

A Proposal for Rational & Equitable Tax Reform

A Citizen's 2% Solution:

How to Repeal Investment Income Taxes, Avoid a Value-Added Tax, and still Balance the Budget

In brief, my premise is quite straightforward.

1. Our Current Federal Tax System is Broken.
2. Our Progressive Tax Structure is a Myth.
3. The Social Security Trust Fund is a figment of our imaginations.
4. The Marginal Federal Tax Burden on the Working Middle Class is twice as high as that which is imposed upon their more affluent neighbors.

Many claim that America's great tax challenge is a "lack of will" to increase taxes enough to pay for our required services, but I think the problem is more severe than that. I think we are dealing with a fundamentally "corrupt process" in which the entire discussion of taxes has become intellectually dishonest as we insist upon trying to redistribute Other People's Money to achieve the goals of special interest groups.

We lie to ourselves and pretend we have a progressive tax system while the working middle class pays higher marginal tax rates than the very wealthy. We use the fiction of a Social Security Trust Fund to impose hidden, higher taxes upon the poor and middle class, which more than offset the progressive elements of our Federal Income Tax schedules (which comprise only 20% of the overall national/state/local tax burden). Our Political Class, both on the Right and the Left, combine these fictions with Structural Budget Deficits to conspire to shield the wealthy from even a nominal tax assessment upon accumulated assets.

Our federal government has crafted a remarkably Byzantine structure of incentives and preferences; taxing revenues differently based upon their varying source and magnitude, pretending employment taxes aren't really a part of the general revenues, using exclusions, deductions, multiple rate schedules, alternative minimum calculations, surcharges, phantom trust accounting, etc., etc. etc., ad infinitum, all apparently designed to provide politicians tools with which to fractionalize and bribe their constituents and reward their campaign contributors. It appears designed to ensure that no two citizens receive equal treatment.

I flatly reject the idea of imposing a Value Added Tax, or energy tax, or beverage tax, or any of the recently proposed add-on revenue fixes on top of the existing jury-rigged, dysfunctional mishmash we currently utilize. Every one of these regressive bolt-on options is guaranteed to make things worse

instead of better, increasing burdens upon the portion of the population least able to carry them and becoming an additional obstacle to economic growth.

Nor is it reasonable to think can we improve the situation by ratcheting up the “progressive” rate schedule or imposing a “millionaire’s income tax surcharge”. Experience has repeatedly reinforced the lesson that higher progressive rates applied to our current income tax structure are counter-productive because they discourage investment, retard growth and stimulate tax avoidance efforts. The wealthy will find a way to avoid them and they will fall crushingly upon the backs of the working middle class.

Unless we fundamentally reform the structure and process of taxation in America, I see no possibility of closing our budget gap or bringing responsible leadership back to our fiscal policy. It is with this perspective that I propose the following:

We should combine and simplify our existing employment and income taxes into a single two-tiered income tax and supplement it with an annual 2% Tax on Net Assets.

If we eliminate the crazy-quilt rat’s-nest of deductions and exclusions used to conduct the shell game of tax deception and make revenue collection subject to equal treatment we can reform our existing Federal Income Tax program to be far simpler and fairer.

We should be honest about Social Security taxes; quit pretending there’s a Trust Fund and hiding behind that pretense to make the working middle class bear a higher tax rate than the wealthy. We should maintain the existing roughly 15% tax burden from the first dollar of employment earnings but stop the fiction of pretending it’s a Social Security / Medicare Contribution and acknowledge that it is simply a part of the general income tax. [Note that I do not propose here any changes in the social security benefits programs – but simply demand honesty relative to the revenue sources.]

We should then add a 10% to 15% step-up somewhere in the vicinity of the existing \$34,000 earnings threshold and make the resulting 25% to 30% maximum tax rate applicable to all employment earnings. If all exclusions and deductions (except exemptions for dependents) are removed from the tax code there is no reason why this two-tier tax structure shouldn’t replace all existing Federal Income Tax revenue while reducing maximum marginal earned income tax rates (inclusive of what are now defined as employment taxes) to this 25%-30% maximum threshold. This is a modified “Flat Tax” proposal, but it is done in two tiers and absorbs existing employment taxes into its 25%-30% maximum rate.

Corporate income taxes, personal investment income taxes, estate and inheritance taxes and gift taxes should all be *repealed* and replaced with an annual 2% tax on net assets (subject to a standard base deduction of perhaps \$250,000).

Existing investment income taxes are an obstacle to productive redeployment of capital; they retard growth, stimulate tax avoidance efforts and should be repealed. They should be replaced by a nominal 2% tax upon individual net worth in excess of a standard deduction. The wealthy privileged elite of our

society neither need nor deserve the tax advantages they currently receive which allow them to enjoy perpetual tax-free appreciation of “unrealized gains”. Today, the man who simply holds his accumulating wealth (the lucky soul already at the top of the pile for whom it is excess income, unnecessary to sustain his day to day existence) receives a 100% tax discount versus his less fortunate peers.

A man of wealth and a man of labor both receive benefits from society. If a man labors and generates income, but has no wealth, he still is taxed – though his expenses may consume his income leaving him limited ability to pay. If another man has wealth, even great wealth, but manages it to avoid reporting income, he is currently shielded from taxes – even if he has a far greater ability to pay. Where is the right and wrong in this disparate treatment? Do the benefits and protections of society not provide equal or greater value to the man of wealth as to the laborer? I believe our tax policies need to be structurally modified to reflect a more equitable distribution of the costs of our society.

Should we expect the wealthy to willingly agree to increase their contribution to support society? Perhaps we should. But we needn’t rely upon their magnanimous generosity because their personal self-interest would also be served:

The long term cost of inflation created by our systemic deficit spending exceeds the cost of a 2% asset tax that could balance the budget.



The preceding is a brief summary of the core premise and proposal presented in *A Citizen’s 2% Solution*. It is my self-assigned civics project, triggered by a belief that our Federal Budget policies are, in the words of the Congressional Budget Office, on “An Unsustainable Path”. I urge you to please help make this proposal the subject of an Open Public Dialogue.

Congress has just initiated the largest expansion of government in the nation’s history. How are we going to pay for it?

A very large portion of our population argues against their own principles of equal treatment as well as their personal self interest because the debate on tax reform is framed by the patently false allegation that “nearly 50% of the population pays no taxes”, an allegation that is only true if we pretend that employment taxes aren’t taxes.

I believe rational and equitable tax reform is the greatest challenge of our generation. My intention in drafting this book has been to illuminate the issues and challenges and trigger a broad discussion of this important topic. I believe the analysis and proposal set forth deserves a fair reading and critical comment and reaction as part of the important debate upon potential reform alternatives.

Respectfully,
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A Citizen's 2% Solution

A Confluence of Benefits

ECONOMIC GROWTH

- Repealing corporate income taxes will stimulate business hiring and make U.S. corporations more competitive
- Flattening and reducing earned income taxes will stimulate growth in middle class disposable income and thus consumer demand
- Removing the tax bias toward unrealized gains will stimulate more fluid and productive reallocations of private capital

EQUAL TREATMENT

- Proposal normalizes effective tax rates between earned income and investment returns
- Avoids regressive VAT or consumption taxes
- Eliminates “double taxation” of corporate income and dividends/capital gains
- Eliminates preferential treatment of the already privileged
- Replaces the “pretence of progressivity” as depicted in our income tax rate schedules with *equal treatment* toward holders of wealth that will allocate a greater portion of the tax burden based upon a citizen's real ability to pay.
- Repealing the corporate income tax and reforming existing tax expenditures, thereby eliminating the morass of special treatment policies and loopholes now written into our tax code, will take investors' and business' hands out of our government's pockets

FISCAL RESPONSIBILITY

- Increased tax revenues are a required step toward a balanced budget
- A balanced budget will convert the hidden taxes of inflation and debt imposed on future generations to a current tax burden, which can thus be more readily and responsively monitored, managed and matched to expenditures
- A balanced budget will stabilize the currency

The long-term cost of inflation exceeds the cost of a 2% asset tax which could control deficit spending and stabilize the currency. Any benefit from inflation on the Public Debt is overwhelmed by the cost imposed upon Private Debt Holders, whose aggregate holdings are four times the amount of our national public debt.

By improving the perceived equity of tax revenue policies we can minimize the divisive lobbying for government programs funded with Other People's Money – and hopefully thereby also impose greater discipline upon disbursement programs and priorities.