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Herman Cain's VAT

By Jennifer Rubin

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In addition to concerns about regressivity and the introduction of a national sales tax, Herman Cain's tax plan suffers from a fatal flaw, many fiscal conservatives argue. The Cato Institute's Dan Mitchell explains:

Josh Barro and Bruce Bartlett are both claiming that the business portion of Cain's 9-9-9 is a value-added tax (VAT) rather than a corporate income tax.
In other words, instead of being a 9 percent flat tax-9 percent sales tax-9 percent corporate tax, Cain's plan is a 9 percent flat tax-9 percent sales tax-9 percent VAT.

Let's elaborate. The business portion of Cain's plan apparently does not allow employers to deduct wages and salaries, which means — for all intents and purposes — that they would levy a 9 percent withholding tax on employee compensation. And that would be in addition to the 9 percent they presumably would withhold for the flat tax portion of Cain's plan.

Employers use withholding in the current system, of course, but at least taxpayers are given credit for all that withheld tax when filling out their 1040 tax forms. Under Cain's 9-9-9 plan, however, employees would only get credit for monies withheld for the flat tax.

In other words, there are two income taxes in Cain's plan — the 9 percent flat tax and the hidden 9 percent income tax that is part of the VAT (this hidden income tax on wages and salaries, by the way, is a defining feature of a VAT).

This seems to me to be the critical weakness in the plan that subsumes any benefits it may offer. It renders the plan decidedly nontransparent. It makes clear that the rate is not 9 percent for individual taxpayers but 18 percent plus a 9 percent sales tax.

Mitchell's 2009 video on the unsavory aspects of the VAT tax is well worth a look. What is interesting is that, far from being an anti-Washington tax scheme, Cain's 9-9-9 plan resuscitates one of the worst, old ideas floating around European capitals and Washington. Moreover, it repeats one of the central flaws of past VAT schemes; it doesn't replace the income tax code, it adds another new tax and revenue stream. He also (at approximately at 5:40) explains why a VAT does not make us more "competitive" or help exports. It is a devastating critique.