



Texas VAT Bill Would Threaten State's Prosperity

Boasting the laudable goal of eliminating property taxes throughout the State of Texas, a recently filed Value-Added-Tax (VAT) bill — [House Bill 3472](#) — would replace not only property taxes, but also business franchise taxes, a limited statewide sales tax, and various other local sales taxes with a VAT. Texans have never experienced the economically depressing effects of a VAT, but once they realize what those effects would be, they will oppose any VAT in order to preserve their state's prosperity.



As reported by *The New American*, in 2009 and 2010 [Democrats pushed for a national VAT](#) to balance the federal budget and finance a massive expansion of unconstitutional federal spending. Some [Republicans are willing to consider implementing a VAT](#), even though a VAT is “the most effective way to increase the size of government.” More coverage by *The New American* concerning the VAT can be found [here](#), [here](#), and [here](#), pointing out the prodigious revenue-raising capacity of a VAT as well as the detrimental economic effects of a VAT. Many of these observations about the effects of a *national VAT* would also apply to the proposed Texas *state VAT*.

As of March 26, [House Bill 3742](#) has no State *Senate* sponsor in the Texas State Legislature — a legislative requirement for passage through the Texas legislature — and no House co-sponsors among other Texas state representatives. But that could change overnight if the necessary sponsors materialize, thereby allowing the bill to move forward in the legislative process.

To pay for the statewide elimination of property taxes and other current state taxes, [HB 3742](#) proposes a *state VAT* of seven percent (Sec. 220.104) that would apply generally to “any person who in this state supplies any service or property in the ordinary course of a trade or business in which the person engages for the purpose of profit” (Sec. 220.101), with a few exemptions carved out for governmental entities; religious, educational, and public service organizations; and very small businesses with taxable receipts of less than \$100,000 in the preceding 12-month period (Sections 220.151–220.153).

According to [HB 3742](#), all businesses subject to the VAT would be required to submit to the Texas Comptroller a quarterly tax report that would include, among other calculations, “the aggregate output taxes [VAT charged to customers] and input taxes [the *aggregate VAT* already paid to all suppliers] that accrued during the preceding quarterly period” (Sec. 220.302). This excerpt gives the reader some idea of the complexity of the business bookkeeping — as well as the state governmental oversight — that would be required by the proposed VAT.

Without getting bogged down in the details of HB 3742 — now approaching 300 pages, with various sections reserved for expansion during committee mark-up — the most urgent need for Texans deliberating on this bill is to take a closer look at some of the presuppositions as well as the predictable economic effects of the proposed Texas VAT.

To start with, any VAT — just like any *business tax* — represents a craven concession to the sheer demagoguery of the now-commonplace declaration that “Businesses have to pay ‘their fair share’ of



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taxes!” Anyone with a modicum of business experience understands that in order to stay solvent, businesses must surreptitiously charge the retail consumer of their services or products for any “business” taxes that the government imposes. Businesses do this by adding the cumulative cost of such taxes into the price that is ultimately charged to the retail consumer. Thus, businesses are able to balance their books and stay in business. In a political atmosphere that deliberately obscures the identity of who ultimately pays for ALL taxes — i.e., the retail consumer — businesses simply calculate any government-imposed “business” tax as one more cost of doing business that is necessarily passed on to the retail consumer.

But that lack of understanding of simple free-market economics is not the only demerit of the proposed Texas VAT. A VAT applied to businesses would also distort the marketplace in ways that most citizens may not have anticipated. Each business-to-business purchase in the process of commercializing a service or product adds more “value” and puts more tax into the final retail price. In order to cut costs, big businesses would then tend to reduce their outsourcing of services and subcomponent production to smaller, subcontracting businesses. Furthermore, in order to compensate for reducing their contracts with small businesses, big businesses would tend to invest in building more internal capacity to provide these services or produce those subcomponents *in house*.

From an economic perspective, a VAT would inexorably reduce the size and number of most small businesses while encouraging the expansion and vertical consolidation of many big businesses — thereby leaving the State of Texas much further away from the free market economy that America once enjoyed.

In addition to these *economic* distortions, the historically prodigious revenue-raising capacity of any VAT would become an ongoing *political* temptation to those state legislators who are intent upon expanding Texas state government. Quiet lobbying by influential public officials in Austin for gradually raising the VAT — a fraction of a percentage point during each legislative session — would most likely not be reported in today’s news media.

Citizen opposition to a slowly rising tax burden would likely be muted because the aggregate VAT paid for any service or product is never printed on the retail sales receipt, and because the aggregate VAT *varies* for each service or product, depending on how many business transactions required the addition of yet another VAT into the price during the course of production before the final service or product was purchased by the retail consumer. This process would continue from the initial stage of extracting raw materials that go into a product, its subsequent manufacture, assembly, and even distribution, until it is placed on the store shelves. Thus, most Texans would have a difficult enough time discovering just how much VAT they would be paying for their *own individual* purchases, not to mention the difficulty of figuring out the *total* VAT “tax bite” that is being taken out of *the whole Texas economy*.

To sum up, eliminating property taxes along with several other state and local taxes is a laudable goal — but not at the expense of subjecting the relatively vibrant Texas economy to the damaging effects of a VAT. As proposed, the Texas VAT bill, HB 3742, would downsize or eliminate many small businesses, encourage vertical consolidation among big businesses, and facilitate the growth of state government by gradually increasing the VAT rate.

In contrast, a similarly broad-based retail sales tax paid only by retail consumers would be visible on every purchase receipt, and this visibility would help to rein in the natural tendency of some state legislators to raise taxes, because Texans would be able to keep track of the tax burden on every Texan, with a glance at the retail sales tax rate on any Texas sales receipt. Furthermore, as we have already



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seen above, because this sales tax would be applied only once — at the final point of purchase by the consumer — such a retail sales tax would not distort the Texas economy as the cumulative, hidden effects of a VAT would.

While many of the details of HB 3742 could be successfully worked out in the 2013 Texas Legislative session, it should be clear by now that, all other things being equal, a VAT would smother the Texas economy, while a broad-based retail sales tax on all services and products purchased by retail consumers would allow the Texas economy to flourish.



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