

How Could We Improve the Federal Tax System?

How would the tax system need to change with return-free filing?

RETURN-FREE TAX FILING

Q. How would the tax system need to change with return-free filing?

A. The simpler the system, the easier it would be to increase the number of return-free filers.

Although many countries have adopted return-free tax systems, most of them have simpler tax codes than the United States. Implementing a return-free system that most US taxpayers could participate in would require sweeping changes in the tax code to make it more like those countries'. Common elements of such codes include a "basic" rate for most taxpayers, the designation of individuals (rather than families) as the unit of taxation, taxation of interest and dividends at one rate (and at the source), exemption of some capital gains from taxation, and the paring of deductions, allowances, and credits.

Still, with just minor reforms, the current system could accommodate return-free filing for the substantial number of taxpayers who now file simple returns. A big stumbling block is that the current withholding formulas are not designed to be exact for dependent filers, dual-income couples, or taxpayers with more than one job during the year. Indeed, if dependent filers and filing units with income from more than one job were still required to file a return, only 8 million taxpayers with wage income could be exempted from filing. Even among these 8 million, changes in personal circumstances during the year could cause withholding errors.

Without any changes in the law, it might still be possible to fine-tune withholding formulas to meet most taxpayers' needs. But there's no free lunch here: attaining the additional precision would add significant complexity to Form W-4 and the computation of withholding allowances.

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Further Reading

Gale, William G., and Janet Holtzblatt. 1997. ["On the Possibility of a No-Return Tax System."](#) *National Tax Journal* 50 (3): 475–85.

US Department of the Treasury. 2003. [Return-Free Tax Systems: Tax Simplification Is a Prerequisite](#). Washington, DC: US Department of the Treasury.