Q. Why are taxes so complicated?

A. Our tax system could be simple if its only purpose were to raise revenue. But it has other goals, including fairness, efficiency, and enforceability. And Congress has used the tax system to influence social policy as well as to deliver benefits for specific groups and industries.

Almost everyone agrees that the current tax system is too complicated, yet almost every year the system gets more complex, not less. Why? Tax simplicity almost always conflicts with other policy goals.

For example, the simplest—and least distorting—tax is a head tax, a fixed-dollar tax on everyone. But a head tax would be unfair, taking no account of differences in the incomes and needs of individuals, families, and businesses.

COMPETING GOALS FOR A TAX SYSTEM

Most people believe taxes should be fair, conducive to economic prosperity, and enforceable, as well as simple. But even people who agree on these goals often disagree about the relative importance of each. As a result, policies usually represent a balance among competing goals, and simplicity often loses out to other priorities.

For example, most countries tailor tax burdens to individual taxpayers’ characteristics. That can make taxes fairer, but more complex. Income has to be traced from businesses to individuals. Individual characteristics such as marital status and number of dependents, as well as the composition of expenditures or income, have to be reported and documented. These conflicting objectives appear to be especially relevant in the current tax code, where the desire to reduce tax burdens for particular groups have added significant complexity.

POLITICS OF TAX POLICY

Politics compounds complexity. Interest groups—and thus politicians—support tax subsidies for particular activities. And these targeted subsidies inevitably complicate the tax system by creating distinctions among taxpayers with different sources and uses of income.

EFFECTS OF INCREMENTAL LEGISLATIVE CHANGES

The current tax law was not enacted all at once but is a result of numerous provisions added or subtracted in multiple tax bills. Often Congress designs legislation under self-imposed constraints, such as short-term revenue goals or effects on the distribution of tax burdens among income groups. The result is that
tax incentives are often designed in complex ways to limit the revenue losses or benefits to high-income taxpayers or to prevent their use by unintended beneficiaries.

The result of this process is a set of very complex provisions that appear to have no overall logic if the tax law were being designed from scratch. These include phaseouts of certain tax benefits at high incomes, multiple incentives for higher education and retirement savings, multiple benefits for taxpayers with dependents with different eligibility definitions, and an entirely separate tax schedule, the individual alternative minimum tax, that applies to certain taxpayers using selected tax preferences. The Tax Cuts and Jobs Act of 2017 substantially reduced the number of taxpayers subject to the alternative minimum tax through 2025 and, by raising the standard deduction and capping the state and local tax deduction, reduced the number of taxpayers who benefit from itemized deductions. But it left many other complex benefits in the tax law largely unchanged and added a new deduction for business income, with its own complex limits to minimize abusive transactions.

Annual reports by the National Taxpayer Advocate have presented proposals for simplifying the tax code, including reforms of education incentives, retirement incentives, child benefits, and the alternative minimum tax.

Further Reading


