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Opening Statement

Federal Tax Reform Panel

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In his State of the Union address, President Bush set out three objectives for tax reform: “pro-growth, easy to understand, and fair to all.” Since the enactment of the Tax Reform Act of 1986, we have been moving farther away from its goals of fairness and simplicity with each succeeding tax bill. I am looking forward to working with my colleagues on the Tax Reform Panel to find our way back to a fairer, less complex system of raising revenue, one that also ensures strong economic growth and international competitiveness for our country. As we examine how to assemble changes to the tax system that promote growth, fairness and simplicity, we need to keep several goals in mind.

First, we need to think about incentives. We have long used the tax code as a way to encourage people and businesses to create value for our economy

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and society. I am sure that any reform proposal we bring forward will include some such provisions; indeed, the Executive Order that established our Panel directed us to recognize "the importance of homeownership and charity in American society." As we consider which tax expenditures should be retained, which should be expanded, and which should be eliminated, we must keep in mind that tax expenditures are only justified when they actually change behavior in the way we intend it to change. It is not worth the revenue loss if a tax expenditure subsidizes behavior that would occur even without the tax incentive; all that happens is that we create a windfall for a few at the expense of all taxpayers. Fortunately, we have data about the effect of tax expenditures that have been in the code for years, and I look forward to carefully scrutinizing that data so that we are certain every tax subsidy we support is likely to produce its intended effects.

Second, we need to remember fiscal discipline. As we go about our work, we must keep in the forefront of our minds that the tax system is primarily designed to raise revenue to support the activities that the federal government engages in – both at home and abroad. Our proposal is supposed to be revenue neutral, that is, to raise the same amount of money as the current tax system raises. Some tax reform proposals that we are likely to consider may not result in immediate revenue loss, but over time they will substantially reduce the revenue that the federal government collects. We cannot focus only on the short-run and leave the next generation to face dire fiscal realities. Given the current federal fiscal situation, with a deficit estimated at around \$500 billion in fiscal year 2005, as well as with looming shortfalls in the entitlement programs – Medicare and Social Security – we have a profound obligation to recommend changes that are fiscally prudent not just in the next five or ten years, but also in the long term. We must be aware that the fiscal health of the country is much more dramatically affected by revenue decisions and decisions about entitlement programs than it is by spending through the annual appropriations process.

Third, we must remember that progressive rates are not the only important feature of a tax system that is designed to be "fair to all." The goal of fairness is concerned with how the tax system treats people in different circumstances. We need to recognize that in our complex society, taxes can be unfair not only when they fail to take into account differences in income levels. We need to consider fairness across differences in tax status, looking at whether some tax credits should be refundable to provide incentives to those without tax liability as well as to those who owe taxes. We must consider what is fair across differences in marital status, determining the right structure to tax married couples when both work and earn income. We need to think about how to fairly balance the tax burden on income from wages – already burdened by payroll taxes – with the tax burden placed on income from savings and investment.

Fairness also implicates issues of transparency. Citizens must understand, in at least a general way, how they will be taxed. It is not fair, for example, to surprise them with an alternative minimum tax that was designed only to apply to the very wealthy in our country, but which is now projected to apply by 2010 to more than 34 million Americans, many of them families with relatively modest incomes.

These are some of the issues, among many, that I hope we will address in our work. I am looking forward to the next few months of discussion and analysis and to bringing forward options for reform that are consistent with the President's goals, and with the goals we all share for a better, fairer tax system.