

# Simplifying the Tax System Will Help Our Economy

By Martin Lobel

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Everyone agrees that our tax system is broken. It is too complex. It interferes with the free market too much, and, worst of all, it doesn't equitably raise the revenue we need to fund programs enacted by Congress. Most of the proposed tax system fixes are the equivalent of putting a Band-Aid on a spurting artery. It is time to stop the auction system of tax legislation and go back to basics: raising the revenue we need with as few special interest subsidies as possible. Now is the time to do it, because this is one of the few times that the public's attention is focused on the issue, which will make it much harder to hide special interest deals behind a cloud of complexity.

Corporate tax laws are so complex that even with the best intentions, it is almost impossible to comply with them. And the temptations to cheat are overwhelming, particularly for the multinational corporations that can use transfer pricing and tax havens to avoid taxation. Every IRS commissioner who has testified on transfer pricing has admitted that the Service cannot police it. This gives those multinational corporations a real competitive advantage over domestic corporations paying much higher taxes.

Abolishing corporate income taxes would make sense if it were possible to impute the income to shareholders and collect taxes from them. But far too many shareholders are tax exempt or foreign, so that's not possible.

Abolishing corporate tax provisions and imposing a tax on the income corporations declare under oath to shareholders and the SEC should be considered. That way, corporations would avoid tax accounting costs and corporate tax rates could be substantially lowered, thereby minimizing the economic distortions

caused by tax planning while raising the same amount of revenue. Such an arrangement would also take some of the pressure off the demand for special subsidies in the tax code by sophisticated corporations. Actually, that could be this proposal's fatal flaw, because it could impair congressional fundraising. This rationale, however, does not apply to taxes intended to discourage harmful behavior, such as smoking or polluting.

There is another problem on the horizon. If we give in to the multinationals' push to adopt international financial reporting standards rather than U.S. generally accepted accounting principles, there will be far too much temptation to use the much looser IFRS to manipulate income and avoid taxes. Finally, in light of increasing worldwide trade, we should work with other countries — particularly those in the OECD — on an international mechanism to ensure that profits don't get "lost" in tax havens.

Individual taxes are too complicated and shift too much of the burden from upper-income to middle-income taxpayers. Even though the IRS is a terrible social welfare agency, Congress continues to impose new welfare programs for upper- and lower-income individuals on it. We need to eliminate all those special welfare provisions and make tax rates truly progressive once again. If a welfare program is worth funding, it is worth reviewing each year in the appropriations process to determine whether it is worth continuing, and if so, at what level. For far too long Congress has financed social programs through the tax system and continued them whether they work or not. At the very least, we need to sunset every tax subsidy at least once every five years.

In short, we shouldn't be satisfied with simply tweaking the system. We need to go back to basics and use the tax system to raise money, not subsidize every special interest that is sophisticated enough or deserving enough of government help. By simplifying and lowering our business and personal taxes, we will make them more equitable and allow our economy to function more efficiently. ■