NATIONAL REVIEW

Is the Border-Adjustment Tax Really Dead?

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That's what *Roll Call* asserted on Tuesday:

House Republican leaders' controversial border adjustment tax is dead

So did the *New York Times* a few weeks ago:

After months on life support, the border adjustment tax looks as if it's finally dead.

Unfortunately, I am not sure it is dead enough.

First, bad ideas, like government programs, never quite die in Washington. They resurface regularly and I expect this one to be no different. This is particularly true in this case since the Republicans and many of their allies seem to have accepted, or at least internalized, the idea that spending cuts and entitlement reforms may never happen. If that's the case, they think we need to raise revenue to cut taxes so to simply make ends meet.

How else can we explain the refusal by House Ways and Means chairman Kevin Brady, Speaker Paul Ryan, and others to push for spending cuts as a way to pay for some of the revenue losses? How else can we explain their insistence that a very problematic destination-based border-adjustment tax (BAT) is the only way to alleviate the revenue gap created by the proposed tax reform? Because, that's really the true argument for the BAT: Without the BAT, no overhaul of the tax system. Even the *New York Times* and *Roll Call* have been writing their stories linking the demise of the BAT to the end of any hope for fundamental reform. Chairman Brady even noted after a hearing on the subject, "If someone has a better solution, bring it."

It's unfortunate. The insistence that the BAT is the only answer to tax reform showcased by the House GOP leadership has prevented the free-market movement, broadly defined, from uniting behind the fight for tax reform. It also ignores that there is growing evidence that the BAT will probably not raise as much revenue as expected. This study published in May by PERC is interesting in that regard.

In addition, this argument failed to recognize that cutting the corporate tax rate and other features of the tax plan would boost revenues more than the score of the House GOP Blueprint has given them credit for. One reason is that it ignores that cutting the corporate-tax rate would, in and of itself, reduce tax avoidance and hence increase the amount of reported and taxable income. The

Cato Institute's Alan Reynolds has a really good post on this, here. The good news is that we need not implement a BAT and undermine tax competition to reduce tax avoidance.

The other reason why I am not sure the BAT is dead completely is that there are some discussions about "phasing-in" the tax. During the hearing a few weeks ago, Larry Lindsey called for implementing a smaller import tax to get people used to the idea. Chairman Brady and some of his allies have also made the case that a gradual phase-in would be the way to go.

That's not a good idea. First, half of a bad policy is still a bad policy. More importantly, phasing-in the BAT means that currencies will not adjust quickly and totally — opening the door for some serious distortions. Also, as AEI's Stan A. Veuger explained to me:

The big problem I see with a gradual phase-in is that that would lead to a predictable appreciation of the dollar. This would trigger arbitrage-induced preemptive appreciation, which would harm US exporters (as they now face lower prices abroad without receiving the border adjustment subsidy yet). To avoid this, I suppose you could make the phase-in so slow that that trade becomes unattractive, but then you lose all the revenue.

As I said, half of a bad policy is still bad policy!

That's why we need to move on entirely and find alternatives. They exist believe me. Here is a paper, for example, by Adam Michel and Romina Boccia on how to do it. It involves good principles of tax reform and spending cuts.