



Harris Sherline: Random Facts About America's Income-Tax Laws

By Harris Sherline, May 11, 2013

It's time to reflect once again on the annual ritual of self-flagellation that Americans are forced to endure each year. The income tax deadlines have become a sort of rite of passage for citizenship, although as things stand today almost half of all workers don't pay any income tax at all.

Following are some random facts (in no particular order) about our income tax laws, who pays and who doesn't, and the impacts our system of taxation has on the nation's productivity:

When the 16th Amendment to the Constitution established the federal income tax in 1913, the intent was to tax only the very rich. Rates began at 1 percent and increased to 7 percent for taxpayers with income in excess of \$500,000 (\$11,756,212 in today's dollars), or 2,251 percent inflation.

Less than 1 percent of the population paid any income tax at all, compared with almost 50 percent of taxpayers paying as much as 35 percent of their taxable income today.

The top 1 percent of wage earners pay almost 39 percent of total individual income taxes, while the top 25 percent pay about 86 percent, and the top 50 percent pay approximately 97 percent. Translation: Just half of all taxpayers pay almost 100 percent (96.93 percent) of all income taxes, while almost 50 percent pay no income taxes at all.

The Internal Revenue Service has more than 95,000 employees (FTEs or full-time equivalents) and a total budget of \$13.3 billion, up from \$12.2 billion in 2010.

Estimates of unreported commercial activity in the United States amount to as much as \$1 trillion a year, and the IRS Oversight Board report for fiscal 2007 notes that the tax gap, “the difference between what is owed and what is collected ... is estimated at \$345 billion of lost revenue annually.” Question: If it’s an underground economy, how does the IRS know how much income is not reported?

The Cato Institute reported that businesses and individuals now waste more than 6.6 billion hours on federal tax compliance activities each year, which the Tax Foundation estimated amounted to \$265.1 billion in 2005. That’s equivalent to more than 3 million people working full time, just to deal with tax compliance. This amounted to a 22 percent tax compliance surcharge on the total amount collected through the tax system.

The Gettysburg Address is 269 words, the Declaration of Independence is 1,337 words, and the Holy Bible is 773,000 words. The tax law has grown to more than 7 million words today from 11,400 words in 1913 (Tax Lawyer’s Blog, 10 Interesting Tax Facts). Our tax laws have become so complex and contradictory that no one, not even the most brilliant tax professionals, including IRS experts, fully understand them.

There are at least 480 tax forms, each with many pages of instructions. Even the easiest form, 1040EZ, has 33 pages of instructions.

The IRS sends out 8 billion pages of forms and instructions each year. Laid end to end, they would circle the globe 28 times; 300,000 trees must be cut down every year to produce enough paper for all the IRS forms and instructions.

When General Electric Co. filed the corporation’s tax return electronically, it took 24,000 pages to document. The Associated Press (June 1, 2006) noted, “If GE had sent paper forms, the return would have stacked up 8 feet high.”

In 1993, the General Accounting Office audited the IRS for the first time in its history and found widespread evidence of financial malfeasance and gross negligence, including the fact that the agency was not able to account for 64 percent of its congressional appropriation.

The Alternative Minimum Tax (AMT) “was created in 1969 to target 21 — yes, 21 — millionaires who had managed to avoid paying any taxes at all” (The Wall Street Journal, April 14, 2007). “This year more than 3 million taxpayers will be hit by the Alternative Minimum Tax on the(ir) 2006 income. But next

year (2007) that number could have increased to 23 million" Note: It didn't, only because Congress passed a so-called "patch" to prevent it.

The federal income tax, currently as high as 35 percent of taxable income, is increased by as much as 9.3 percent in California income taxes, plus another 6.2 percent and 1.45 percent in Social Security and Medicare taxes, which makes the total tax burden for some taxpayers almost 52 percent, not including excise, sales and property taxes, along with a host of other taxes, assessments and fees to numerous to mention. In 2010, more than 141 million individual income tax returns and 2.3 million corporate income tax returns were filed.

Households in the lowest 20 percent of income received about \$8.21 in federal, state and local government spending for every dollar of taxes paid (in 2004), while those in the top 20 percent received only 41 cents in benefits (Tax Foundation Working Paper No. 1, March 2007).

It's worth noting, I think, that when I started practicing public accounting in the early 1960s, the filing deadline was March 15, not April 15, and only one 90-day extension was permitted. Today, the due date for filing is April 15, and it is possible to obtain a six-month extension — to Oct. 15 — primarily because of the increased difficulty of obtaining the necessary information and the complexity of preparing and filing tax returns.

Many societies view taxation as a contest between tax collectors and citizens, with payment or avoiding payment of taxes as the prize. But we are different we are told, because Americans voluntarily, that is, willingly, file tax returns and pay their taxes. Baloney! If that's true, why do we hear so much about taxes not being paid by people who work or do business in the "underground economy"? Would you file a tax return if you were not afraid of the consequences of not filing?

Putting aside the government's hype and PR initiatives, the reason our income tax system is so successful is fear — fear of being audited, fear of being assessed, fear of tactics employed to collect unpaid taxes, fear of intrusion into our personal affairs, fear of not being able to defend ourselves against the unlimited power of government in general and the IRS in particular.

I believe the IRS has carefully cultivated this image over a period of many years. Who can say that they don't have a sudden, albeit perhaps brief, fearful reaction when they find a letter or notice from the IRS in their mail? I know I do, and I'm a retired CPA. I don't want to hear from them — ever! When I do get some sort of communication from my friendly tax agency (federal or state), I just know it's going to cost me time, money and aggravation. Perhaps you've noticed over the years that around tax time it's common

to see a spate of media stories about delinquent taxpayers. In my opinion, that's no accident. Case in point is an April 14 Sacramento Bee article about the Franchise Tax Board releasing its annual list of delinquent taxpayers, which adds up to more than \$193 million.

One of President Ronald Reagan's many sage observations sums up the situation rather neatly: "The taxpayer: That's someone who works for the federal government but doesn't have to take the civil service examination."

For my part, I believe Americans are overtaxed and underserved by our government, while our politicians are constantly looking for ways to impose new taxes under the radar of public scrutiny and awareness. Will it ever end? Probably not, until we have allowed ourselves to be taxed into near or complete oblivion.