



## The Flat Tax is Simple, Fair, and Pro-Growth

by Amy K. Frantz

On January 7, 2005, President Bush announced the creation of the President's Advisory Panel on Federal Tax Reform. This bipartisan panel, headed by former Republican Senator Connie Mack and former Democrat Senator John Breaux, will submit a report to the Secretary of the Treasury by August 31 with recommendations for reforms to make the tax code more simple, fair, and pro-growth than our current tax system. A flat-rate income tax would fulfill all of these goals and should be one of the panel's proposals.

Our federal taxes were due last month. Most of us probably spent many hours preparing our own tax returns or had to pay someone else to prepare them for us. The current income tax code, with its many deductions, exemptions, and credits, is extremely complicated and makes paying our taxes a time-consuming or expensive task. Even the IRS agrees, as it states in the instructions for Form 1040 (which are 128 pages long!), "We try to create forms and instructions that can be easily understood. Often this is difficult to do because our tax laws are very complex."<sup>1</sup>

A flat-rate income tax would eliminate the complexity of our current tax code. Imagine how simple it would be to multiply your income for the year by one single tax rate and pay that amount in income taxes, with a minimal amount of deductions or exemptions. Taxpayers would no longer need a 128-page instruction book or a Certified Public Accountant to comply with the tax code.

Under a flat tax system, everyone pays the same portion of their income as taxes. Bill Gates would pay more in total taxes than a college graduate working at their first job, but both of them would pay the same flat-rate percent of their income in taxes. The flat tax also creates a system in which two people with the same income would pay the same amount of income tax. Under our current tax system, income tax is based on far more than just the amount of income earned for the year.

Another benefit of the flat income tax is that the taxpayer is not punished for saving or investing, as the taxpayer is under our current system that imposes a tax on interest income, capital gains, and dividends. Interest or investment income has already been taxed once when first earned by either an individual or a corporation. The flat tax would not tax this income a second time. Replacing our current tax system with a flat income tax "would add as much as two percentage points to the nation's economic growth rate."<sup>2</sup>

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A Publication of:

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Countries around the globe are recognizing the benefits of a flat tax and replacing their own tax systems with a flat income tax. Russia replaced its tax system with a flat-rate income tax in 2001. Prior to that, Russia had a three-bracket income tax with a top tax rate of 30 percent. Under the old system, tax evasion was widespread. With a flat tax — the tax on personal income is 13 percent — the Russian “economy has enjoyed four years of sustained growth.”<sup>3</sup> Total income tax receipts have also grown since the flat tax was implemented four years ago, as the lower rate has discouraged tax evasion and led to less economic activity going unreported, which had previously been taking place “underground.”

Many other Eastern European countries have also reformed their tax systems by implementing a flat tax. Estonia was the first country to do so, implementing a flat tax in 1994. Since then, Latvia, Serbia, Ukraine, Slovakia, Georgia, and Romania are among the countries that have followed suit, recognizing the benefits of a flat tax system. Even in Iraq, the old tax system with a top tax rate of 45 percent has been replaced with a 15 percent flat income tax.

The flat tax is not just a national issue. Six states, including our neighbor to the east — Illinois — have a flat income tax system. Both the Governor and current State Legislators have spoken of reforming and simplifying Iowa’s tax system. It is encouraging that our elected officials on both the state and national levels have recognized the need for tax reform. For an income tax system that is simple, fair, and pro-growth, they should consider the flat tax.

#### **ENDNOTES:**

<sup>1</sup>2004 1040 Instructions, Including Instructions for Schedules A, B, C, D, E, F, J, and SE, Department of the Treasury, Internal Revenue Service, <<http://www.irs.gov/pub/irs-pdf/i1040.pdf>>, (April 6, 2005).

<sup>2</sup>John C. Goodman, “Principles of a Flat Tax,” *Brief Analysis #195*, National Center for Policy Analysis, <<http://www.ncpa.org/ba/ba195.html>>, (April 7, 2005).

<sup>3</sup>Alvin Rabushka, “Flat and Happy . . .,” *Wall Street Journal*, January 12, 2005, p. A10, col. 3.

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