



MAKE IT JUST ANOTHER DAY

FairTaxMI.org

Taxing Services in Michigan

Taxpayers have a natural and healthy resistance to the application of a tax where there is none now, and for this reason, resistance to the idea of applying the FairTax to services in Michigan is natural and should be anticipated. It is important that the FairTax be applied to goods and services purchased by the final consumer for the reasons discussed below.

Today, there is no Michigan sales tax on services, however, that is not to say that services are not taxed. Under the current MI tax code, services are taxed directly via the Single Business Tax (SBT) and personal property tax, real property taxes and other taxes, and indirectly by the taxes passed on to them in the price of the goods and services they purchase in the course of their business. All business taxes are embedded in the prices of the goods and/or services being produced. As Dr. Alan Greenspan has lectured Congress, "Only people pay taxes". Like rent, utilities, supplies, etc., all business taxes are passed on to downstream businesses and/or consumers in the price of the good or service being produced. These taxes are commonly called "hidden taxes" because they are included in the selling price of goods and services and not visible to downstream business and consumers.

Since a MI FairTax would likely eliminate the SBT, personal property and some other business taxes, it would also eliminate these taxes from the hidden taxes. (Because businesses would no longer be incurring the cost of these taxes there would be no expense to pass on to purchasers embedded in the price of the goods and services being produced.) Under the current MI tax code, the producers of both goods and services are paying the SBT, personal property tax, some other business taxes and hidden taxes. To levy a MI FairTax only on the sale of goods removes these taxes from services and completely shifts these taxes to goods. To untax services and drastically increase the tax on goods distorts the economy and natural allocation of resources in the marketplace.

There is no economic justification for the government to pick winners and losers. Do we have as an objective to encourage service businesses to locate in MI at the expense of manufacturing businesses? By increasing the cost of goods and decreasing the cost of services we would artificially distort the economy. When we increase the price of something we discourage consumption of that item. Conversely, when we decrease the cost of an item we encourage its consumption. Why should government be encouraging and/or discouraging the economic activity of individuals and determining winners and losers in the free market. If less government in our personal lives is a desirable objective, then we should get the government out of the business of distorting the free market by regulating the behavior of individuals through artificial price (tax rate) differentials. We must remember that, in the end, the manufacture of goods is the

backbone of our standard of living. We can't eat, live in, transport in, etc. services. There is no logical debate about which is more important, as we value both goods and services and the market determines their relative value.

Some of the problems that will be incurred if only goods are taxed are:

- The tax rate for goods will be increased dramatically to compensate for untaxing services. If we enact a MI FairTax to replace our current Income Tax, Sales Tax, SBT, Personal Property Tax, State 6 mill Education Tax on business, and all business to business taxes, the rate would be about 8.58% (7.47% following enactment of a national FairTax). This rate would have to be approximately doubled if we exclude the sale of services from the tax base, because about half of our economy is comprised of services.
- In a world economy, goods are usually more readily marketed in distant locations than are services. By placing our entire tax burden on goods, the resulting high tax rate would encourage consumers to purchase goods elsewhere. Because of our strong manufacturing base this would be particularly disadvantageous to MI.
- Studies have shown that high tax rates increase the motivation to evade the tax. In essence, the higher the tax the greater the noncompliance.
- To exclude services is to invite intense lobbying to exclude other sectors of our economy, and if the lobbying is successful, result in much higher tax rates on the remaining sectors of the economy.
- Unequal treatment, due to such tax favors, results in resentment from unfair treatment and increased non-compliance will occur.
- Lobbying for tax favors will be almost non-existent with the FairTax because tax favors (loopholes) cannot (will not) be granted. This will result in much less temptation for government officials and lessen any need for campaign finance reform.
- If services are excluded, the MI FairTax will not harmonize with the proposed federal FairTax, which includes taxes on services, and administration of the tax will be more costly and confusing to the public.

It is important to remember that there is no tax on any good or service purchased for businesses purposes. There is no tax liability incurred when an engine is purchased to produce a car, an accountant is paid to provide a financial audit, or a desk is purchased for an office. An engine, accountant's fee or desk is taxed only once and that is when such items are sold to end consumers. This differs from a value added tax (VAT) because the FairTax is levied only one time and that is at the point of retail sale, rather than at every level of production. Because of this, the FairTax is visible to everyone and requires almost no paperwork. A VAT is a tax on business that requires considerable paperwork, and it dishonestly hides the tax from the public via higher prices, similar to Michigan's current business taxes.

Education expenses are considered an investment, rather than a good or service, and, therefore, are not taxed. The cost of education will become more affordable in MI and attract and retain the talent we need to develop our economy to its potential. Another key feature of the FairTax is that it is paid only on retail purchases of services and new

goods by the end consumer. The sale of used goods is not taxed because the FairTax is paid only one time and the tax was paid when the item was originally sold.

To protect the poor, and to assure that no tax will be paid on necessities, The MI FairTax should provide for a monthly "prebate" to every household in the amount of what the tax would be for purchases up to the poverty level for a household of that size. The prebate untaxes the poor and causes the FairTax to be progressive. The prebate prepays the tax on purchases up to the poverty level and it is paid to every household based upon the number of Social Security cardholders residing there. This procedure assures that only legal residents receive the prebate. The attached MI FairTax calculations and the 8.58% mentioned above includes the revenue required to fund and administer these prebates.

According to a recent study conducted by Wirthlin Worldwide and Mellman Group (one survey company generally used by the Democrat Party and the other survey company generally used by the Republican Party) 75% of voters want fundamental tax reform and, by a margin of 4 to 1, voters favor a fair and simple tax system over a tax cut. Other studies show that, when presented with information on the various tax reform alternatives, 85% choose the FairTax over all other alternatives. In other words, the public prefers the FairTax in spite of the fact that it will tax services because it is without loopholes and, thus, FAIR. To further demonstrate the public acceptance of taxing services, almost all candidates for the US House and Senate that advocated the FairTax in the last two election cycles won their races. The huge success of The FairTax Book co-authored by Congressman John Linder and radio talk show host, Neal Boortz is further evidence that the public is way ahead of the media and elected officials on the FairTax. The FairTax Book was number 1 on the New York Times Best seller list for non-fiction for many weeks, whereas, the Steve Forbes book on the flat income tax never appeared on the radar screen.

To be competitive MI must become more business friendly. A MI FairTax will remove the SBT, personal property tax (and perhaps some real property taxes) and most MI hidden taxes from the cost of all goods and services produced in the state, thereby, allowing MI producers of goods and services to be able to sell their products at lower prices while maintaining existing profit margins. We will encourage all companies (and jobs) to locate here, and MI tax revenues will grow with the MI economy. By removing the personal income tax Michigan will be a more attractive place to live and be helpful in attracting and retaining the talent necessary for our prosperity. Let's make Michigan an attractive place to do business and live, then get out of the way.

Roger Buchholtz
MI FairTax Director and
National FairTax Spokesman
10/31/05