

How Could We Improve the Federal Tax System?

VALUE-ADDED TAX (VAT)

How are different consumption taxes related?

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A. A retail sales tax, value-added tax, the flat tax, and the X-tax are closely related. These taxes are contrasted with wage taxes.

A retail sales tax is a flat-rate tax on all sales from businesses to households.

A value-added tax (VAT) is equivalent to a retail sales tax but it collects the tax in small pieces at each stage of production rather than entirely at the final sale.

The Hall-Rabushka flat tax is simply a two-part VAT, with all value added except wages taxed at the firm level and wages taxed at the individual level, after allowing for exemptions based on family size. Businesses and individuals face the same flat rate on all income.

The X-tax is simply a variant of the flat tax in which wages are taxed at graduated rates, and the business tax is set equal to the highest rate on wages.

A wage tax is quite different. It would tax wages directly, as would the flat tax or X-tax, but it would not contain the business component of such taxes.

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Further Reading

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