

Destination-Based Cash-Flow Tax Retail Sector Break Out

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Agenda

- Taxation of retail sector under current law
- Impact on retail of converting to a cash-flow tax
- Impact on retail of converting to a destination-based tax
- Other tax reform options

Taxation of Retail Sector under Current Law

- According to one study,¹ the retail industry's average domestic effective corporate tax rate over 2007-2011 was 36.4%, nearly 10 percentage points higher than the average of all other industries
- Effect of worldwide tax system on retail
 - Expansion of retail operations in other countries
 - Supply chain for retailers in this country

¹ Source: Report prepared by PwC on behalf of the Retail Industry Leaders Association, *U.S. Retail Trade Industry: Employment, Taxes, and Corporate Tax Reform* (Sept. 12, 2012)

Cash Flow Tax

- Immediately expense most investments
 - Expense investment in a new store other than land
 - Retain inventory rules?
- No deduction for net interest expense
- Impact on retail
 - Pro-growth benefit?
 - Blueprint: Expensing would provide greater incentive to invest compared to current law
 - But no GAAP benefit to expensing, while denial of interest deductions is permanent
 - Simplification benefit?

Impact on Retail of Converting to a Destination-Based Tax

Impact of BAT on Retail Sector

- Border Adjustments – In calculating cash flow, do not include revenue from exports and do not expense or deduct import costs
- Equalizes treatment of U.S.- and foreign-based MNCs with respect to their U.S. tax burden
 - BUT, U.S.-based retailers have disproportionately high percent of U.S. sales
 - Unanswered questions: Treatment of individuals (e.g., buy car in Canada and drive into US; direct b2c sales by foreign retailers)
- Revenue from BAT used to reduce corporate tax rate
 - \$500B annual trade deficit x's 20% tax on imports
 - Would retail disproportionately benefit from this reduction?

Consumption taxes – In general

- Advocates for shifting from taxing income toward taxing consumption point to pro-growth incentives for increased savings and investment and removal of the distortions caused by the corporate income tax
 - Both the DBCFT and a traditional VAT use consumption as a tax base
- In general, is the retail sector opposed to any shift in the direction of a consumption tax?

Effect of DBCFT on Net Importers

- Some advocates of DBCFT claim that it will incentivize U.S. production over foreign production
- These claims are incompatible with others' claims that exchange rates will adjust 1:1 so that net importers won't be hurt

Alternative Tax Reform Proposals*

- Other consumption-based systems
- Corporate integration
- Camp “Option C”
- Enzi
- Trump campaign’s modified worldwide system with a 15% rate