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## Proposal for a Fair, Simple Income Tax System

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## Description

- tax base: income
- exemptions: no deductions allowed.
- tax rate(s): 25% of income over \$40,000 on individuals only.
- distribution of the tax burden: low income families pay no income tax.
- treatment of charitable giving: no deductions allowed.
- treatment of home ownership: simple calculated based on capital gain.
- collection method(s): current Internal Revenue bureaucracy.
- treatment of businesses: businesses are not taxed

## Impact of Proposal Relative to Current System

- simplicity: this is the simplest possible approach.
- fairness: this is the fairest possible approach.
- economic growth and competitiveness: ideal for business and the economy
- compliance and administration costs: lowest possible costs.

## Transition, Tradeoffs and Special Issues

Transitioning to this proposed income tax system will be simple, fair and easy for all parties except tax accountants and tax whose services would no longer be in high demand. Some IRS agents would still be required but by and large, the IRS bureaucracy could probably be reduced by 90 percent

The transition could take place quite rapidly due to the fairness and simplicity. The only reason to spread the transition over multiple years is to give workers in the tax industry ample time to find alternate employment.

Here's a simple solution that will finally make income taxes fair and simple and at the same time will fix our economy.

1. Eliminate income tax on businesses. Tax only individual people. Business owners should be taxed ONLY on the money they take out of the business as personal income
2. Tax individual people at a flat tax rate of 25% of the income above their first \$40,000 per year. No loopholes. No deductions. No subsidies for any "special" groups like home owners or married couples or people with children. (These numbers are expected to be revenue neutral at the current point in time but can be changed accordingly)
3. All money coming in to the individual should be taxed including wages, interest, dividends, capital gains, inheritance and gifts etc

There are two variables here the government can play with: the flat percentage rate and the baseline amount (25% and \$40,000 in number 2 above). These two variables are the only aspects of this structure that congress should be allowed to modify.

This approach is fair to everyone because everyone, rich and poor alike, is taxed by the exact same formula. The baseline amount protects low-income people. There is less incentive to cheat because the system is fair to everyone equally. According to the Economist magazine, Russia discovered that making income taxes simple and fair increased both productivity and compliance (see: [http://www.economist.com/finance/displaystory.cfm?story\\_id=3860731](http://www.economist.com/finance/displaystory.cfm?story_id=3860731))

What about a capital gain on the sale of your home? The capital gain is the sales price minus the purchase price and that is what should be taxed. Keep it simple - interest rates and payments should not factor into the equation. This rule should apply to anything an individual sells at a gain such as a car or a boat or artwork (few individuals own anything that gains value other than a house) These rules are exceedingly fair, simple and consistent. There are NO special rules for houses versus artwork and there are NO mathematical gymnastics to deal with changing interest rates. Just fair and simple.

What if your home loses value? Too bad. There are no deductions for capital losses because there are no deductions. It should be recognized and emphasized – it is deductions that make the tax system complicated and unfair. It is NOT the progressive rates, per se, that leads to unfairness and complication.

Why not tax business? Because it's a huge drag on our economy and because "business" is just a concept. Without people, there is no business. People are the atomic level entity making and spending money. In addition, taxing business is complicated. Some businesses like grocery stores have very low margins whereas other businesses have margins over 30%. It's these differences in margin that make it necessary to tax based on "net" income and that's what introduces all the complexity and unfairness in the income tax system. The concept of taxing "net" income opened the door to special subsidies for home owners and other such nonsense that simply isn't equally fair to all parties.

This flat individual-only income tax will improve our economy because businesses will be able

to focus solely on good business rather than red tape and tax impact. Will the absence of income tax from businesses significantly reduce federal tax receipts? Not much. It's a little-known fact but individual tax payers provide the bulk of federal tax receipts. According to ABC World News with Peter Jennings on April 12, 2005, by the year 2003, corporations were only paying 16 percent of the total tax money taken in by the federal government. Businesses don't really pay much into the government anyway but they do waste a lot of resources and time trying to manage and reduce their income tax liability.

The budget of the IRS is somewhere in the neighborhood of \$10 Billion (with a B) per year! That's an instant nearly \$10 Billion dollar savings if we can reduce the vast IRS bureaucracy.

Some people advocate a national sales tax to replace the income tax system. That's a pretty ridiculous idea. There is already a pretty good incentive to cheat on sales tax by purchasing online or out of state. How much more incentive would there be if the sales tax was high enough to replace the income tax system? On top of that, sales tax receipts by the government would fluctuate wildly with the economy and therefore, predicting receipts and setting the budget would be a guessing game. Receipts from a flat income tax would be much more stable and would lead to a much healthier economy.

Some people argue for a national sales tax on the basis that government should tax consumption rather than production in order to encourage people to save but it is NOT the business of government to decide if people should spend or save their money. This is a common mistake but it's very important to remember that government exists in order to protect the rights of its citizens, not to influence the activities of its citizens. It is not government's job to be promoting family values or savings or sexual abstinence. With this principal in mind, it's easy to see that a flat income tax on individuals only and not on businesses is far superior to a national sales tax.

What about other so-called "flat tax" proposals? As mentioned before, it is deductions and the myriad special calculations that make the tax system complicated and unfair. It is NOT the progressive rates, per se, that leads to unfairness and complication.

This simple, fair, flat, individual-only income tax system would lead to the strongest economy the world has ever seen, even surpassing the dot-com bubble of recent years.

I've written more detail on these ideas here:

<http://superstition.blogspot.com/2005/04/magic-bullet-to-fix-income-taxes-and.html>

<http://superstition.blogspot.com/2004/02/fair-taxes-and-improved-economy.html>

<http://superstition.blogspot.com/2004/08/more-on-flat-tax.html>

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