

How Could We Improve the Federal Tax System?

What did the President's Advisory Panel on Federal Tax Reform say about the national retail sales tax?

M

Q. What did the President's Advisory Panel on Federal Tax Reform say about the national retail sales tax?

A. Put simply: a nonstarter.

The President's Advisory Panel on Federal Tax Reform's first objection to replacing the current tax system with a national retail sales tax hinges on the latter's effect on income distribution. The report (2005) noted that "lower and middle-income families would be especially hard hit by a stand-alone retail sales tax" (2005, 211).

The panel was also concerned that, although the proposed demogrant program (which would provide cash rebates to needy households) would make the retail tax system less regressive, it would be a bear to administer. And it would thus "inappropriately increase the size and scope of government" (208). Moreover, the panel concluded that, with the demogrant, the tax rate needed to sustain current federal revenues would exceed—perhaps far exceed—34 percent. Meanwhile, households would still be liable for state and local sales taxes, which currently average 6.5 percent.

Nor was the panel impressed with the tax's value as a tool to simplify the tax system. Taxpayers would still be required to complete state income tax returns unless states abolished their own income taxes. Moreover, a new government agency would be required to monitor both collection of the tax and allocation of demogrants.

The panel also expressed concern about likely evasion: "A federal retail sales tax assessed at a rate of at least 34 percent, added on to state retail sales taxes, would provide substantial inducement for evasion at the retail level" (218). And with third-party reporting—such as W-2 and 1099 forms—notably absent from the proposal, "evasion rates are estimated to be around 50 percent" (218).

There's more glum news here. The panel noted that states would lack the ability to collect the tax and that an agency analogous to the IRS would be needed to enforce compliance. It also pointed out that states currently rely on taxpayers' fears of audits of federal income tax returns to deter state sales tax evasion. If the federal government abandoned income tax enforcement along with the income tax, states would be left hanging. Last, the report cited concern that the burden of collecting the national retail sales tax would disproportionately fall on small businesses and small service providers, raising their costs.

Updated May 2020

Further Reading

President's Advisory Panel on Federal Tax Reform. 2005. [*Simple, Fair, and Pro-Growth: Proposals to Fix America's Tax System*](#). Washington, DC: President's Advisory Panel on Federal Tax Reform.

How Could We Improve the Federal Tax System?

What did the President's Advisory Panel on Federal Tax Reform say about the national retail sales tax?

M

Copyright © 2020. Tax Policy Center. All rights reserved. Permission is granted for reproduction of this file, with attribution to the Urban-Brookings Tax Policy Center.