

rate in a globalized world with mobile capital. The United Kingdom, for example, has dropped its patent box tax rate to 10 percent, but some companies can find an even lower patent box tax rate in the Netherlands, he said.

"To the extent you're taxing capital, you cannot get away from this, you'll never get away from it," Goulder said. "That's why you see these trends that are going on in the world."

### Need for Revenue

One of the key considerations in a possible tax reform effort and for the future of the income tax is whether the code should raise more revenue than it does, unlike the revenue-neutral Tax Reform Act of 1986.

The 1986 law offset reduced marginal rates for individuals with increased corporate taxes, Columbia Law School professor Michael J. Graetz said. In 1986 there was a "pot of gold to finance rate cuts, and there is no pot of gold today," he added. Jared Bernstein, senior fellow at the Center on Budget and Policy Priorities, argued that the United States needs revenue greater than its historical average of 18 percent of GDP. Focusing on the psychology of taxpayers, Bernstein suggested that a way to gain greater support for tax reform that raises revenue would be to tie taxes more directly to the programs they fund, for example with dedicated infrastructure or health-care taxes.

"If people are disconnected between what they're willing to pay for and what they get, our tax system can't survive," Bernstein said.

Thorndike argued that President Obama, by focusing on tax increases for a narrow sliver of the population, has given the U.S. public only "20 percent of an affirmative case" for higher revenue overall. "I think you squander your opportunity when you spend a lot of time raising taxes a little bit on very rich people," he said.

The current income tax system cannot supply all the needed additional revenue, Graetz said. "I think we're going to need something higher than the historical average of revenue," he said. "Is it 20 [percent of GDP]? Is it 21? I don't know, but you are putting a huge amount of pressure on the income tax if you are going to rely only on the income tax or mostly on the income tax and payroll taxes to produce that much revenue." In his book *100 Million Unnecessary Returns: A Simple, Fair, and Competitive Tax Plan for the United States*, Graetz suggests adding a VAT to a reworked individual income tax system, using revenue from the VAT to exempt joint filers making

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## OTHER NEWS

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### Panelists Urge Congress to Seek Alternative to Income Tax

Lawmakers should consider a revenue source apart from the current income tax to pay for the cost of government, panelists said at a February 22 Tax Analysts forum. Christopher E. Bergin, president and publisher of Tax Analysts, moderated the panel discussion on whether the federal income tax, which celebrates its 100th birthday this month, can retain its role as a prime source of federal revenue. The current income tax system, which became possible only with the ratification of the 16th Amendment, developed when broad-based state-level property taxes grew increasingly impractical, according to Joseph J. Thorndike, director of the Tax History Project at Tax Analysts. "As the financial world got more complicated, it became harder and harder to tax all forms of property because a lot of it was invisible," Thorndike said. (Forum transcript, Dec 2013-4310.)

The original income tax was set at 7 percent with an exemption set at \$100,000 in today's dollars and was intended to be a "light tax applied to just a handful of people," Thorndike said.

Whether the income tax is now failing and should be replaced, just as it replaced state-level property taxes, is open to debate, Thorndike said. "What seems more likely to me is that the income tax may have to share the stage fairly soon," just as the old property tax system overlapped with the income tax before slowly fading away, he said. Robert Goulder, editor in chief of Tax Analysts' international publications, argued that the income tax deters capital formation and makes it difficult to maintain a competitive corporate tax

less than \$100,000 (\$50,000 for single filers) from the income tax, and using payroll adjustments rather than an earned income tax credit. Graetz cited a 2012 report (*Doc 2012-1581*) from the Urban-Brookings Tax Policy Center and the Pew Charitable Trusts that said his plan would require a VAT rate of 12.3 percent to pay for the proposed exemption and would allow more than 100 million taxpayers to avoid filing a tax return.

Mortimer Caplin, who served as IRS commissioner during the John F. Kennedy administration, argued instead that every taxpayer should fill out a tax return as “part of the price of citizenship.” He agreed, however, that the United States may have to adopt a VAT and cited a 1961 speech in which Kennedy argued that a “strong tax system is essential to a strong democracy.”

“The Internal Revenue Service at that time had a different function,” Caplin said. “A lot of it was really selling to the American public the importance of compliance with our tax laws.”

### Carbon Taxes

A carbon tax could raise revenue in addition to the income tax, but Graetz urged lawmakers to consider a carbon tax only in the context of energy policy, not as a potential source of revenue. Given the regressive nature of the tax and proposals for refunds to lower- and middle-income earners, a carbon tax would generate less revenue than expected, he said.

“I think there is much less revenue for general purposes or for earmarking or whatever you want to do in a carbon tax than there is in a much broader-based consumption tax,” Graetz said.

Goulder agreed, saying that a carbon tax “shouldn’t even be about the revenue; it should be about capturing the externality.”

### Partisanship and Tax Reform

The panel agreed that the future of tax reform remains uncertain, pointing to the current inability of lawmakers to work across the aisle.

“We’re never going to get real tax reform — the kind of tax reform that solves big problems rather than little, small problems — we’re never going to get that until we restore this faith in government, whatever that takes,” Thorndike said.

House Ways and Means Committee Chair Dave Camp, R-Mich., released a discussion draft (*Doc 2011-22576*) on how the United States can adopt a territorial system of taxation and a separate draft (*Doc 2013-1731*) on the taxation of financial products. Camp and Ways and Means ranking minority member Sander M. Levin,

D-Mich., have announced a set of bipartisan working groups on tax reform, while Senate Finance Committee Chair Max Baucus, D-Mont., is working on a set of white papers on tax reform. Graetz suggested that Camp’s and Baucus’s work will serve as a “gap filler,” because the White House and Treasury Department haven’t engaged much in the tax reform debate. (Prior coverage, *Doc 2013-3390*.)

— Meg Shreve