



Forget Tax Reform — Try a Flat-Tax Revolution

David Yeliang Xia

February 8, 2017

Americans now have fewer than 70 days to file their federal income taxes, and for many taxpayers, this year's filings will likely be as costly and complicated as ever. Yet with Donald Trump now the nation's 45th president, future filings may become a lot simpler. After all, the president promises "across-the-board income tax reduction, especially for middle-income Americans."

High taxes and the endless complexity in the Internal Revenue Service code are truly problems, but the solution calls for far more than the just tax reduction Trump envisions. Instead, Americans deserve a tax revolution — the kind only a flat tax can provide.

What does a true flat tax look like? I propose cutting individual income taxation to 15 percent for taxpayers with incomes above \$232,425, and 7 percent for those with annual incomes below that but higher than \$40,000. That's a far cry from the 33 percent an individual filer making over \$250,000 now pays, or the 39.6 percent a married couple filing jointly would have to pay on the same level of income. It's also an improvement on the 25 percent rate that a single filer making \$40,000 now pays.

And for those concerned that flat taxes might be regressive — meaning falling more heavily on those with lower incomes — under my proposal those with incomes lower than \$40,000 would pay no federal income tax at all. Citizens or permanent residents with incomes below \$30,000 could still expect subsidies or grants from the federal and state government, respectively.

The flat tax would also apply to businesses. Under a flat tax as I propose, corporate taxation could be reduced to 12 percent — drastically lower than the 35 percent corporate tax that a typical mid-sized business now pays. This would make the United States substantially more attractive for investment from countries with emerging markets, also encouraging U.S. firms overseas or joint ventures to withdraw their business back to the United States.

This new set of reduced rates would put thousands or even tens of thousands of dollars back in taxpayers' pockets — particularly those from the middle class.

The flat tax would also mean an end to the many loopholes and deductions currently in the IRS code. Instead, taxpayers would benefit from a system where what they see is what they get. Every tax bracket would come with a fixed, stable rate, making it far easier to determine what you owe each April.

This drastic simplification would also go a long way toward more effectively funding the government. Current tax law slows economic growth. It distorts economic incentives, doing more to encourage tax avoidance or create tax shelters than anything else. A more transparent flat tax would eliminate many of those negative incentives. The elimination of loopholes and deductions would help ensure government revenue remains stable, even with reduced nominal rates.

Experience from other parts of the world shows how these simpler rates can help boost an economy. More than three dozen countries have implemented a flat tax system. Hong Kong has had a flat tax for decades, with a maximum rate 15 percent for all residents, and Russia has had a flat tax of 13 percent since 2001. Belarus has a 12 percent flat tax, Bolivia's flat tax is 13 percent, and Hungary's is 15 percent, to name just a few.

In particular, Hong Kong's success under a flat tax system needs little introduction. Its simple and low tax rate made Hong Kong one of the world's most attractive places to work, invest and live.

Trump isn't the first politician to advocate a fundamental reform of the tax code. When current California Gov. Jerry Brown ran for president in 1992, his platform included a proposed 13 percent flat tax for personal income taxes and business taxes. Republican presidential candidate Steve Forbes proposed a similar plan in 1996. More recently, Republican presidential candidate and Texas Sen. Ted Cruz proposed a 10 percent flat tax for individuals and a 16 percent flat tax for businesses.

Whereas most of these earlier initiatives went nowhere, Trump and a Republican-controlled Congress mean that a flat tax such as I propose now has a chance of becoming reality.

Ultimately, a flat tax would be a huge economic boost. Consumers and investors would have more money in their pockets, while investors would have even more incentive to invest in businesses or non-profit ventures. And no Americans would have to spend considerable time and resources on tax avoidance, freeing up an incredible amount of wealth and capital.

My flat-tax proposal — or any other efforts to move toward flat tax reform — would mean an end to everything that most Americans hate about tax season. All Americans — rich, middle-class, or poor — would benefit from lower, simpler tax filings. And that's nothing short of a revolution.

Xia Yeliang is a visiting fellow at the Cato Institute's Center for Global Liberty and Prosperity. His work focuses on the institutional and policy reforms China must make to become a modern, free society. His research interests include economic history, institutional economics, and macro-economic and other public policy.