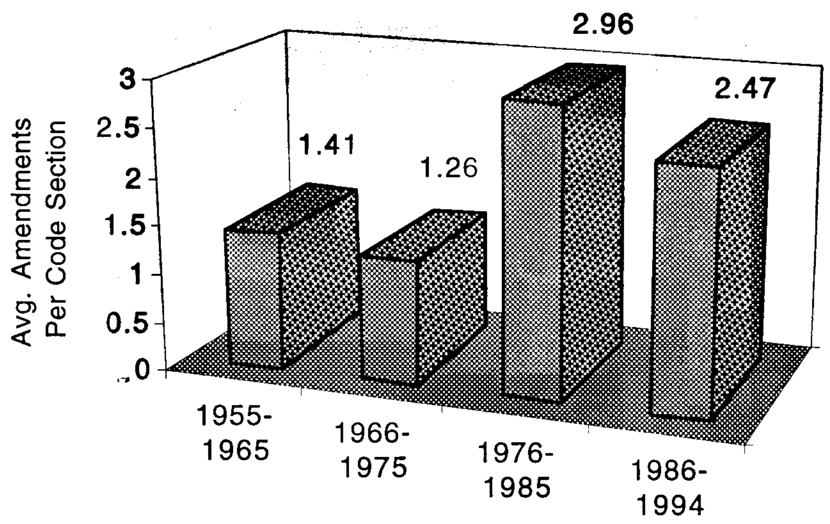
In 1996, based on historical data from the Internal Revenue Service and the Office of Management and Budget, taxpayers will spend about 5.3 billion hours complying with federal tax laws. An hourly cost of $42.4 can be derived by averaging the average labor cost of both the IRS and the accounting firm of Price-Waterhouse. Applying that hourly cost figure to 5.3 billion hours results in a total compliance cost of $224.7 billion. Historically, about two-thirds of the compliance burden (or $150.6 billion) is borne by the business sector. The remaining $74.1 billion is borne by individual taxpayers.

Based on my calculations, at least 70 percent of the total cost of federal tax compliance is due to the income tax, indicating that businesses will pay an estimated $105.4 billion in 1996 to comply with the federal income tax. For businesses, that figure is up from an estimated $83.3 billion in 1992 (70 percent of $119 billion), the latest year for which complete income tax revenue data is available. The 1992 cost of $83.3 billion amounted to 41 percent of the income tax revenue received from all businesses. This ratio offers solid evidence that the income tax on business, particularly the corporate income tax, is an inefficient revenue system for the federal government.

To date, the Tax Foundation has focused its detailed research on the cost to corporations of complying with the federal income tax. The total cost of compliance differs widely across companies of different size. Based on a 1992 survey of large corporations sponsored by the Tax Foundation, the 1996 cost of complying with the federal corporate income tax for the average Fortune 500 firm will amount to an estimated $1.63 million (or $815 million for the entire Fortune 500). For the average small corporation, those with $1 million or less in assets, the <u>minimum</u> cost amounted to an estimated $8,160. But simple averages are quite misleading.

A common research finding clearly demonstrated in *Table 2* is that economies of scale exist in tax compliance. That is, relative

Figure 3
Instability in the Federal Income Tax Code Based on Selected Code Items



Source: Tax Foundation compilation from U.S. Code Annotated (Title 26).

to asset size, small corporations bear a compliance cost burden at least 27.2 times greater (and, on average, perhaps as much as 184 times greater) than the largest U.S. corporations, those with $10 billion or more in assets. What makes this huge differential more amazing from a public policy standpoint is that only 0.16 percent of all U.S. corporations (6,290 returns) paid three-quarters of all corporate income taxes in 1992.

More than 90 percent of all U.S. corporations have assets of $1 million or less and, therefore, bear tremendous relative compliance burdens. In 1992, as a group, these small corporations had to pay at a *minimum* $724 in compliance costs for every $100 they paid in income tax. (For the subset of small corporations that had net income, the figure is $377 in compliance costs for every $100 of income tax paid.) They bore about $28.6 billion in compliance costs for $3.9 billion in income taxes. (That represents about 4 percent of corporate income taxes paid and about 90 percent of the minimum measure of the corporate income tax compliance cost.)

Because complying with tax laws is a fixed cost for any business, it seems likely that smaller companies will bear a greater compliance burden than larger companies under virtually any type of tax system. For example, *Table 3* demonstrates that the value-added tax in Great Britain imposes a compliance burden on that country's smallest companies that is 647 times greater than the burden on the largest firms. Interestingly, however, one measure taken by tax authorities to reduce the compliance burden on small companies in countries that have a value-added tax is to allow these companies to calculate their tax liabilities in a way that is identical to the cashflow method proposed by the Armey-Shelby Flat Tax and the USA Tax System.

Comparing the Relative Compliance Burden of the Federal Income Tax and the Alternative Replacement Proposals

Tables 4 and *5* form the basis of the Tax Foundation's comparison of the cost of complying with the current federal income tax and the various replacement alternatives.

Table 3
Compliance Costs to Businesses of the Value-Added Tax in Great Britain, 1986 and 1987

Size of Business (Annual taxable sales per business in $U.S.)	Compliance Costs as a Percentage of Taxable Sales
0 to 30,000	1.940
30,000 to 75,000	0.780
75,000 to 150,000	0.520
150,000 to 750,000	0.420
750,000 to 1.5 Million	0.260
1.5 Million to 15 Million	0.040
15 Million or More	0.003

Source: Congressional Budget Office, Effects of Adopting a Value-Added Tax, February 1992, p. 71. Original data from Cedric Sandford, et. al., Administrative and Compliance Costs of Taxation (Bath, England: Fiscal Publications, 1989), p. 116.

Table 4 compiles a list of the core individual income tax forms along with both the estimated paperwork-burden calculations (in hours of compliance time) generated by the Internal Revenue Service. It also reports IRS projections for 1996 of the number of tax returns by type. *Table 5* compiles a similar list for the business sector. These lists are far from exhaustive. The lists are also incomplete to the degree that adequate tax return information could not be obtained or estimated for the many schedules and forms that are common auxiliary components of the core forms.

Tables 4 and *5* combined report a total of 3.6 billion hours of required compliance time for the items reported. This figure is well short of the IRS-estimated 5.3 billion hours of compliance time required for the entire federal tax system. However, the magnitude of the minimal lists compiled provide ample information to make comparisons with the replacement alternatives.

To estimate the paperwork burden associated with the alternative replacement proposals (with the exception of the compliance burden on retail businesses of a national sales tax), the Tax Foundation used the same methods that underlie the IRS estimates. These methods are laid out in *Development of Methodology for Estimating the Taxpayer Paperwork Burden*, the 1988 report to the IRS delivered by the consulting company of Arthur D. Little, Inc. In brief, these methods estimate taxpayer paperwork burdens using the various characteristics of tax forms and the informational content of the instructions for these forms.

A. The Armey-Shelby Flat Tax

The postcard-size tax forms advertised by the Flat Tax plan makes the paperwork requirements readily discernible. The average individual taxpayer should take no longer than one hour and eight minutes each year to comply with the Armey- Shelby Flat Tax. The compliance time for the Flat Tax is compared to 11 hours and 36 minutes for the average 1040 Form and two hours and 54 minutes for the average 1040-EZ Form.

Recordkeeping would be simple under the Flat Tax. Both the wage and pension distribution data are supplied to individuals on standard forms (Form W-2 and Form 1099). The average compliance time would be somewhat lower, but, because of the current tax treatment of contributions to pension plans, for the foreseeable future many taxpayers reporting pension and individual retirement account distributions would probably have to make extra calculations to determine what part of the distribution is taxable.

The average business taxpayer should take no longer than three hours and 24 minutes each year to comply with the Flat Tax. That compares to an average 21 hours and 54 minutes for a nonfarm sole proprietor under the current income tax system. It compares to 100-plus hours for the average partnership and

Table 4
A Comparison of the Compliance Burden on Individuals of the Current Income Tax and Alternative Replacement Plans

Individuals Only	1996 Estimated Number of Returns	Average Time in Hours per Form for 1996 Tax Year: Record-keeping	Education Stage	Form Preperation	Packaging/ Sending	Total	Total Hours
Forms							
1040	58,301,036	3.1	2.9	4.7	0.9	11.6	675,320,329
1040A[a]	17,810,000	2.2	2.8	4.2	2.1	11.2	199,175,167
1040EZ	15,510,000	0.1	0.8	1.3	0.7	2.9	44,979,000
1040ES	38,623,500	1.3	0.3	0.8	0.2	2.6	101,064,825
1040X	1,881,500	1.2	0.4	1.2	0.6	3.4	6,334,383
4868 (Extention of Time)	4,854,000	0.4	0.2	0.3	0.3	1.3	6,067,500
1041 (Estates and Trusts)	3,102,300	41.9	17.7	34.1	4.3	97.9	303,766,875
1041A	41,571	28.7	16.9	30.8	9.9	86.3	3,589,538
1041ES	678,500	0.3	0.2	1.4	0.3	2.2	1,504,008
1040 Schedules							
Sch A	44,858,193	2.5	0.4	1.2	0.5	4.6	205,600,049
Sch B	64,083,132	0.6	0.1	0.3	0.3	1.3	83,308,072
Sch D	22,429,096	0.9	0.7	1.0	0.7	3.3	72,894,563
Sch E	27,235,331	2.9	1.1	1.3	0.6	5.8	158,872,765
Sch EIC	8,010,392	0.0	0.0	0.1	0.1	0.2	1,468,572
Sch R	480,623	0.3	0.3	0.4	0.6	1.5	736,956
Individual Totals– Current Income Tax (Forms + Schedules)	307,899,174	NA	NA	NA	NA	NA	1,864,682,603
Armey-Shelby Flat Tax	91,621,036[b]	0.04	0.4	0.3	0.4	1.14	104,447,981
USA Tax System							
Basic Form	94,723,336[c]	0.3	1.8	1.3	1.6	5.00	473,932,423
Sch S (Net Savings Deduction)	66,306,335	0.03	0.3	0.63	0.4	1.36	90,176,616
Sch S-1 (Savings & Withdrawal Info.)	66,306,335	0.14	0.8	1.26	0.4	2.6	172,396,471
Individual Totals– USA Tax (Forms + Schedules)	227,336,006	NA	NA	NA	NA	NA	736,505,509
Schaefer-Tauzin Retail Sales Tax	0	0	0	0	0	0	0

[a]Schedules 1-3 are included in the average time.
[b]Equals sum of nonbusiness 1040, 1040A, and 1040EZ Forms.
[c]Equals sum of nonbusiness 1040, 1040A, 1040EZ, and 1041 Forms.

Source: Tax Foundation, using Internal Revenue Service data and estimation methods.

Table 5
A Comparison of the Compliance Burden on Businesses of the Current Income Tax and Alternative Replacement Plans

Businesses	1996 Estimated Number of Returns	Average Time in Hours per Form for 1996 Tax Year: Record-keeping	Education Stage	Form Preperation	Packaging/ Sending	Total	Total Hours
Sole Proprietorships*							
Form 1040	20,735,964	3.1	2.9	4.7	0.9	11.58	240,191,587
Sch C	18,791,763	6.4	1.2	2.1	0.6	10.27	192,928,762
Sch F	1,944,202	4.4	0.4	1.3	0.3	6.43	12,507,698
Sch SE	12,112,085	0.4	0.3	0.4	0.3	1.33	16,149,446
Partnerships							
Form 1065	1,485,600	38.4	19.8	35.4	4.0	97.58	144,969,800
Partnership Schedules							
Sch D	1,485,600	5.5	1.2	1.3	0.0	8.03	11,934,320
Sch K-1	1,485,600	24.6	8.6	9.4	0.0	42.68	63,410,360
Sch L	1,485,600	15.5	0.1	0.4	0.0	16.00	23,769,600
Sch M-1	1,485,600	3.4	0.2	0.3	0.0	3.82	5,670,040
Sch M-2	1,485,600	1.6	0.2	0.3	0.0	2.07	3,070,240
Corporations							
Forms							
1120	2,115,000	71.3	41.1	72.0	8.0	192.47	407,067,000
1120A	341,900	43.3	23.3	40.8	4.6	111.88	38,252,912
1120S	2,203,100	62.7	20.7	36.6	4.0	124.02	273,221,118
1120X	23,900	12.2	1.1	3.2	0.5	17.10	408,690
1120L	2,747	75.3	23.9	37.3	3.2	139.77	383,924
1120F	21,300	102.4	36.8	64.5	7.0	210.58	4,485,425
1120PC	2,747	106.4	33.3	54.2	5.1	199.02	546,678
1120RIC	7,100	52.4	15.3	29.9	3.8	101.25	718,875
1120REIT	322	55.7	17.3	33.9	4.3	111.18	35,801
7004	2,303,600	5.5	0.8	1.8	0.3	8.35	19,235,060
4626 (AMT)	339,279	18.4	18.2	15.2	0.0	51.88	17,602,926
4562 (Depreciation)	2,456,900	33.7	4.5	5.2	0.0	43.40	106,629,460
1120 Schedules							
Sch D	2,115,000	6.9	3.5	5.7	0.5	16.63	35,179,500
Sch H	211,500	6.0	0.6	0.7	0.0	7.28	1,540,425
Sch PH	105,750	15.3	6.1	8.5	0.5	30.43	3,218,325
1120S Schedules							
Sch D	2,203,100	9.3	4.2	9.2	1.3	24.10	53,094,710
Sch K-1	2,203,100	14.8	10.3	14.7	1.1	40.95	90,216,945
Business Total (Forms + Schedules)	79,153,958	NA	NA	NA	NA	NA	1,766,439,628
Flat Tax	26,881,564	2.3	0.3	0.4	0.4	3.4	91,397,319
USA Tax System	26,881,564	2.5	0.3	0.4	0.4	3.6	96,773,632
Schaefer-Tauzin Retail Sales Tax	NA	NA	NA	NA	NA	NA	192,452,830

* No attempt is made to estimate the other schedules of the 1040 Form that a business filer may be required to complete. Such compliance burdens are left in the Individual section (Table 4).

Source: Tax Foundation, using Internal Revenue Service data and estimation methods.

the 200-plus hours for the average C corporation. The reduction in compliance time comes from a major reduction in every aspect of the overall paperwork burden.

B. The USA Tax System

The USA Tax streamlines the definition of taxable income and would, therefore, substantially reduce the compliance burden associated with the current income tax. However, the USA Tax would require a somewhat greater paperwork burden than the Armey-Shelby Flat Tax. The USA Tax places a levy on both wage and nonwage income and then allows individuals to deduct an unlimited amount of current-year saving. (It also allows individuals to take a credit for payroll taxes paid.) The Flat Tax by contrast adopts a "prepayment" approach that taxes all of an individual's wages (over the exemption threshold), but never taxes income that results from saving.

As a result of this procedural difference, the USA Tax would retain a tax form similar to the current system's 1040A Form and suggests two new basic tax forms — Schedule S (Net Savings Deduction) and Schedule S-1 (Savings and Withdrawal Information). For the average taxpayer that took advantage of the savings deduction, the USA Tax should require no more than eight hours and 58 minutes of compliance time.

The business side of the USA Tax is similar to the Flat Tax in that it is a business cashflow tax. From a compliance perspective, one difference is that the USA Tax would be border adjustable. That is, U.S. businesses could deduct the receipts they generate from the sale of exported goods and services. Border adjustability, therefore, would add to an average business's recordkeeping requirements relative to a Flat Tax. This added recordkeeping accounts for the small difference in business compliance time between the Flat Tax and the USA Tax. In addition, the USA Tax allows for a payroll tax credit. However, the additional compliance costs associated with this credit should be minimal.

C. The Schaefer-Tauzin National Retail Sales Tax

In 1990, the accounting firm of Price-Waterhouse submitted to the American Retail Education Foundation their final report for the *Study to Estimate the Costs of Collecting State and Local Sales and Use Tax*. The study determined that the cost of sales tax compliance for the nation's retailers, on average, amounted to 3.48 percent of total sales tax liability. In dollar terms, this amounted to a 1990 cost of $4.4 billion. This figure is adjusted upward to $6.8 billion in order to reflect the dollar value of all service transactions that would be taxed under the Schaefer-Tauzin plan, but that are typically not taxed under state and local sales tax regimes.

The 3.48 percent-of-tax-revenues figure generated by Price-Waterhouse is best viewed as an historic relationship that does not necessarily generalize to future tax collections. Therefore, my adjustment to the 1990 cost figure ($6.8 billion) is increased by the increase in inflation-adjusted retail sales (20 percent) to yield an $8.16 billion estimated 1996 compliance cost for the Schaefer-Tauzin national retail sales tax. The total hours reported in *Table 5* result from dividing the 1996 cost by the hourly labor cost of $42.4, the labor cost figure used to generate the Tax Foundation's $224.7 billion total compliance cost estimate.

To offset the regressive incidence commonly attributed to a broad-based sales tax, the Schaefer-Tauzin plan proposes to provide a rebate to all wage-earning taxpayers. The rebate will be calculated according to a formula that combines family size, official poverty level statistics, and the number of wage earners per family.

The plan proposes to administer this rebate through a system of payroll tax credits. The rebate, therefore, will not add to individuals' compliance costs, but will add an addition to the compliance costs businesses must bear in association with the payroll tax. However, the additional compliance would be minimal and the Schaefer-Tauzin plan would allow businesses to keep 0.5 percent of the sales tax revenue that they collect on the federal government's behalf.

The Tax Foundation, a nonprofit, nonpartisan research and public education organization, has been monitoring tax and fiscal activities at all levels of government since 1937.

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