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Not a Flat Tax

THE FLAT tax is a flawed idea, less a serious tax proposal than a slogan in the name of which the advocates claim to be able to accomplish several contradictory things at once. They can't, of course, which is why the tax has become a source of quarrels within the Republican Party. It's also why the latest report on the tax commissioned by Senate Majority Leader Bob Dole and House Speaker Newt Gingrich was necessarily so vague.

A principal goal of flat-taxers is to reduce the tax on investment income. The rationale is that the gentler tax treatment will lead to increased savings, investment and economic growth from which everyone will benefit. It's a laudable goal and in some respects a credible notion, though the effect of the tax code on such fundamental forms of economic behavior as savings and investment tends almost always to be less than tax advocates would have you think.

The problem is that cutting taxes on investment income has some awkward side effects. The first is that the principal beneficiaries—the immediate beneficiaries, at any rate—are going to be people at the high end of the income scale, since they are by definition the ones with the most extra money to invest. But few politicians want to be perceived as giving a tax cut mainly to the rich in an era of rising income inequality, and many flat-taxers, though not all, say they remain committed to the principle of progressive taxation. That's what the commission said. How do you square the two?

The second side effect is that, unless you believe in the tax fairy, cutting taxes means the government will have less revenue to cover its costs. Certainly that's true in the short run if not, as some argue, in the longer term—and here we have the Republicans especially pushing for a balanced budget. If you want

to balance the budget while lowering some people's taxes, whose are you going to raise, or is there some other way out of the problem?

The commission proposed to deal with the first of these issues by raising the tax threshold, the income level at which people would begin to owe taxes. Depending on where the threshold was set, that could indeed make the tax system more progressive at lower income levels; lower-income people, too, could see their taxes cut. But that only compounds the problem of who then pays. Do middle-income people, somehow defined, see their taxes go up? The flat-taxers say that won't be necessary, because government spending can be further cut and anyway their proposed tax changes will lead to a great deal of growth. "The transition will help to pay for itself," the commission said. But haven't we heard that before?

The advocates also say that a flat tax will lead simultaneously to greater simplicity and "fairness" in the system, a fair system being defined in part as one that treats everyone and every dollar of taxable income the same. But one of the reasons the tax code is so complicated is that it isn't necessarily fair to treat every dollar the same. Two people with similar incomes may be in very different circumstances; one may have very high medical bills, for example. Should the tax code take that into account? Do we keep the mortgage interest and charitable deductions or junk them? The advocates—and the Republican presidential candidates—disagree.

We have no doubt that the tax system can be improved. A flat tax wouldn't be an improvement. It wouldn't really be flat, just tilted in a different way than is the current code. They need to take this one back to the drawing board.