

**Statement of Bruce Bartlett  
Before the Senate Finance Committee  
March 10, 2015**

Thank you for the opportunity to testify today on the subject of tax complexity, compliance, administration and simplification. I speak not as a tax practitioner, but as someone who has observed the tax policy process at close hand for several decades and written frequently on the subject. I will confine my comments to general observations about what has given rise to tax complexity, what “simplification” means in practice, and obstacles to the achievement of meaningful simplification.

1. ***Distribution tables drive a lot of complexity.*** Although it is seldom said out loud, an important underlying assumption in all major tax bills is rough distributional neutrality or mild progressivity. This means that tax writers are vitally dependent on the distribution tables produced by the Joint Committee on Taxation. There are many technical and conceptual problems with these tables that I won’t go into.<sup>1</sup> One longstanding problem is that no one is quite sure who exactly pays the corporate income tax.<sup>2</sup> I will simply note that if a table looks “wrong” by giving too much of a tax cut to those at the top, this requires redress through some mechanism to take back part of the cut to those in some specific income group as the JCT defines “income.”<sup>3</sup> Often these fixes are complicated and convoluted; I’m thinking about PEP and Pease, for example.<sup>4</sup>

2. ***It’s very hard to cut income taxes without disproportionately benefitting the rich.*** That is because they pay most of the taxes. Any simple cut in rates, even if it is across the board, will produce distribution tables showing massive tax cuts for those at the top, very modest cuts for those in the middle, and nothing at all for those at the bottom because they have no income tax liability. The only way you can “cut taxes” for those with no liability is by making a tax credit refundable. But this simply redefines direct spending into a tax benefit, which is somewhat Orwellian, but satisfies the need to get a distribution table that looks “right.”

3. ***Just because some person or business has no income tax liability doesn’t mean they are relieved of tax complexity.*** When the Tax Reform Act of 1986 was enacted, President Reagan praised it for tax simplification based largely on the fact that a number of taxpayers had been

---

<sup>1</sup> Michael J. Graetz, “Paint-By-Numbers Tax Lawmaking,” [Columbia Law Review](#) (April 1995).

<sup>2</sup> Some recent contributions to the debate on this topic include, “Modeling the Distribution of Taxes on Business Income,” [Joint Committee on Taxation](#) (Oct. 16, 2013); Julie-Ann Cronin et al., “Distributing the Corporate Income Tax: Revised U.S. Treasury Methodology,” [National Tax Journal](#) (March 2013); “How TPC Distributes the Corporate Income Tax,” [Tax Policy Center](#) (Sept. 13, 2012); Kimberly A. Clausing, “Who Pays the Corporate Tax in a Global Economy?” [National Tax Journal](#) (March 2013).

<sup>3</sup> Edward D. Kleinbard, “Reading JCT Staff Distribution Tables: An Introduction to Methodologies and Issues,” [Joint Committee on Taxation](#) (Dec. 9, 2008).

<sup>4</sup> “Deficit Reduction: The Economic and Tax Revenue Effects of the Personal Exemption Phaseout (PEP) and the Limitation on Itemized Deductions (Pease),” [Congressional Research Service](#) (Feb. 1, 2013).

taken off the tax rolls.<sup>5</sup> In effect, he was asserting that paying no income taxes was per se simplification. Of course, this was nonsense. The EITC is the primary reason many people with positive income have no tax liability and often receive a “refund” even though they paid no taxes to be refunded. But the EITC involves complex calculations. Similarly, many small businesses with little or no tax liability may still have complicated returns. And there are big corporations that often have no tax liability that work very hard and jump through a lot of complicated tax hoops to achieve that result. My point is simply that just because someone has no tax liability doesn’t mean they automatically have simple taxes, and just because some legislation increases the number of non-taxpayers doesn’t mean that Congress has made the Tax Code simpler.

**4. *Some of the most serious issues in tax complexity are fundamental to the very nature of an income tax.*** The problem is that it is becoming harder and harder to say precisely what “income” is, or at least taxable income, in today’s world. As this committee knows, the term “income” is nowhere defined in law.<sup>6</sup> Once upon a time when the only income most people received was wages, pensions and perhaps a bit of interest, this was not a problem. But more and more workers these days, such as Uber drivers, are independent contractors; in effect, small businesses, with expenses and incomes that may take multiple forms. The wealthy, especially if they are business owners, can often easily convert wage or interest income into lower-taxed capital gains or dividends. And of course big corporations have whole departments devoted to avoiding the realization of taxable income. Most of the Tax Code’s complexity comes from reporting income.<sup>7</sup>

**5. *Adopting a consumption tax has the potential to achieve meaningful simplification.*** One reason is that consumption is more easily defined and taxed, especially in an increasingly globalized economy, than income.<sup>8</sup> Thus we would be shifting the tax base from something that is increasing intangible to something that is more concrete.<sup>9</sup> Another benefit is that the burden of tax collection would be shifted from individuals to businesses that are better able to employ tax experts. Of course, even consumption taxes break down and Europe has a growing problem with VAT evasion.<sup>10</sup> But at least in principle, individuals would benefit in terms of simplification by paying their taxes as they buy things, rather than having to keep track of income and all the

---

<sup>5</sup> Ronald Reagan, “Remarks on Signing the Tax Reform Act of 1986,” [The White House](#) (Oct. 22, 1986).

<sup>6</sup> Alice C. Abreu and Richard K. Greenstein, “Defining Income,” [Florida Tax Review](#) (2011); Erik M. Jensen, “The Taxing Power, the Sixteenth Amendment, and the Meaning of ‘Incomes,’” [Arizona State Law Journal](#) (Winter 2001); Martin D. Ginsburg, “Taxing the Components of Income: A U.S. Perspective,” [Georgetown Law Journal](#) (Oct. 1997).

<sup>7</sup> Rosemary Marcuss et al., “Income Taxes and Compliance Costs: How Are They Related?” [National Tax Journal](#) (Dec. 2013).

<sup>8</sup> James R. Hines Jr. and Lawrence H. Summers, “How Globalization Affects Tax Design,” [Tax Policy and the Economy](#) (July 2009).

<sup>9</sup> Edward J. McCaffery, “A New Understanding of Tax,” [Michigan Law Review](#) (March 2005).

<sup>10</sup> “2012 Update Report to the Study to Quantify and Analyse the VAT Gap in the EU-27 Member States,” [European Commission](#) (Sept. 2014); Michael Keen and Stephen Smith, “VAT Fraud and Evasion: What Do We Know and What Can Be Done?” [National Tax Journal](#) (Dec. 2006).

exemptions, exclusions, deductions and credits that go with our income tax system.<sup>11</sup> I am highly sympathetic to the tax plan devised by Columbia University law professor Michael Graetz, which would go a long way toward achieving meaningful simplification for most people by eliminating their need to keep records or even file returns.<sup>12</sup>

**6. *We could do a lot more to achieve no-return filing for many people even within the current tax system.*** Few people realize that even under current law, the IRS will calculate your taxes for you if you have a limited income sources, don't itemize or use special tax forms, and have an income below \$100,000.<sup>13</sup> Any number of studies by the Treasury Department and others have shown how return-free filing could be expanded.<sup>14</sup> Other countries have such a system.<sup>15</sup> One problem is that return-free filing would probably require increased withholding on things like dividends and interest. I don't need to remind this committee how unpopular that would be.<sup>16</sup>

**7. *Contrary to popular belief, a single statutory rate tax does very little to simplify the tax system.*** In 1978, there were 26 statutory income tax brackets; 10 years later there were only two. It was widely believed that this led to meaningful simplification for individuals. In fact, the simplification was superficial; the vast bulk of complication in the tax system comes from defining the tax base. The great advance in simplification promised by the original flat tax proposal developed by Stanford scholars Robert Hall and Alvin Rabushka came from adopting a pure consumption tax base; the single rate was basically the cherry on top.<sup>17</sup> In any case, it is effective marginal rates that matter, economically, and just about any effective rate can be achieved even under a flat rate system depending on the nature of the tax base. Furthermore, surveys have shown that hardly anyone knows what their tax bracket is and tend to grossly overestimate it. Keep in mind also that the corporate tax has always been essentially a flat rate, but no one thinks the corporate tax system is simple. There is no evidence that fewer tax brackets improves economic efficiency.<sup>18</sup>

---

<sup>11</sup> Bruce Bartlett, "The Conservative Case for a VAT," [Tax Analysts](#) (Feb. 11, 2011).

<sup>12</sup> Michael Graetz, "The Tax Reform Road Not Taken – Yet," [National Tax Journal](#) (June 2014).

<sup>13</sup> IRS, [Tax Guide for Individuals, 2014](#), p. 205.

<sup>14</sup> U.S. Treasury Department, [Report to the Congress on Return-Free Tax Systems: Tax Simplification Is a Prerequisite](#) (Dec. 2003); Austan Goolsbee, "The Simple Return: Reducing America's Tax Burden Through Return-Free Filing," [Brookings Institution](#) (July 2006).

<sup>15</sup> William G. Gale and Janet Holtzblatt, "On the Possibility of a No-Return Tax System," [National Tax Journal](#) (Sept. 1997); Koenraad Van der Heeden, "The Pay-As-You-Earn Tax on Wages: Options for Developing Countries and Countries in Transition," [International Monetary Fund](#) (Sept. 1994). Just the other day, I noticed that Singapore's Inland Revenue Authority was [praising the benefits](#) of its no-filing service.

<sup>16</sup> Withholding on interest was instituted by the TEFRA legislation in 1982. It was so unpopular it was repealed six months after taking effect. "Congress Passes Repeal of Interest Withholding," [New York Times](#) (July 29, 1983).

<sup>17</sup> Charles E. McLure Jr., "The Simplicity of the Flat Tax: Is It Unique?" [American Journal of Tax Policy](#) (Fall 1997); Lawrence Zelenak, "The Selling of the Flat Tax: The Dubious Link Between Rate and Base," [Chapman Law Review](#) (Spring 1999); Alan L. Feld, "Living With the Flat Tax," [National Tax Journal](#) (Dec. 1995).

<sup>18</sup> David Altig and Charles T. Carlstrom, "The Efficiency and Welfare Effects of Tax Reform: Are Fewer Tax Brackets Better Than More?" [Federal Reserve Bank of Cleveland](#) (1994).

**Table 1. Tax Rate Perceptions and Reality, 2010**

On average, about what percentage of their household incomes would you guess most Americans pay in federal income taxes each year – less than 10 percent, between 10 and 20 percent, between 20 and 30 percent, between 30 and 40 percent, between 40 percent and 50 percent, or more than 50 percent, or don't you know enough to say?			
Tax/Income	All	Tea Party Members	Actual
Less than 10%	5%	11%	86.5%
10% - 20%	26%	25%	12.9%
20% - 30%	25%	26%	0.6%
30% - 40%	10%	14%	
40% - 50%	2%	3%	
More than 50%	1%	1%	n/a
Don't know	31%	15%	

Sources: [New York Times/CBS News Poll](#), [Joint Committee on Taxation](#)

8. *Even radical simplification and reform is highly unlikely to raise economic growth more than a small amount and only over a long period of time.*<sup>19</sup> I know that there are estimates of the compliance cost and the deadweight cost of the tax system that are very high.<sup>20</sup> But the compliance cost is like the cost of commuting to and from work; reducing it would improve our well-being, but wouldn't necessarily raise growth and might even reduce it based on the way GDP is calculated. Reducing the deadweight cost would have an effect similar to reducing the effective marginal tax rate. But as we know from experience after the 1986 reform, which lowered the top rate from 50 percent to 28 percent, there was no outpouring of growth. Serious efforts by economists to find any economic impact from the 1986 Act have turned up very little; mostly accounting changes, not real economic effects.<sup>21</sup> The effect of statutory tax rates on growth tend to be grossly exaggerated.<sup>22</sup>

9. *Strong presidential leadership will be necessary to achieve any meaningful tax reform or simplification.* Political studies of the 1986 act show that President Reagan's personal commitment and the active engagement of the Treasury Department were essential to its

<sup>19</sup> Nancy L. Stokey and Sergio Rebelo, "Growth Effects of Flat-Rate Taxes," [Journal of Political Economy](#) (June 1995); William G. Gale and Andrew A. Samwick, "Effects of Income Tax Changes on Economic Growth," [Brookings Institution](#) (Sept 9, 2014); "Economic Growth and Tax Policy," [Joint Committee on Taxation](#) (Feb. 20, 2015).

<sup>20</sup> Martin Feldstein, "Tax Avoidance and the Deadweight Loss of the Income Tax," [Review of Economics and Statistics](#) (Nov. 1999); "Summary Estimates of the Costs of the Federal Tax System," [U.S. Government Accountability Office](#) (Sept. 27, 2005).

<sup>21</sup> Alan J. Auerbach and Joel Slemrod, "The Economic Effects of the Tax Reform Act of 1986," [Journal of Economic Literature](#) (June 1997); David A. Guenther, "Earnings Management in Response to Corporate Tax Rate Changes: Evidence from the 1986 Tax Reform Act," [Accounting Review](#) (Jan. 1994); Anil Kumar, "Labor Supply, Deadweight Loss and Tax Reform Act of 1986: A Nonparametric Evaluation Using Panel Data," [Journal of Public Economics](#) (Feb. 2008).

<sup>22</sup> "Tax Rates and Economic Growth," [Congressional Research Service](#) (Jan. 2, 2014); "Taxes and the Economy: An Economic Analysis of the Top Rates Since 1945," [Congressional Research Service](#) (Dec. 12, 2012).

enactment.<sup>23</sup> One problem, as this committee well knows, is that of what is sometimes called “salami-slicing,” small compromises to a proposal that was carefully balanced can eventually add up to something worse than nothing at all. I am disappointed that President Bush chose to ignore the recommendations of his tax reform panel, which were very good, and that President Obama and the Treasury have shied away from active engagement in this issue other than to offer a relatively limited business-only reform proposal.<sup>24</sup> The expiration of the Bush tax cuts would have been a perfect opportunity to develop a larger tax package that would have improved the tax code, but it was not utilized.

10. *Tax policy should pay more attention to horizontal equity.* It is a generally accepted principle of taxation that those with similar incomes should pay similar taxes. The complexity of our current system, however, causes tax rates to vary tremendously between those with roughly the same income. The following table and figure illustrate this point.

**Table 2. Distribution of Average Federal Tax Rates, 2012**

Family cash income group	Average rate at each breakpoint in the rate distribution				
	10 <sup>th</sup>	25 <sup>th</sup>	Median	75 <sup>th</sup>	90 <sup>th</sup>
Lowest quintile	-13.7	0.0	5.4	13.1	15.5
Second quintile	-8.7	0.5	7.2	17.0	20.9
Middle quintile	1.7	5.4	13.3	20.4	23.5
Fourth quintile	7.2	12.1	17.2	22.3	26.2
Highest quintile	12.1	17.4	21.9	26.0	29.3
Top 1 percent	8.7	21.2	29.6	32.3	34.6
Total	0.0	5.0	14.5	20.7	25.0

Source: Treasury Department; includes income, corporate and payroll taxes<sup>25</sup>

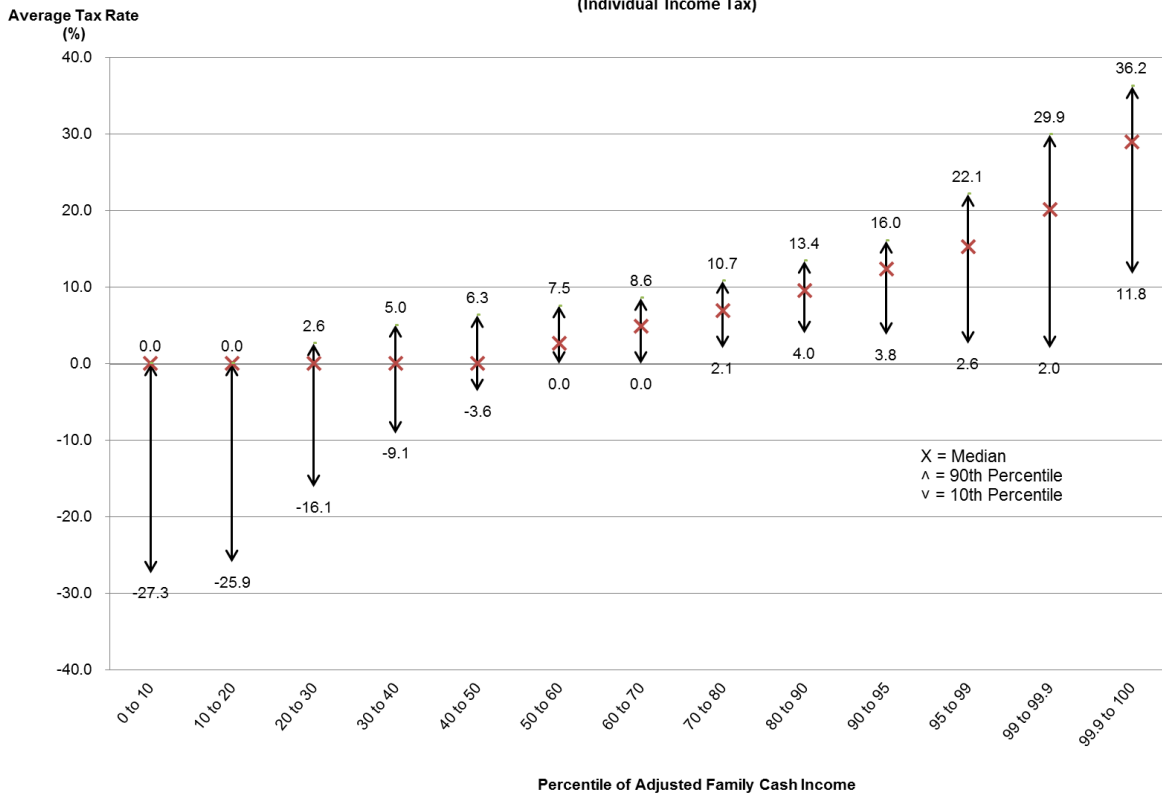
<sup>23</sup> Robert P. Inman, “Presidential Leadership and the Reform of Fiscal Policy: Learning from Reagan’s Role in TRA 86,” [NBER Working Paper No. 4395](#) (July 1993); John F. Witte, “The Tax Reform Act of 1986: A New Era in Tax Politics?” [American Politics Research](#) (Oct. 1991).

<sup>24</sup> President’s Advisory Panel on Federal Tax Reform, [Report](#) (April 13, 2005); “The Advisory Panel’s Tax Reform Proposals,” [Congressional Research Service](#) (July 13, 2006); “The President’s Framework for Business Tax Reform,” [White House and Treasury Department](#) (Feb. 2012).

<sup>25</sup> Council of Economic Advisers, [Economic Report of the President, 2012](#), p. 88.

**Figure 1**

**Variation in Average Tax Rates Within and Across Income Classes  
2015 Current Law and Income Levels  
(Individual Income Tax)**



Source: U.S. Treasury Department, [Office of Tax Analysis](#) (Sept. 23, 2014).

11. **Please make all the “extenders” permanent or get rid of them.** This is particularly a problem with the R&D credit, which has been extended 16 times, often retroactively.<sup>26</sup> By never having been enacted permanently, it fails to achieve its purpose of stimulating additional R&D and is instead a reward for what companies would have done anyway.<sup>27</sup>

12. **Combine overlapping tax incentives for the same purpose.** There are many tax subsidies for education, retirement saving and other worthwhile purposes.<sup>28</sup> Consolidating these incentives would not only achieve simplification, but provide an opportunity to better target them toward those that need them.

<sup>26</sup> Michael Brossmer et al., “Sweet 16: The Research Tax Credit Gets Its 16<sup>th</sup> Extension,” *Tax Notes* (March 2, 2015).

<sup>27</sup> McGee Grigsby and John Westmoreland, “The Research Tax Credit: A Temporary and Incremental Dinosaur,” *Tax Notes* (Dec. 17, 2001).

<sup>28</sup> Elaine Maag, “Tax Simplification: Clarifying Work, Child, and Education Incentives,” *Tax Notes* (March 28, 2011).



13. ***Please give the IRS more money.*** It has been forced to cut back on taxpayer assistance because of cuts to its budget.<sup>29</sup> It has also cut back on audits, thus making the tax system more unfair by rewarding tax evaders.

14. ***Give up on fundamental tax reform for now and concentrate on a few reforms that are not controversial and will help improve and simplify the Tax Code.*** The dream of a tear-up-the-tax-code-and start-over-from-scratch reform is very appealing, but it has never been done in our history. Even a reform as big as those in 1969, 1976 and 1986 appears beyond reach in the present political environment. The hope of doing a big once-and-for-all reform, unfortunately, has held hostage legislation that is needed and would incrementally improve the code. I think some members of Congress believe that noncontroversial reforms need to be saved for fundamental tax reform, perhaps as sweeteners. An alternative view would be that if Congress can just do any kind of meaningful reform on a bipartisan basis, which is essential, then maybe it would improve the prospects for everyone working together on something bigger.

15. ***It does nothing to restrain the growth of taxation to make paying our taxes as difficult as possible.*** There is a school of thought that says the more painful taxes are the more people will hate them, which will encourage support for tax cuts and opposition to tax increases.<sup>30</sup> This has always been the principal reason why many conservatives oppose the VAT—they fear that is too good a tax and thus will lead to a higher tax burden than would be the case if tax collection and payment is extremely burdensome. But it should be remembered that the deadweight cost of taxation—the lost production over and above the tax—is an implicit tax. So by maintaining and excessively burdensome tax system to keep the explicit tax take as low as possible, we are simply imposing higher de facto tax rates in another form.

---

<sup>29</sup> Liz Weston, “Prepare to Wait for U.S. Tax Help,” [Reuters](#) (March 2, 2013); “Observations on IRS’s Operations, Planning, and Resources,” [U.S. Government Accountability Office](#) (Feb. 27, 2015)

<sup>30</sup> Gary S. Becker and Casey B. Mulligan, “Deadweight Costs and the Size of Government,” [Journal of Law and Economics](#) (Oct. 2003).