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On Tax Day, let's rethink government

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This Tax Day, there's good news and bad news. The good news is that Americans will enjoy an extra two days to file their returns. (April 15 was Sunday, and today is Emancipation Day, a legal holiday in the District of Columbia.)

The bad news? Washington will burn through our \$2.5 trillion in taxes by July 31. After that, everything goes on credit. And by December, even the federal credit card will be maxed out, and politicians will again raise the debt ceiling.

Can we get out of this mess by raising taxes? The willingness to try anything is understandable, but the question is misleading. This Tax Day, it's important to remember that the government cannot raise taxes. It can only raise tax rates.

Here's why the distinction matters. Taxes are what you get when you apply tax rates to economic activity, which the government doesn't control.

As tax rates rise, economic activity tends to fall. Since the 1950s, federal tax receipts have been a fairly constant 18 percent slice of the economy.

In the years when the top marginal tax rate was above 50 percent, federal receipts averaged 17 percent of the gross domestic product. In the years when the top marginal tax rate was below 50 percent, federal receipts averaged 18 percent of GDP. Federal receipts were 18 percent of GDP when the capital gains tax rate was above 25 percent and when the tax rate was below 25 percent. Whether the effective corporate tax rate was above or below 30 percent, the federal government's tax revenue was the same 18 percent of GDP.

Historically, it hasn't mattered whether tax rates are high or low: The government collects the same 18 percent of the economic pie.

Surprise: The government actually has no control over how much tax revenue it collects.

Perhaps the answer to reining in the deficit is to cut spending. This year the White House has proposed cutting NASA's budget by \$60 million. That much money will fund Washington for a full 10 minutes. The government actually spent more money in the time it took White House staffers to write the sentences announcing the NASA cuts than what the cuts saved us.

Starting in January 2011, the White House spent weeks publicly wringing its hands over whether to cut \$300 million in community block grants. What the White House didn't tell you is that the federal government blows through \$300 million every 45 minutes.

In the government's defense, there are no moderate cuts that will balance the budget. If the government shut down all of NASA plus the Army, Air Force, Marines and Navy, the budget still wouldn't balance.

Don't look for waste among the litany of agencies and departments either. The government collects enough revenue to pay for Social Security, Medicare and the interest on the debt. That's all. Politicians waste our time when they debate whether we can afford this program or that program. We can't afford any program.

There is a solution, but it requires rethinking government.

First, we need a tax code so simple that a bright elementary school student could do your taxes. We need a fair tax code that eliminates both taxation without representation and representation without taxation. If the government is destined to collect 18 percent of the economic pie no matter what it does, then let's make sure that the pie is as big as it can be. Low, simple and transparent taxes are a good start.

Second, we need to break Washington's monopoly on government. The Constitution established the federal government as a referee to encourage competition among the states. States that governed well would be rewarded with growing economies and populations. States that governed poorly would be punished as people voted with their feet. This is how it works in free markets.

Instead of adopting this model of a healthy market, Washington has adopted the model of the robber barons — shut down the competition so the customer has nowhere else to go. American government was supposed to be eBay, not Standard Oil. Our Constitution established a good model for government. Perhaps it's time that we gave that model a try.

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