Q. The Graetz Competitive Tax Plan: Update for 2015.

A. Graetz's proposal recommends cutting income and payroll taxes and making up the revenue with a value-added tax.

Columbia University law professor Michael Graetz introduced his "Competitive Tax Plan" more than a decade ago and has recently updated it. Broadly, the plan shifts the tax system, which is based on income, to one based on consumption. The plan is revenue neutral and would not change the overall income distribution.

The Competitive Tax Plan contains five components.

- A value-added tax (also called a goods and services tax) with a broad base and a single rate of 12.9 percent. Businesses with less than $1 million in gross receipts would be exempt. There would be 18 to 24 months between enactment and implementation, which Graetz expects would accelerate purchases of durable goods and provide a short-term boost to the economy. The tax would be modeled after modern value-added taxes in New Zealand, Australia, Canada, Singapore, and South Africa. States would be given incentives to harmonize their tax policies with the federal tax.

- An individual income tax in which the first $100,000 of income for married couples would be exempt from taxation ($50,000 for singles and $75,000 for heads of household). Above this threshold, tax rates would be 14, 27, and 31 percent. The alternative minimum tax and surtax on investment income would be repealed. With these reforms, less than one-fifth of the households now paying income tax would be required to file returns.

- A corporate income tax with a reduced rate of 15 percent. All credits except the foreign tax credit would be eliminated, and the corporate alternative minimum tax would be repealed. The plan may also subject large businesses (even if they are not corporations) to the corporate income tax while simplifying the taxation of small businesses.

- The current payroll tax, but with credits of 15.3 percent of wages for workers with earnings up to $10,000 and a credit of $1,530 for workers earning between $10,000 and $40,000. The credit phases out for incomes above $40,000.

- Refundable child credits would be established and distributed through debit cards. Each child would qualify for $1,500 per year, with a phaseout provision for higher-income earners. Low- and moderate-income earners, on the other hand, would receive an additional rebate of up to $3,500 for one child and $5,200 for two or more children.

How Could We Improve the Federal Tax System?

The Graetz "Competitive Tax Plan:" Update for 2015

Further Reading

Graetz, Michael. 2008. *100 Million Unnecessary Returns: A Simple, Fair, and Competitive Tax Plan for the United States*. New Haven, CT: Yale University Press.

———. 2013. "The 'Competitive Tax Plan' Updated for 2015." Presentation given at the National Tax Association, Tampa, FL, November 21.

Toder, Eric, Jim Nunns, and Joseph Rosenberg. 2012. "Using a VAT to Reform the Income Tax." Washington, DC: Urban-Brookings Tax Policy Center.