OPPORTUNITY 08
Independent Ideas For Our Next President

Tax Policy

Fixing the Tax System
Support Fairer, Simpler and More Adequate Taxation

Background

A good tax system raises the revenues needed to finance government spending in a manner that is as simple, equitable, stable, and conducive to economic growth as possible. The challenge for the next President will be to make reform work not just in the abstract, but in the real world, where special interests often rule the roost.

In the next few years, three critical factors will push tax issues to the forefront of policy discussions. First, under current law, almost all of the Bush Administration's tax cuts will expire at the end of 2010. The loss in revenues from making the tax cuts permanent would be enormous – as would be the required spending reductions. Second, the rapid growth in the alternative minimum tax (AMT) will increase the inequity and complexity of the tax system. Third, the expected increase in government spending over the next several decades -- fueled mainly by increased entitlement spending for Medicare, Medicaid and Social Security -- will force our nation's leaders to come to terms with the need for an increase in revenues to above 20 percent of GDP.

Despite these pressures on the system, tax changes are not inevitable, and achieving meaningful reform—that is, with substantial design improvements—will require strong political leadership.

Recommendations

The U.S. tax system does not have to be as complex and unfair as it currently is. The next President should not only seek to simplify the system from the taxpayer's point of view, but also provide long-term financial resources for the government spending that the public demands. The next President should support tax reforms that:

- tax all new corporate investment income only once
- remove all corporate subsidies in the tax code and strengthen corporate anti-sheltering provisions
- integrate payroll and income taxes for individuals
- introduce return-free filing for many taxpayers

- consolidate and streamline tax subsidies for education, retirement and families
- eliminate or revise various tax deductions and
- create a value-added tax that would, eventually, raise 5 percent of GDP in revenues

Key Facts

- loss in revenues from making the Bush Administration's tax cuts permanent would be equal to several times the resources needed to repair Social Security
- the number of taxpayers facing the alternative minimum tax (AMT) is slated to grow exponentially, from about 3 million today to 30 million by 2010
- since 1950, tax revenues have hovered between 16 and 20 percent of the gross domestic product (GDP)
- government spending is projected to rise to about 27 percent of GDP by 2030

A full version of this proposal, as well as supporting background material, is available at www.opportunity08.org.

About the Author and the Project

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William G. Gale is a Brookings vice president and director of the Economic Studies Program. He also is co-director of the Urban-Brookings Tax Policy Center and director of the Retirement Security Project. Gale is an expert on tax policy, budget and fiscal policy; and public and private pensions. He served as a senior staff economist for the Council of Economic Advisers under President George H.W. Bush.

Opportunity 08 aims to help 2008 presidential candidates and the public focus on critical issues facing the nation, presenting policy ideas on a wide array of domestic and foreign policy questions. The project is committed to providing both independent policy solutions and background material on issues of concern to voters.