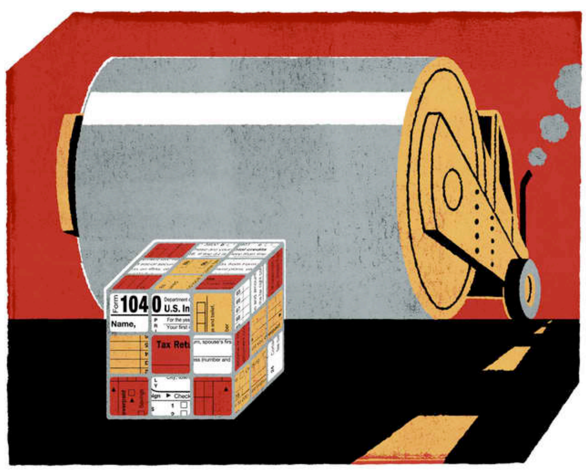
The New York Times

November 6, 2011

The Problem With Flat-Tax Fever

By ROBERT H. FRANK

CLOSE watchers of presidential politics weren't surprised to see many of this year's Republican hopefuls proposing to replace the nation's progressive income tax with a flat tax. Such plans reliably surface every four years, and, just as reliably, sink without a trace.



That's not because the current tax system is far from the abominable tangle of complexity that candidates say it is. Actually, it's worse. Flat-tax proponents promise to sweep away that mess by imposing a single levy on every dollar earned. That change, many contend, would allow taxpayers to file their returns on postcards. And surveys suggest positive voter responses to several of the most recent proposals.

Yet none will be adopted, for at least two reasons. One is that a flat tax would do nothing to make filing tax returns any simpler. But, more important, it would greatly exacerbate longstanding growth in income inequality.

One Republican candidate, Herman Cain, enjoyed widespread attention when he unveiled his “9-9-9” plan last month. The plan, as he described it, calls for three simple taxes, each with a 9 percent rate. The first is a tax on income, and the second, on goods bought, is essentially a sales tax. The third taxes business revenue. But because it deducts paid dividends and other nonlabor expenses, it amounts to a tax on wages.

Mr. Cain touted his plan’s simplicity, and many voters were apparently impressed. In some surveys of potential Republican primary voters, he quickly captured the top spot held until then by Mitt Romney. Rick Perry, the Texas governor, responded with a flat-tax proposal of his own. At this point, Mr. Romney is the only top-tier Republican candidate without some variant of a flat-tax proposal. But give him time.

The contention that a flat tax would be simpler because it involves only a single rate is flatly wrong. The complexity of the current system has nothing to do with its multiple income brackets.

The hard step in figuring your tax bill is to compute your taxable income — roughly, the amount you earn, less the myriad exemptions, deductions and various other offsets described in the 3.4-million-word code of the Internal Revenue Service. You'd also have to calculate your adjusted gross income under a flat tax. But once you've completed that step under either system, you consult the tax tables to see how much you owe. In the current system, the entries have multiple brackets and rates already built into them, so this step is no harder than it would be under the tables for a flat tax.

The much more serious concern is that a flat tax would reinforce the trends toward greater income inequality that have been seen over the last several decades. As documented by a recent Congressional Budget Office study, the top 1 percent of income recipients in the United States earned 275 percent more in 2007 than they did in 1979, adjusted for inflation, a period when the earnings of middle-income households grew by less than 40 percent. A flat tax would increase inequality by substantially reducing rates on the most prosperous households, while increasing them on low- and middle-income households.

According to an analysis by the nonpartisan Tax Policy

Center, Mr. Cain's proposal would increase the annual tax bill of a typical family of four earning $50,000 a year by more than $4,000, but would reduce the taxes owed by a similar family earning between $500,000 and $1 million by almost $60,000. The center also estimated that families in the top one-tenth of 1 percent of households would enjoy an average annual tax reduction of nearly $1.4 million under the Cain plan. Similar distributional effects are common under all flat-tax plans, not just Mr. Cain's.

Rising inequality exacts a toll not just on those with lower incomes, but also on those much higher up the income scale. In their 2009 book, "The Spirit Level: Why Greater Equality Makes Societies Stronger," the British public health researchers Richard Wilkinson and Kate Pickett document a range of social ills that are reliably associated with increased income inequality, both over time within nations and at any particular moment across a broad range of countries. Countries and times with lower inequality fare better on virtually every published index of health, well-being and quality of life.

Those with the highest levels of inequality, like the United States, invariably score poorly on these indexes. And those same countries consistently experience higher rates of violent crime.

TO say that flat-tax proposals are problematic isn't to deny that our current tax system is profoundly dysfunctional. Every year, corporate lobbyists and other supplicants use campaign contributions and other inducements to persuade legislators to enact additional exemptions, deductions and other loopholes. Voters are justifiably angered by having to wade through this complexity, or by having to hire one of the nation's 1.2 million professional tax preparers to do so.

Although a flat tax won't be adopted, taxing consumption is actually a good idea. We should replace the progressive income tax with a simplified and much more steeply progressive tax on each household's annual consumption expenditure — calculated as the difference between its income and its annual savings. But because half of the members of the Congressional "supercommittee" entrusted with cutting the deficit have pledged never to approve any new tax under any circumstances, that won't happen any time soon.

For the time being, then, our best bet is to do all we can to reduce the gratuitous complexity of our progressive income tax.

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