S CORP

DEFENDING AMERICA'S SMALL AND FAMILY-OWNED BUSINESSES

"THE MACRO-ECONOMIC IMPACT OF INCREASING TAX RATES ON HIGH-INCOME TAXPAYERS"

Study Highlights

Overview

- Dr. Robert Carroll and Gerald Prante of Ernst & Young have authored a new study examining the economic impact of the higher tax rates advocated by the President and others on high-income taxpayers.

- Using a new general equilibrium model, the study finds that raising tax rates on Americans earning more than $250,000 over time would result in:

    - Fewer jobs -- 710,000 fewer jobs;
    - Lower wages -- 1.8 percent lower;
    - Less investment -- 2.4 percent less; and
    - A smaller economy -- 1.3 percent smaller.

- For flow-through businesses (S corporations, partnerships, and sole proprietorships), the study finds that the top individual income tax rate on their business income will rise from 35 percent today, to 44.7 percent starting next year.

- The increase in the top two income tax rates would directly affect nearly one million pass-through business owners, and potentially affect another 1.2 million in 2013.

S Corporations are at Risk

- Ernst & Young found that of the 900,000 business owners paying the top two rates, 500,000 are shareholders of S corporations.

- Of the $576 billion in flow-through business income earned by business owners paying the top two tax rates, more than half ($354 billion) is earned by S corporation shareholders.

- In all, 72 percent of all S corporation income is earned by shareholders paying the top two tax rates.

Impact on Business Investment

- Higher tax rates would raise the cost of business investment, resulting in less investment here in the United States.

- The study finds that for flow-through businesses and corporations alike, higher tax rates would increase the cost of business investment:

- For corporations, the marginal effective tax rate on new investment would increase by 15.8 percent; and
- For flow-through businesses, the marginal effective tax rate would rise by 15.6 percent.

- This higher marginal effective tax rate on new business investment over time would reduce investment here in the United States by 2.4 percent, resulting in less capital and lower wages for workers.

Study Specifics

- The study estimated the effects of the policies advocated by President Obama and certain members of Congress that would allow the top tax rates paid by workers, investors, and business owners to rise sharply starting January 1, 2013.

- Specifically, the study looked into the effects of the following tax rate increases scheduled to take effect beginning next year:

  - The top two rates on individual and flow-through income;
  - The top rates on capital gains, dividend, and interest income;
  - The reinstatement of the phase-out of itemized deductions (Pease); and
  - The addition of the new 3.8 percent tax on investment income.

- The study points out that this policy would raise the top tax rate on S corporation and other flow-through income from 35 percent to nearly 45 percent.

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