

ISSUE BRIEF

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Tax Day 2014: How Tax Reform Would Make Filing Taxes Better

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April 15, the day Americans' tax returns for the previous year are due to the IRS, is fast approaching. Families all over the country are scrambling to find documentation for their incomes and any expenses they incurred that might be deductible, creditable, or exemptible. It is a day of consternation for most families because of the mind-numbing complexity of completing this annual task.

The best that can be said of Tax Day is that it provides a yearly reminder of just how convoluted the tax code is and how much damage it does to the economy. It should also serve as a periodic reminder that filing taxes does not have to be this way. Tax reform, if done right, would help Americans in numerous ways.

Raise Incomes. The biggest difference taxpayers would notice would be increased annual incomes. Families would see their incomes grow because tax reform would lessen the severe disincentives that the tax code currently imposes on the fundamental activities of economic growth—working, saving, investing, and taking on risk. This would allow the economy to grow stronger, which would mean more opportunities for Americans at all income levels to find higher-paying jobs and earn larger wage increases.

Done correctly, tax reform would also mean that families earn more but would not pay higher marginal tax rates on their higher earnings. The tax code would not punish families as it does today for being more successful and for earning higher compensation because they are more productive.

Simpler to File. Since tax reform would make what is taxable—i.e., the tax base—easier to define and would have at most only a few deductions and credits necessary to maintain neutrality, filing taxes annually would be immensely simpler for all families.

There would be no need for pricey software, and only those families with the most complex financial arrangements would require paid tax preparers. Highly skilled lawyers and accountants could put their considerable talents to more productive uses, which would further boost the economy.

Increased Fairness. A renewed confidence in the fairness of the system would result because of the more easily understandable tax base and minimal number of deductions and credits. Tax liabilities would be more transparent because there would be few if any ways for taxpayers with more knowledge of the tax code (or ability to pay accountants and lawyers who have it) to lower their tax liability in ways that are largely inaccessible for average taxpayers.

It would also be readily apparent that everyone was paying their fair share. Families with similar financial circumstances would be confident that they were paying similar amounts of tax. It would also be clear that higher-earning families were paying commensurately higher taxes. High earners pay almost all federal income taxes today—the top 10 percent of earners pay 71 percent¹—but because the

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tax code is so convoluted, many believe they get away with paying less than they rightfully owe.

Less Influential Government. The government would be less influential in citizens' personal decisions because taxes would no longer pick winners and losers in the market, nor would it seek to reward or punish families for making certain economic decisions.

For instance, no longer would taxes reward taxpayers who choose to purchase certain government-determined environmentally friendly products or make it relatively more appealing to provide child care outside the home. Taxes would not influence the decisions of families to have a second earner enter or stay in the workforce. Families would make these decisions based on market considerations and the unique preferences of every family.

Reduced Chances of IRS Abuse. The IRS has the almost impossible job of trying to enforce the incomprehensible tax system Congress has created. However, that does not excuse the agency for its behavior in targeting certain conservative groups for enhanced and unwarranted scrutiny. Those actions badly damaged its credibility, which is regrettable because most people who work at the IRS are hard-working and dedicated professionals who do not deserve to be tarred with the misdeeds of others.

Nevertheless, the IRS will need reform to restore its credibility. Although there will always be the need for a revenue-collecting agency, tax reform should significantly curtail the mischief in which the agency is able to engage.

The job of determining taxpayers' taxable income and whether they paid the proper amount of tax on it would be simplified, meaning the agency could significantly shrink in size. A smaller agency would lessen the chances of bad behavior. Although taxpayers would likely still have to provide some personal information to the agency, it would be far less than they have to report today, which would further reduce the ability of the agency to act improperly.

Current Efforts Increase Chances of Achieving Tax Reform. Despite these benefits that would accrue if Washington made tax reform a reality, tax reform is unlikely this year because of the one-sided nature of current efforts.

Tax reform is being led in the House of Representatives by Ways and Means Committee Chairman Dave Camp (R-MI). Camp released a thorough and detailed proposal for tax reform recently that will keep debate alive,² but he is finding little willingness to advance the cause beyond what either President Obama or the Senate is prepared to do.

Given their reluctance, Camp and the rest of the House of Representatives will have to keep making the case to the American people that we need tax reform while making clear to them the ample benefits they will experience if it becomes a reality. Those efforts will not be in vain, because the heightened visibility they create will increase the chances for passing tax reform sooner rather than later.

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1. The Heritage Foundation, "Reduce the Tax Burden," *Federal Budget in Pictures 2014*, Chart 1, <http://www.heritage.org/federalbudget/pdf/2014/top10-percent-income-earners.pdf>.

2. See Curtis S. Dubay and David R. Burton, "Chairman Camp's Tax Reform Plan Keeps Debate Alive Despite Flaws," Heritage Foundation *Backgrounder* No. 2890, March 14, 2014, <http://www.heritage.org/research/reports/2014/03/chairman-camps-tax-reform-plan-keeps-debate-alive-despite-flaws>.