

EDITORIAL/OPINION

VAT Chance for Tax Fairness

By CLYDE WAYNE CREWS Jr.

Back during the blip of interest in the value-added tax (VAT) after Bill Clinton first took office, a CNN reporter asked a man-in-the-street what a "VAT" was. The puzzled reply was pretty much on target. He said a VAT is a "large tub."

The value-added tax, which House Ways and Means Chairman Bill Archer, R-Texas, last week cited as a potential replacement — in combination with a national sales tax — for the income tax, is unfortunately back in play. The on-again, off-again VAT is a "large tub," metaphorically speaking, into which huge but nearly untraceable amounts of American consumers' expenditures will disappear.

The federal government already consumes 28% of the income of the typical family. Without drastic cuts in federal spending prior to reforming the federal tax code, the VAT, or even the proposed national sales tax, could be heaped on top of the existing income tax. But the VAT is especially fearsome, whether or not it replaces what we have.

A VAT is a tax placed on the value added to goods at each point in the production-distribution process. Republicans legitimately working to scrap the Internal Revenue Service and institute a national sales tax unfortunately have left the door open for the VAT, which was last considered by Democrats as a way to pay for deficit reduction and Clinton's health-care plan. Compliance and administrative costs for a VAT could approach \$8.5 billion annually.

Experience in other industrialized nations confirms that high rates are assured: The base VAT rate among the most prosperous countries averaged 16.6% in 1991, on top of other taxes in those countries.

A VAT is best described as a dishonest national sales tax. When plain-vanilla sales taxes are added to the goods we buy, we know the amount simply by looking at our receipts. And even though Americans work more than one-third of the year for federal, state and local governments before keeping a dime for themselves, we can still know how much we fork over by looking at our pay stubs and old federal and state income tax returns.

Knowing how much we are taxed is a fundamental right that preserves our ability to challenge excess federal spending. But a VAT hides the truth. When prices rise under a VAT system, we have no way of knowing how much of the increase is due to the tax and how much to

increases in raw material costs or other economic factors.

Instituting a flat tax and perhaps only then moving toward an above-board national sales tax would be best; that way the government never gets the chance to hide taxes from taxpayers as the VAT would allow.

While a VAT may appear theoretically elegant and unassailable as long as it replaces the existing clot of exemptions, deductions, credits and carry-overs, it will prove an economic and political nightmare for several reasons.

First, international experience indicates the VAT would not replace the existing tax system but would be added to what we already have.

Second, the VAT would be complex, with many rates likely rather than a single rate. Even ex-Ways and Means Committee Chairman Dan Rostenkowski said the VAT "would emerge from Congress looking like a lace doily."

Third, once enacted, it would be far too easy, and the temptation too overwhelming, for politicians to resist raising the surreptitious VAT. Because the tax would encompass the whole of the productive economy, tremendous amounts of revenue can be raised by tiny, almost imperceptible increases in the VAT rate. In a tired old game played by politicians, the resulting price

increases will be attributed to "corporate greed" or "mysterious" inflation.

That the VAT will rise once initiated is surely not mere speculation; all but three of 28 countries that have altered their standard VAT rate since introduction have increased rather than decreased the tax, according to International Monetary Fund data. Many other countries that have kept the standard rate constant nevertheless impose higher rates on "politically incorrect" categories of luxury goods.

A VAT also aggravates the tendency to expand government. Because the VAT's fixed percentage disproportionately harms poorer Americans who must spend a larger percentage of their budget on basic consumption goods, VATs create political pressure for expanding social welfare spending to correct the built-in unfairness — the very last stimulus needed now that substantial welfare reform may occur.

Since exempting staples such as food, medicine and housing from the VAT will significantly decrease its revenue potential, a VAT-propelled government enjoys a permanent excuse to expand social welfare programs to lessen inequities the tax imposes on poor families.

Of course in the real world, VATs probably will deliver the full range of economic blows: Count on an expansion of welfare spending, plus an increasing base VAT rate, plus greater rates for ever-expanding categories of "luxury" goods.

On average there are three VAT rates per country. Such politically motivated tiers give the lie to the "neutrality" that VATs are said to boast, and they foster political burlesque like the French dispute over whether dandruff shampoo is a medicine taxable at 5.5% or a cosmetic taxable at 18.6%.

The confounding nature of the VAT, coupled with its unmatched revenue potential, are the sources of its irresistible appeal worldwide. These features guarantee that the VAT will not die as a political issue so long as America's government binge continues.

Working Americans deserve a government downsizing, as well as a shift from the income tax to a flat tax and perhaps eventually to a sales tax. Massive reform of the tax code, such as that envisioned in the 104th Congress, provides a chance to lay the VAT to rest once and for all. That's what should be done.

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