THE DAILY CALLER

The gloomy prospects for tax reform

By: Daniel Mitchell – April 15, 2013

Is tax reform impossible? That's a depressing topic to address on Tax Day, particularly since I've spent the past 20 years pushing for tax reform.

I hate to think that my life has been wasted, but let's consider several reasons why it's become more difficult to scrap the Internal Revenue Code and implement a simple and fair system such as the flat tax.

1. The barnacle effect — Our tax code is now a 74,000-page monstrosity, and it seems that politicians make the system more convoluted every year with new credits, deductions, exemptions, preferences, exclusions, and other special provisions.

Every new layer of complexity is akin to more barnacles on a ship, undermining performance. In theory, it makes sense to scrape off these barnacles and restore the ship, but that requires some degree of long-run thinking.

Our political system, though, is dominated by lawmakers who tend not to think past the next election cycle. That makes it difficult to convince them to undertake a big project, even if they're sympathetic to tax reform.

2. The redistribution effect — I've never agreed with the deterministic political analysis about "makers" vs "takers," but there's little doubt that a growing number of Americans now see tax returns as a vehicle for getting money from the government.

I'm not talking about the fiscal illusion that results when some people over-pay their taxes and then are happy to get a refund. Those people should get dunked in cold water until they realize it doesn't make sense to give politicians an interest-free loan.

But I'm talking about a different crowd. There are now millions of Americans who benefit from redistribution programs that are laundered through the tax code. The "earned income credit" is the best-known example. Simply stated, "refundable" credits allow people to get checks from the government even if they didn't pay any tax.

Needless to say, those people don't have much incentive to oppose the current system.

3. The corruption effect — The metropolitan DC area is now the wealthiest region of the nation; it includes 10 of America's 15 richest counties. But most of this prosperity is the result of "rent-seeking," which is a dorky term economists use to describe what happens when people use the coercive power of government to obtain unearned wealth.

One of the main sources of that unearned — and undeserved — prosperity is the tax code, which takes money from the economy's productive sector and gives it to DC-based bureaucracies.

But the real problem (at least in terms of fixing the tax code) is that Washington is a boomtown in part because so many people make big bucks manipulating the tax code. Lobbyists obviously would hate a simple and fair flat tax, but there are also pervasively corrupt segments of the economy, such as the ethanol industry, that rely on favoritism in the tax code. And you better believe those folks never wander too far from the corridors of power.

Many of these insiders are former politicians and former Capitol Hill staffers — particularly those that worked on the tax-writing committees. They make big bucks, and the current staffers look forward to the day when they can cash in on their "government service" and start "earning" huge salaries. Needless to say, these people are not exactly advocates of reform.

4. The anti-tax competition effect — Beginning with the Reagan and Thatcher tax cuts, the world experienced a virtuous period of tax competition that lasted for about 30 years. Even politicians in statist nations such as France and Germany felt compelled to lower tax rates because of fear that jobs and capital would migrate to jurisdictions with better policy. The trend was boosted by globalization.

In recent years, however, high-tax nations and left-wing international bureaucracies such as the Paris-based Organization for Economic Cooperation and Development have worked to undermine tax competition and make it easier for politicians to impose class-warfare tax policy. They first went after so-called tax havens in order to make it easier for them to track and tax flight capital.

Now the OECD has a new plan to go after multinational companies and significantly boost their tax burdens, presumably through the creation of a global tax return and a policy called "formula apportionment." This system would cripple corporate tax competition and reverse the positive trend to lower corporate tax rates.

The Obama administration, unsurprisingly, has been working with Europe's decrepit welfare states in favor of these misguided policies. And every time they make progress, politicians feel less pressure to lower tax rates and reform tax systems. Why bother improving the tax code, after all, if you think that taxpayers have no choice but to submit?

So what's the takeaway from this depressing list? Well, the answer to my question almost surely is yes. It's more difficult than ever to reform our tax system.

But that's not an argument for capitulation. It's simply sober-minded analysis.

To close on a positive note, the fact that we now face more obstacles to tax reform means that the benefits of tax reform are even larger.