

Which tax system should replace the current?

Written by Dr. Garth A. Rose

Thursday, 10 November 2011 12:15 - Last Updated Friday, 11 November 2011 12:21



The current U.S. tax system will be a pivotal issue in the [2012 presidential/general elections](#) . Some economists and candidates seeking the GOP presidential nomination suggest scrapping the current tiered payroll/income tax system; some in support of a [Fair Tax](#) (a national consumption tax) and others for a [Flat \(Income\) Tax](#)

As the debate develops, loopholes appear in this Fair Tax proposal. Fairness is doubtful if tax reform requires Americans to pay a singular tax rate on their daily consumption, including rent, beauty care, taxis, utilities and healthcare.

The rich and the poor would pay the same tax. Yet, since the wealthy "one percent" uses less of their income to buy goods and services, compared to the "[99 percent](#)" middle and lower income classes, the "one percent" would have an advantage. Some in the extreme lower-income bracket would be left worse off under this reform. Most of the lower bracket earners do not pay income tax and take home all the cash they earned. If this group pays the Fair (consumption) Tax, they would have less cash at their disposal.

Some Fair Tax supporters suggest that, as occurs in some countries such as Canada, low income citizens would periodically be refunded a portion of the Fair Tax to compensate for their additional tax expense.

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However, the complications of refunding and collecting the Fair Tax from merchants, landlords, healthcare and other service providers, weakens arguments that the Fair Tax system would abolish the massive IRS system. The system may carry another name, but would remain just as massive.

A high consumption tax, as proposed, could actually cost the government revenue. A consumption tax would chase wealthy shoppers outside the U.S., to buy in markets with lower consumption taxes. The tax would also deter tourists from shopping in the U.S. Today, because of the relatively low consumption tax in several U.S. states, shoppers from countries with a much higher consumption tax flock to the U.S., boosting the American economy.

One of the strongest arguments against the Fair Tax is the uncertainty over how the new tax would relate to current state consumption taxes. Would the tax be so high that it collects enough revenue to split between the federal and state governments, thus abolishing state taxes, or will the federal tax be charged to consumers in addition to state taxes? This has to be clarified with consumers' interest in mind. The Fair Tax has many loopholes and unanswered questions that need explanation to be fully understood.

Under the Flat Tax system, every employed American would pay the same equal percentage on their income, regardless of how much they earn. Although people would still pay an income tax, their taxations would no longer be based on various tax brackets, or be reduced by tax credits and tax breaks.

The rich would pay the same percentage on all the income they earn, as would the low income worker. New taxpayers, who are now precluded from paying income tax, would be included. Theoretically, this would increase federal revenue. The Flat Tax would also not affect the very poor; the plan eliminates taxes on the first \$10,000 earned, and in some proposals, the first \$15,000.

The key argument for the Flat Tax is that it places the tax burden on all Americans, without placing undue pressure on lower income groups.

Another strong argument is that the Flat Tax does not penalize workers for seeking advanced positions with higher incomes. Under the current tax system, if a worker gets promoted to a

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higher income position, the worker enters a new tax bracket and must pay more taxes. Under a Flat Tax, the same percentage of the income would be paid as tax.

Currently, both the Fair Tax and the Flat Tax proposals require more discussion for the public to understand the relevant implications. There is no question that the current tax system needs reform, but reform must create a fair system that appropriately taxes the "one percent," as it does the "99 percent", even if it involves a combination of both proposals.