

How do you pay down an \$8 trillion debt? The Obama administration needs an answer, as the non-profit Congressional Budget Office says America's debt could rise to \$20 trillion by 2020.¹

One possible answer has a very European ring to it: a VAT, or value-added tax.

What are the chances of Americans paying a national sales tax? And what about an Internet tax? Or an energy tax? Are they also possible?

A VAT of bubbling controversy. Last year, Obama administration economic adviser Paul Volcker mentioned the possibility of a value-added tax. The CBO is now studying the idea.²

India and the member states of the European Union have VATs: sales taxes imposed on producers, distributors and consumers as a product makes its way through the marketplace. VATs collect a great deal of state revenue while discouraging tax fraud. In France, the VAT is 20%; in Germany, 19%.¹

The VAT would not replace our federal income tax, just supplement it. So the furor we saw over health care reform might pale in comparison to the protests over this.

Volcker thinks a VAT is "not as toxic an idea" to America in 2010 as it might have been decades ago. White House budget director Peter Orszag thinks it will never fly, calling it "popular with academics but not seriously considered by policy makers."³

A VAT could generate trillions. The CBO says each percentage point of VAT could bring in \$1 trillion in the next ten years. It also projects that the health care reforms will cost \$2 trillion or more over that period.¹

Some economists and political analysts think a VAT is inevitable. Why, exactly?

Peter Orszag's office, the Office of Management and Budget, has projected federal government expenses of \$5.7 trillion for 2020. However, it estimates that the government will only collect \$4.7 trillion in total taxes in 2020, meaning a deficit of \$1 trillion. Well, at least that's better than the 2010 shortfall of \$1.6 trillion, right? Yes, but ... the OMB projects income tax receipts of just \$2.3 trillion in that year. So if Washington wants to wipe out a 2020 deficit using its #1 revenue generator, it would have to collect 44% more in income taxes, which is unthinkable.³

Rather than trying to do that, it could put a VAT in place – a major tax to be sure. Think double digits. By federal projections, if the government charged Americans a 7% national sales tax on every consumable in 2020, then it could raise \$1 trillion. If it spared essentials like food and clothing from VAT (it likely would), then the VAT would need to be higher than 7%.³

One major gripe about VATs around the world is that they burden the poor. Certainly, poor people in America would be pinched by a VAT, possibly to the point of federal subsidy.

However, the government needs a lot of money in a short window of time, and the VAT is beckoning, with voices such as Volcker, Nancy Pelosi and John Kerry bringing up the idea.

An Internet tax? Back in 1998, President Clinton signed the Internet Tax Freedom Act into law, which prohibited federal, state and local governments from charging bandwidth taxes, email taxes and Internet access taxes. It was extended in 2007 with President Bush's signature.⁴

However, the National Broadband Plan out in April from the Federal Communications Commission contains Recommendation 4.20: "The federal government should investigate establishing a national framework for digital goods and services taxation." It also says, "Recognizing that state and local governments pursue varying approaches to raising tax revenues, a national framework for digital goods and services taxation would reduce uncertainty and remove one barrier to online entrepreneurship and investment."⁵ (Huh?)

So far, this is as far as this idea has gotten. The governments of the United Kingdom and Canada are currently considering Internet tax proposals.

An energy tax? In an interview with Charlie Rose on PBS last year, Volcker floated the notion of "a tax on carbon, tax on energy, that's a big revenue producer if you're willing to do it. Not very popular to say the least." It was part of a roster of potential tax code changes presented to the President in December, and he brought it up again in April in New York City.^{6,7}

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Citations.

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² bostonherald.com/business/general/view.bg?articleid=1245809&srvc=rss [4/9/10]

³ cnn.com/2010/02/05/news/economy/vat_deficit.fortune/index.htmss [2/5/10]

⁴ georgewbush-whitehouse.archives.gov/news/releases/2007/10/images/20071031-17_d-0350-2-515h.html [10/31/07]

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