

News from Senator

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STATEMENT OF SENATOR DOLE FINANCE COMMITTEE HEARINGS ON THE FLAT-RATE TAX

TODAY THE FINANCE COMMITTEE BEGINS THOROUGH AND COMPREHENSIVE CONSIDERATION OF THE ISSUES RAISED BY PROPOSALS TO MOVE IN THE DIRECTION OF A FLAT-RATE, OR PROPORTIONAL, INCOME TAX SYSTEM. THESE INITIAL HEARINGS FOLLOW ON MY ANNOUNCEMENT LAST MAY THAT OUR COMMITTEE WOULD UNDERTAKE AN EXTENSIVE REVIEW OF THE FLAT-RATE CONCEPT AND RELATED ISSUES OF TAX, SOCIAL, AND ECONOMIC POLICY. THIS IS ONLY A BEGINNING: THERE ARE MANY INDIVIDUALS AND ORGANIZATIONS WHO WOULD LIKE TO BE HEARD ON THIS SUBJECT, AND WHILE WE CAN ACCOMMODATE A SMALL NUMBER NOW, WE WILL DO OUR BEST IN FUTURE ROUNDS OF HEARINGS TO HEAR EVERYONE - WE NEED TO HEAR AS WIDE AS POSSIBLE A RANGE OF OPINIONS AND PERSPECTIVES ON THIS SUBJECT, BECAUSE WE ARE CONSIDERING FUNDAMENTAL CHANGE.

OVER THE NEXT THREE DAYS IT IS HOPED WE CAN BEGIN TO ESTABLISH A FRAMEWORK TO GUIDE FURTHER DELIBERATIONS ON RESTRUCTURING OUR TAX SYSTEM. WE CAN DO THAT BY CLEARLY FORMULATING THE BASIC OPTIONS, BY DEVELOPING THE FACTS AND FIGURES NECESSARY TO INFORMED DECISIONS, AND TO PINPOINT THE TECHNICAL AND PRACTICAL PROBLEMS THAT WILL HAVE TO BE DEALT WITH IF WE WANT TO MODIFY THE TAX SYSTEM IN A MAJOR WAY. OUR WITNESSES ARE PREPARED TO HELP US DO ALL OF THAT; IN PARTICULAR THE TREASURY DEPARTMENT HAS EXAMINED THE ISSUE IN SOME DETAIL, AND WHILE THEY ARE NOT PREPARED TO MAKE SPECIFIC RECOMMENDATIONS AT THIS TIME, I HOPE THAT WE WILL GET AN INDICATION OF HOW THE ADMINISTRATION THINKS WE OUGHT TO PROCEED, AND OF HOW THEY RANK THE ISSUES IN TERMS OF PRIORITIES. THIS MORNING'S TESTIMONY FROM ASSISTANT SECRETARY CHAPOTON SHOULD PROVIDE ABLE ASSISTANCE IN FORMULATING OPTIONS FOR FURTHER CONSIDERATION.

BASIC CHOICES

AT THE OUTSET, I WOULD LIKE TO OUTLINE SOME OF THE BASIC CHOICES WE HAVE BEFORE US IN CONNECTION WITH THE FLAT-RATE ISSUE. SOME OF THESE CHOICES ARE SIMPLY MATTERS OF TRYING TO FORMULATE THE BEST TAX POLICY; SOME OF THEM ARE PRIMARILY DECISIONS ABOUT ECONOMIC POLICY; AND OTHERS ARE REALLY POLITICAL DECISIONS, OR DECISIONS ABOUT WHAT IS BEST FOR OUR SOCIETY.

FOR EXAMPLE, WE HAVE TO DECIDE WHETHER SIGNIFICANT PROGRESSION IN RATES IS DESIRABLE--AS UNDER THE PRESENT SYSTEM--OR WHETHER EVERYONE SHOULD PAY THE SAME PROPORTION OF INCOME IN TAXES. THE ANSWER TO THIS QUESTION WILL DEPEND IN PART ON YOUR VIEW OF HOW IMPORTANT THE PRINCIPLE OF PROGRESSIVITY IS TO MAINTAINING POPULAR SUPPORT FOR THE TAX SYSTEM. THE ANSWER ALSO WILL DEPEND ON SOME SIMPLE FACTS: HOW PROGRESSIVE IS THE PRESENT SYSTEM, WHEN YOU TAKE INTO ACCOUNT THE DISTRIBUTION OF TAX PREFERENCES AVAILABLE UNDER PRESENT LAW, PARTICULARLY DEDUCTIONS THAT TEND TO FAVOR THOSE IN HIGHER RATE BRACKETS.

WE ALSO HAVE TO DETERMINE HOW MUCH A GAIN IN SIMPLICITY AND ECONOMIC EFFICIENCY CAN BE MADE BY MOVING TO A STREAMLINED LOW-RATE OR FLAT-RATE STRUCTURE. DEFINING INCOME WILL ALWAYS BE A SOURCE OF MAJOR COMPLEXITY, AND CUTTING OUT TAX PREFERENCES AS SUCH DOES NOT DEAL WITH THAT PROBLEM. A LARGE ZERO BRACKET, IF IT WERE ADOPTED AS PART OF A RESTRUCTURING OF OUR TAX SYSTEM, COULD PROVIDE SIGNIFICANT GAINS IN SIMPLICITY BY REDUCING THE NUMBER OF ITEMIZERS. AGAIN, HOWEVER, WE WOULD NEED TO EVALUATE THE IMPACT OF SUCH A CHANGE ON THE DISTRIBUTION OF THE TAX BURDEN AND IN TERMS OF ECONOMIC EFFICIENCY.

IN ADDITION, THERE ARE A NUMBER OF SPECIFIC WAYS IN WHICH A FLAT-RATE, OR LOWER-RATE, TAX SYSTEM MIGHT BE STRUCTURED. A SINGLE RATE COULD BE APPLIED, AS SOME PROPOSE, TO A COMPREHENSIVE INCOME BASE. THIS WOULD MEAN EVERYONE PAYING THE SAME PROPORTION OF INCOME IN TAX, WITH CHANGES IN THE TYPES OF THINGS WE HAVE USUALLY INCLUDED IN INCOME: ITEMS SUCH AS SOCIAL SECURITY AND RETIRMENT BENEFITS, AMONG OTHERS. ALTERNATIVELY, RATES COULD BE SIGNIFICANTLY REDUCED AND THE BASE BROADENED BY ELIMINATING A RANGE OF TAX PREFERENCES, BUT WITHOUT GOING ALL THE WAY TOWARD A SINGLE RATE WITH A COMPREHENSIVE BASE. THESE TWO BASIC OPTIONS CAN BE VARIED, IN ADDITION, BY INCLUDING IN EITHER A LARGE ZERO BRACKET: GUARANTEEING A DEGREE OF PROGRESSIVITY AND PROTECTION FOR LOWER-INCOME TAXPAYERS, WITH SOME GAIN IN SIMPLICITY AS WELL FROM REDUCING THE NUMBER OF ITEMIZERS, ASSUMING THE OPTION OF RETAINING SOME DEDUCTIONS IS CHOSEN. FINALLY, WE COULD CONSIDER A FLAT-RATE TAX ON A LESS COMPREHENSIVE INCOME BASE; PRESERVING SOME BASIC TAX PREFERENCES THAT HAVE WIDE SUPPORT, BUT AT THE SAME TIME PRESUMABLY REQUIRING A HIGHER RATE TO GENERATE THE NECESSARY AMOUNT OF REVENUE. THESE FIVE OPTIONS, AND A DISCUSSION OF SOME MAJOR ISSUES IN CORPORATE TAXATION THAT ARE RAISED BY THE FLAT-RATE DEBATE, ARE DISCUSSED IN MORE DETAIL IN A NARRATIVE OUTLINE AND MEMORANDUM ON CORPORATE ISSUES, WHICH I WILL INCLUDE IN THE RECORD FOLLOWING MY STATEMENT AND MAKE AVAILABLE TO THE MEMBERS FOR THEIR INFORMATION.

WHAT IT COMES DOWN TO IS A CHOICE OF WAYS TO PROCEED. EVERYONE WANTS GREATER EQUITY IN THE TAX CODE, AND A SIMPLER SYSTEM, AND A TAX SYSTEM THAT PROMOTES--OR AT LEAST DOES NOT INHIBIT--ECONOMIC ACTIVITY. CHOOSING THE SYSTEM THAT BEST BALANCES EACH OF THESE GOALS IS NOT EASY, HOWEVER: AND DECIDING HOW TO MOVE TOWARDS A BETTER SYSTEM MAY BE THE MOST DIFFICULT CHOICE OF ALL.

HOW TO PROCEED

THE WAYS IN WHICH WE MIGHT PROCEED SEEM, TO THIS SENATOR AT LEAST, TO BE FAIRLY STRAIGHTFORWARD. FIRST, WE COULD CONTINUE TO WORK THROUGH THE TAX CODE ON AN ITEM-BY-ITEM BASIS AND MAKE DECISIONS ABOUT WHAT SHOULD GO OR BE MODIFIED AND WHAT SHOULD BE PRESERVED: IN OTHER WORDS, FURTHER BASE-BROADENING AND TAX REFORM EFFORTS COMPARABLE TO THOSE INCLUDED IN THIS YEAR'S TAX EQUITY AND FISCAL RESPONSIBILITY ACT. THIS APPROACH COULD BRING SUBSTANTIAL GAINS IN EQUITY AND SIMPLICITY OVER TIME, BUT IT WOULD NOT NECESSARILY INVOLVE THE KIND OF FUNDAMENTAL RETHINKING OF OUR TAX STRUCTURE THAT MANY PEOPLE SEEM TO WANT.

INSTEAD, WE MIGHT DO AS SOME ARE URGING, AND AGREE ON A MAJOR REVISION OF THE TAX SYSTEM IN THE DIRECTION OF LOWER RATES AND A BROADER BASE, AND TAKE THE NECESSARY STEPS TO IMPLEMENT SUCH A SYSTEM. THIS WOULD MEAN AN EXPLICIT CHOICE OF A NEW APPROACH TO TAXES; COMPREHENSIVE AND CAREFULLY THOUGHT OUT; AND A DIFFICULT PERIOD OF TRANSITION TO RECONCILE THE NEW SYSTEM WITH THE OLD WHILE SAFEGUARDING THE ECONOMIC INTERESTS OF THOSE WHO HAVE MADE FINANCIAL DECISIONS BASED ON THE PRESENT SYSTEM. THE POTENTIAL PITFALLS WITH

THIS APPROACH ARE THAT IT REQUIRES LONG-RANGE PLANNING AND IMPLEMENTATION, AND THERE IS THE RISK THAT THE CONSENSUS BEHIND THE NEW SYSTEM COULD ERODE DURING THE LENGTHY COURSE OF IMPLEMENTATION. THAT COULD LEAVE US WITH A SYSTEM NO BETTER, OR EVEN WORSE, THAN PRESENT LAW.

FINALLY, WE MIGHT AGREE TO PROCEED, AGAIN ON A STEP-BY-STEP BASIS, TO COUPLE BASE-BROADENING MEASURES WITH RATE REDUCTIONS IN AN EFFORT TO SIMPLIFY THE SYSTEM AND REDUCE TAX-INDUCED DISTORTIONS OF ECONOMIC DECISION-MAKING. THE ADVANTAGES HERE WOULD BE THAT WE WOULD HAVE AN OPPORTUNITY TO THINK OUT EACH STEP AS IT IS TAKEN, AND TO BUILD A CONSENSUS ON THE DESIRABILITY OF THOSE STEPS. THE DISADVANTAGE IS THAT YOU WOULD NOT MAKE A SPECIFIC COMMITMENT TO A BOTTOM-LINE GOAL FOR OUR INCOME TAX POLICY.

MUCH TO BE DONE

JUST OUTLINING THE POLICY OPTIONS AND PROCEDURAL OPTIONS MAKES CLEAR HOW MUCH THERE IS TO BE DONE IF WE WANT TO REBUILD OUR TAX SYSTEM IN A WAY THAT IS FAIRER, SIMPLER, AND BETTER FOR THE ECONOMY. NO SYSTEM CAN BE SUSTAINED WITHOUT A STRONG POPULAR CONSENSUS: INDEED, A MAJOR REASON WE ARE CONSIDERING FUNDAMENTAL REFORMS IS THE INDICATION OF WEAKENING CONSENSUS BEHIND OUR PRESENT SYSTEM, AS DEMONSTRATED BY THE GROWING COMPLIANCE PROBLEM. WE DO NOT WANT TO HASTILY ADOPT A SYSTEM THAT CANNOT BE SUSTAINED OVER TIME, EITHER BECAUSE OF TECHNICAL FLAWS OR LACK OF POPULAR SUPPORT.

SO OUR TASK IS TO BEGIN TO SEARCH OUT THE KIND OF CONSENSUS NEEDED TO SUPPORT ANY FAR-REACHING CHANGE IN TAX POLICY. THE DIRECTION HAS BEEN SET, IN A WAY, BY THE RATE REDUCTIONS ADOPTED IN 1981 AND THE BASE-BROADENING AND COMPLIANCE MEASURES WE AGREED TO THIS YEAR. WE HAVE ALREADY MOVED TOWARDS LOWER RATES AND A BROADER BASE, AND HAVE PUT THE PRESSURE ON TO REEXAMINE THE TAX SYSTEM BY INDEXING INDIVIDUAL RATES TO END BRACKET CREEP. THERE DOES SEEM TO BE A GROWING CONSENSUS FOR FURTHER REDUCTION OF RATES AND BROADENING OF THE TAX BASE. WITH PROPER BALANCING OF THE GOALS OF EQUITY, EFFICIENCY, AND SIMPLICITY, THAT CONSENSUS CAN GROW, AND IT HAS THE POTENTIAL TO OPEN THE WAY TOWARDS THE FIRST MAJOR RESTRUCTURING OF TAXES IN YEARS. I HOPE THE WITNESSES THIS MORNING, AND OVER THE COURSE OF THESE HEARINGS, WILL SHED SOME LIGHT ON THE PROSPECTS FOR DRAMATIC CHANGE IN TAXATION AS WELL AS HELP CLARIFY OUR CHOICES.