

Tax Reform: The Broad Picture

THE EXISTING FEDERAL TAX SYSTEM is basically on the surplus or net income that is realized as individuals and businesses sell the goods and services over which they have control. In the case of the individual income tax the deductions to arrive at the tax base have lost any relationship they ever had to a cost figure that could be used to calculate net income. The corporate income tax has stayed much closer to the fundamental relationship of the tax, *i.e.*, that it is a tax on profits. But here also the tax has wandered far afield from its original theoretical character. Finally, the gift and estate taxes have proved to be a tax concept only justified because of failure of income taxes to reach all net incomes. They possess many weaknesses of their own, both of the administrative and conceptual kind.

The elimination of these taxes at the federal level is called for because of the evolution that has taken place in both the taxes themselves and in the economic environment in which the taxes function. Their abandonment would leave the federal government short someplace between \$350 and \$400 billion which would have to be made up with new taxes. The new taxes, to avoid stimulating inefficiency and retarding private savings as the existing fiscal system tends to do, would have to be very broad-based so that the rates could be low while providing substantial and stable revenues. The two tax bases fitting these requirements rather well, while also being balanced between wealth and consumption, are net wealth and the sale of value added as goods or services.

Two taxes resting on these bases and utilizing rather well the procedures developed for these taxes in other countries would provide the revenues lost through repeal of federal income taxes and the federal gift and estate tax. Therefore, the potential exists to shift the federal general tax system to a net wealth tax possessing a high ability-to-pay characteristic and a value added tax assessed as productivity is marketed.

At the same time as the major federal tax reform was being carried out that would shift the federal tax system away from retarding and inefficient impacts, the state and local government tax systems would be encouraged to improve the ability-to-pay characteristics of their revenue systems. State government reliance on income and land taxes would most likely increase. State income taxes would expand because they had been given up by the federal government. State land taxes would be initiated because land is likely to be excluded from the federal net wealth tax for constitutional reasons. A state land tax—which would be a reform of the present real property tax—would appear to be an innovation that would increase the justice of the manner in which the nation's tax system functions.

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