

THE ONE FUND SOLUTION: “IT’S MY MONEY AND I NEED IT NOW!”

Gordon T. Butler*

ABSTRACT	263
I. INTRODUCTION	263
II. THE CURRENT FISCAL CRISIS.....	265
III. RECENT PROPOSALS	272
A. <i>The Moment of Truth</i>	272
B. <i>Bipartisan Policy Center Plan</i>	276
C. <i>The Roadmap for America’s Future</i>	284
D. <i>Michael J. Graetz and the Competitive Tax Plan</i>	290
IV. MAJOR CONCERNS IMPACTING THE SOLUTION	293
A. <i>An Upside Down Savings Cycle</i>	294
B. <i>Tax Expenditures</i>	297
C. <i>Housing</i>	299
D. <i>Education</i>	301
E. <i>Healthcare</i>	305
F. <i>Retirement Savings</i>	308
G. <i>The Value-Added Tax (the “VAT”) as a Second Income Tax</i>	313
H. <i>Congressional Ability to Keep Any Plan of Action</i>	315
I. <i>Return to the 1990s Budget Enforcement</i>	319
J. <i>Retirement and Health Care Planning is Challenging Even for the Experts</i>	320
K. <i>Will the 112th Congress Address the Debt Crisis?</i>	324
L. <i>Other Considerations</i>	327
M. <i>Preparation for the Next Emergency</i>	332
V. THE NEXT TWO YEARS	333
VI. THE ONE FUND SOLUTION: IT’S MY MONEY AND I NEED IT NOW!	340
VII. CONCLUSION.....	351

* Gordon T. Butler, JD University of Texas at Austin; LL.M. (Tax) New York University, Professor of Law, St. Thomas University School of Law, Miami, FL, and Member: The Florida Bar. The author expresses his appreciation to the University of Houston Business and Tax Law Journal for the opportunity to present this article at its symposium: “How Will We Pay?, Changing the Federal Tax System to Better Fund Social Entitlements.”

ABSTRACT

The thrust of the article is to look at several proposed solutions to the current debt crisis, the long term effects of which will be dominated by Social Security, Medicare, and Medicaid, and suggest that private accounts structured as presented in the One Fund Solution giving each individual a visible stake in their own future and some control over the use of their money is a concept that would make everyone a part of the solution to the debt crisis.

I. INTRODUCTION

My 2009 article, *American Paternalism and the One Fund Solution*,¹ argued that a long-term solution to the federal entitlement crisis was the establishment of private accounts providing each citizen a means to accumulate and use savings to cover major life events in investments, which would yield an annual return commensurate with GDP growth and be guaranteed against inflation and taxation loss by the federal government.² Contributions to such a fund would be mandatory, and withdrawals would be permitted for limited uses during the person's lifetime with the primary objective of providing a source of funds for medical and retirement and, subject to limitations, for housing, education, and other high priority uses.³ The fund would be administered by the Social Security Administration.⁴

The One Fund Solution is consistent with American Paternalism. American Paternalism is described as the uniquely American belief that government has an obligation to see that people unable to take care of themselves are provided governmental assistance, but that such assistance should be consistent with individual freedom of choice and should not be so large as to dominate every life decision.⁵ In fact, housing, health care, education, and retirement are dominated by the federal tax system and each area has seen the costs inflate beyond the reach of the average citizen, who has effectively lost decision making power over how the fruits of his life work should be used.⁶

Presently, an economic crisis has seized the nation with only limited prospects of a return to the pre-crisis normalcy. In fact,

1. See 9 WYO. L. REV. 485 (2009).

2. *Id.* at 540-41.

3. See *id.* at 523.

4. *Id.* at 524.

5. *Id.* at 488, 550.

6. See *infra* Part III.

projections of future economic conditions are so dire and threatening that every thinking person should engage himself in obtaining a better understanding of the situation and how it might affect him. Not only has massive government spending been used to address the crisis, it seems unlikely that the deficits such spending has created will ever be eliminated, or that the nation will return to a balanced budget.⁷

This economic crisis will soon be aggravated by the post-World War II baby boom generation, which is the generation born between 1946 and 1964.⁸ This group will reach age sixty-five in 2011, thereby qualifying for Medicare and a year later for full benefits under the Social Security system.⁹ This massive demand for funds and services coupled with the extreme expense of providing medical care for America's poor under the Medicaid system provide a challenge that cannot be carried out under current conditions. Without serious changes to these programs and the promises of the federal government, debt will consume the United States budget.

Numerous solutions to the spending side as well as the revenue-generating side have been proposed. One such effort was the President's bipartisan National Commission on Fiscal Responsibility and Reform ("Commission"), which President Obama created with the mandate to produce a report suggesting methods for bringing the deficit to a sustainable level by 2015.¹⁰ Other reports and suggestions have also been presented. The provisions of these proposals vary with respect to taxes and spending, but in many ways they keep the same level of government control over every major life decision. This paper examines the various aspects of these representative plans,

7. See generally CONG. BUDGET OFFICE, CBO'S 2011 LONG-TERM BUDGET OUTLOOK 1 (2011) [hereinafter CONG. BUDGET OFFICE, LONG-TERM BUDGET OUTLOOK]. Deficits have caused the federal debt held by the public to grow from 40% of GDP in 2008 to 62% of GDP at the end of 2010. *Id.* at 13. Under the extended-baseline scenario, annual deficits will decrease to 3% of GDP by 2014 and then continue at 3% to 4% of GDP, such that debt would grow to 84% of GDP by 2035. *Id.* This scenario creates long-term budget projections by extending the ten-year baseline concept based on current law under rules formulated originally under the Balanced Budget and Emergency Deficit Control Act of 1985. *Id.* at 2 n.2. The alternative fiscal scenario incorporates changes to current law that are widely expected to be made such as extending tax cuts originally enacted in 2001 and now extended through 2021. *Id.* at 2. Under the alternative fiscal scenario, federal deficits will decline for the next few years, but then will grow at a much faster pace such that federal debt held by the public will be 100% of GDP by 2021 and almost 190% by 2035. *Id.* at 4-7.

8. See CONG. BUDGET OFFICE, WILL THE DEMAND FOR ASSETS FALL WHEN THE BABY BOOMERS RETIRE? 1 (2009) (noting that between 1946 and 1964, some 78 million babies were born in the United States).

9. CONG. BUDGET OFFICE, LONG-TERM BUDGET OUTLOOK, *supra* note 7, at 37, 52.

10. Exec. Order No. 13,531, 75 Fed. Reg. 7927 (2010).

compares such aspects to similar aspects of the One Fund Solution, and concludes that the One Fund Solution offers a superior long-term solution to the entitlement crisis than other proposals.

Part one sets forth the dimensions of the crisis and emphasizes how our political leaders have led the nation into an uncertain area where there is danger of massive inflation and financial meltdown occurring at any time without advance warning. Part two examines the highlights of three comprehensive plans for addressing the debt crisis and one tax reform plan that will increase U.S. competitiveness. Part three explores a number of areas that must be addressed if a budget solution is to be achieved. Part four predicts that a solution is unlikely to occur before the next presidential election. Part five describes the One Fund Solution and how it reflects proposals that cherry pick the best of the proposals described in part three.

II. THE CURRENT FISCAL CRISIS

At the end of the federal government's fiscal year 1980, immediately before President Ronald Reagan was sworn in as the 40th President of the United States, the total national debt was just under \$1 trillion.¹¹ From that modest beginning, total federal debt, including the portion held by the public, grew dramatically over the next thirty years as follows:¹²

End of Fiscal Year	President Elected	Total Debt in trillions \$	Percent of GDP	Public Debt in trillions \$	Percent of GDP
1980	Ronald W. Reagan	\$0.9	33%	\$0.7	26%
1988	George H. W. Bush	\$2.6	52%	\$2.0	41%

11. OFFICE OF MGMT. & BUDGET, EXEC. OFFICE OF THE PRESIDENT, FEDERAL DEBT AT THE END OF YEAR 1940-2016, THE BUDGET FOR FISCAL YEAR 2012 HISTORICAL TABLES, 7.1 (2010), <http://www.whitehouse.gov/omb/budget/Historicals/>. Total debt of the United States includes total public debt plus intra-governmental holdings such as the treasury securities held by the OASI trust fund administered by the Social Security Administration. See CONGRESSIONAL BUDGET OFFICE, CBO'S 2011 LONG-TERM BUDGET OUTLOOK, *supra* note 7, at 52, 87. The Congressional Budget Office ("CBO") utilizes the measure of debt held by the public. See *generally* CONG. BUDGET OFFICE, FEDERAL DEBT AND INTEREST COSTS, 17-21 (2010).

12. OFFICE OF MGMT. & BUDGET, *supra* note 11, tbl. 7.1.

1992	William J. Clinton	\$4.0	64%	\$3.0	48%
2000	George W. Bush	\$5.6	57%	\$3.4	35%
2008	Barack H. Obama	\$10.0	69%	\$5.8	40%
2010	n/a	\$13.5	93%	\$9.0	62%
2011 est.	n/a	\$15.5	103%	\$10.8	72%
2016 est.	n/a	\$20.8	105%	\$15.1	76%

In thirty years, the national debt grew by a factor of \$13 to \$13.5 trillion.¹³ How long will it take to pay it off? The answer is that, without dramatic action by Congress, it is unlikely to be reduced in the twenty-first century. The White House estimates that debt will grow by \$3.769 trillion between 2012 and 2016 and an additional \$3.436 trillion by 2021.¹⁴

While there are many causes of this exploding debt, recent increases are the result of the subprime mortgage crisis, which began in 2007 and nearly caused a worldwide financial meltdown.¹⁵ This same crisis called for the bailing out of the banking system and continues to require assistance for homeowners whose mortgages exceed the value of their homes.¹⁶ This crisis also caused the United States to enter a recession, as unemployment numbers grew to 10% and called for economic stimulus that promised to reduce unemployment.¹⁷ Failing to do so, however, the recession resulted in significant revenue losses

13. CONG. BUDGET OFFICE, FEDERAL DEBT AND INTEREST COSTS 17-21 (2010).

14. OFFICE OF MGMT. & BUDGET, EXEC. OFFICE OF THE PRESIDENT, FISCAL YEAR 2012 BUDGET OF THE U.S. GOVERNMENT 1, 171 (2010). Debt increases indicated are taken from Table S-1 in the Summary Table attached to the budget. *Id.* at 169-71. These projections were made at a time when "none of the full-year appropriations bills for 2011 was enacted." *Id.* at ii (General Note 3).

15. CARMEN REINHART & KENNETH ROGOFF, THIS TIME IS DIFFERENT: EIGHT CENTURIES OF FINANCIAL FOLLY xxvii (2009).

16. *Id.* Reinhart and Rogoff address the U.S. subprime "meltdown" in great detail and compare it to similar events in the U.S. and other countries. *Id.* at 203-72.

17. CONG. BUDGET OFFICE, LONG-TERM BUDGET OUTLOOK, *supra* note 7, at 25.

in both 2009 and 2010.¹⁸ In addition, the United States financial crisis was experienced by developed countries world-wide.¹⁹

While the world is struggling to recover from the recession, it has become clear that these temporary debt increases are due to explode even further due of the uncontrollable growth of entitlement programs.²⁰ As the post-World War II baby boomer generation reaches age sixty-five in 2011 and begins claiming Medicare benefits at a rate averaging nearly 11,000 per day for the next nineteen years, they will also begin qualifying for full Social Security benefits a year later.²¹ While Social Security can be fixed with modest adjustments such as increasing the age for full retirement to age seventy, increasing the wage base subject to the Social Security tax to 90% of payroll (approximately \$180,000 today), or making the benefit indexes more realistic, no simple fix is available for Medicare and Medicaid.²²

To address this problem of exploding debt, President Obama, on February 18, 2010, appointed eighteen members to the Commission to study the debt problem and report on a plan to bring the debt under control by reducing the deficit to 3% of GDP

18. *Id.* Revenues as a percentage of GDP dropped to 14.9% in 2009, the lowest since 1950. David Roberts, *Is Tax Revenue Around 19 Percent of GDP Really a Law?*, 130 TAX NOTES 1076, 1078 (2011).

19. See REINHART & ROGOFF, *supra* note 15, at 206-08 (pointing out the suddenness of the crisis, placing it in a global perspective, comparing it to other crises, and calling it a “transformative moment in global economic history whose ultimate resolution will likely reshape politics and economics for at least a generation”).

20. PETER G. PETERSON, WILL AMERICA GROW UP BEFORE IT GROWS OLD: HOW THE COMING SOCIAL SECURITY CRISIS THREATENS YOU, YOUR FAMILY, AND YOUR COUNTRY 98-102 (1996) [hereinafter PETERSON, WILL AMERICA GROW UP] (explaining the 1972 shift to automatic cost of living increases and the one-time 10% increase in benefits). Since the early 1970s when automatic COLAs were introduced into the entitlement programs, Congress has been unable to make the annual decision as to the level of entitlement spending. *Id.* at 102-03.

21. *Id.* at 31-49. Peterson, an investment banker and former Secretary of the Commerce, was concerned about how Social Security would be able to handle seventy-six million baby boomers born between 1946 and 1964 that begin reaching age sixty-five in 2011. *Id.* at 22. Peterson called for a balanced budget by 2002. *Id.* at 158.

22. Senator Pete Domenici & Dr. Alice Rivlin, The Debt Reduction Task Force, *Restoring America's Future: Reviving the Economy, Cutting Spending and Debt, and Creating a Simple, Pro-Growth Task System*, BIPARTISAN POLICY CENTER, 72 (2010), <http://www.bipartisanpolicy.org/sites/default/files/BPC%20FINAL%20REPORT%20FOR%20PRINTER%202%2028%2011.pdf> [hereinafter Domenici & Rivlin]; see National Comm'n on Fiscal Responsibility and Reform, *Moment of Truth*, 6, 51 (2010), http://www.fiscalcommission.gov/sites/fiscalcommission.gov/files/documents/TheMomentofTruth12_1_2010.pdf [hereinafter *Moment of Truth*]; see also MICHAEL GRAETZ, 100 MILLION UNNECESSARY RETURNS 140-41 [hereinafter GRAETZ, UNNECESSARY RETURNS] (calling solving the retirement income problem “child’s play” when compared to solving the problem of providing the elderly with access to health care and long-term care).

by 2015.²³ This bipartisan Commission was established with the understanding that if its recommendations were approved by fourteen of its eighteen members, they would be submitted to an up or down vote in Congress.²⁴ The Commission issued its report with the affirmative vote of eleven members, including six of the twelve members holding elective office.²⁵

Recognizing that the failure to act on the exploding debt could devastate the country, the Commission entitled its report *The Moment of Truth*.²⁶ The Commission noted that “[i]n 2010 federal spending was nearly 24 percent of Gross Domestic Product (GDP),” the highest since World War II.²⁷ “Tax revenues stood at 15 percent of GDP, . . . the lowest level since 1950.”²⁸ The Commission also predicted that the rise in federal debt held by the public since 2001 could reach 90% of GDP by 2020.²⁹ As a result, revenues could only pay for Medicare, Medicaid, Social

23. Jeremy Scott, *Fiscal Commission Co-Chairs Target Tax Expenditures*, 129 TAX NOTES 753, 753 (2010). Scott states, “Bowles and Simpson call for heavy spending cuts, a restructuring of Social Security that lifts the cap on payroll taxes and raises the retirement age, and the elimination of all tax expenditures in the code. The last proposal would raise \$1.1 trillion annually, but almost none of that would go toward deficit reduction.” *Id.*

24. Exec. Order No. 13531, 3 C.F.R. 3-5 (2010); Sam Goldfarb, *Pelosi Appoints Final Three Members of Fiscal Commission*, 126 TAX NOTES 1578, 1578 (2010).

25. William M. VanDenburgh and Nancy C. Nichols, *Fiscal Commission’s Report Frames Budgetary Debate*, 130 TAX NOTES 447, 448-49 (2011). Interestingly, it appears that only one senator, Finance Committee Chair Max Baucus (D-Mont.) voted against it, and one House member, John M. Spratt Jr., (D-S.C.) voted for it. *Id.* at 449. Six Senate members and six Congressmen were part of the Commission. *Id.* Senate Majority Whip Richard Durbin (D-IL), Senate Budget Committee Chairman Kent Conrad (D-ND), Senators Tom Coburn (R-OK), Mike Crapo (R-Idaho) and Judd Gregg (R-NH) voted for the report, while Senator Max Baucus (D-Mont.) voted against it. *Id.* at 454. One Democratic Congressman, Representative Spratt of South Carolina, voted for the report, while two Democratic congressional members, Representatives Becerra of California and Schakowsky of Illinois and three Republican congressional members, Representatives Camp of Michigan, Hensarling of Texas, and Ryan of Wisconsin, voted against it. *Id.* The Commission’s co-chairs, former Republican Senator Alan Simpson and former White House Chief of Staff Erskine Bowles, supported the report. *Id.* Of the remaining four members, three supported the report. *Id.* These three members included Republican Dave M. Cote of Honeywell International, Inc., Alice Rivlin of Brookings Institution, and former director of the CBO and OMB and Vice President of the Federal Reserve Bank, Ann M. Fudge. *Id.* Andy Stern, former president of Service Employees International Union, voted against the report. *Id.* Republican Sen. Gregg did not run for reelection in 2010. Jeremy Scott, *GOP Victory Will Change Tone, But Not Substance of Tax Debates*, 129 TAX NOTES 654, 654 (2010). Democratic Congressman Rep. Spratt of South Carolina, who was the former House Budget Committee Chair, lost his 2010 reelection bid. See Drew Pierson, *Republicans Expect to See Tax Reform in Obama’s 2012 Budget*, TAX NOTES TODAY, Jan. 5, 2011, para. 16, <http://services.taxanalysts.com/taxbase/tnt3.nsf/Number/2011+TNT+3-1?OpenDocument&Login>.

26. See *Moment of Truth*, *supra* note 22, at 6-7.

27. *Id.* at 10.

28. *Id.*

29. *Id.* at 11.

Security and interest payments on the national debt by 2025.³⁰ The Commission described the critical nature of the situation as follows:

Predicting the precise level of public debt that would trigger such a crisis is difficult. But a key factor may be whether the debt has been stabilized as a share of the economy or if it continues to rise. Investors, reluctant to risk throwing good money after bad, are sure to be far more concerned about rising debt than stable debt. In a recent briefing on the risk of a fiscal crisis, CBO explained that while “there is no identifiable tipping point of debt relative to GDP indicating that a crisis is likely or imminent,” the US. Debt-to-GDP ratio is “climbing into unfamiliar territory” and “the higher the debt, the greater the risk of such a crisis.”³¹

Unfunded entitlements, outstanding war debt, and wasteful stimulus have brought the nation to a place where the current trend is unsustainable.³² Without significant action to curtail America’s debt, the country’s financial condition could face a devastating collapse. Economists can predict its coming but cannot predict the point at which the straw breaks the camel’s back. A recent two-part article by Martin A. Sullivan begins,

It is undeniable that we are on the path to fiscal collapse. This decline will occur in two stages. First there is the decay as the swelling national debt wears away the economy’s foundations and commits more and more future income to foreign creditors. We are already in stage one.

In stage two a lethal combination of phenomena arises in quick succession: greater default risk, looming inflation, higher interest rates, declining growth, financial market instability, and an acceleration of government borrowing. They feed on each other. The economy heads on a downward spiral. Between stage one and stage two there is a tipping point. Experts know it will come, *but nobody wants to predict when*. This article is about the slow economic

30. *Id.*

31. *Id.*

32. *Id.*

decline of stage one. Next week part 2 will describe the hell of a full-blown fiscal collapse.³³

Sullivan's articles argue that government debt, whether borrowed at home or abroad will, through a crowding-out effect, reduce domestic capital formation or ownership of domestic capital.³⁴ In either case, Americans' future well-being is reduced.³⁵ He notes three studies that have quantified the impact of government debt on long-term growth.³⁶ Using standard Congressional Budget Office figures, he projects a debt-to-GDP ratio in 2020 of 85%, that the debt-to-GDP ratio is increased to 97% when the effects of higher interest rates and lower growth rates are considered.³⁷ Sullivan predicts that the president's deficit reduction Commission will be of little help and that political polarization will result in inaction and gridlock until the 2012 elections.³⁸

In part 2 of his article, Sullivan points out that instability in the debt market could cause the debt-to-GDP to explode and that such a result would occur if the "primary balance," that is, the budget balance taking everything into account except for interest, remains in deficit as is currently the case.³⁹ Debt cannot rise infinitely because it will slow capital formation and economic growth; therefore, a second indicator is needed.⁴⁰ For

33. Martin A. Sullivan, *Fiscal Crisis, Part 1: The Slow Descent to Second-Class Status*, 129 TAX NOTES 499, 499 (2010) [hereinafter Sullivan, *Part 1*] (emphasis added). Sullivan cites several prestigious sources to the effect that the "tipping point" cannot be accurately predicted. *See id.* at 502.

34. *See id.* at 499.

35. *See id.*

36. *Id.* at 499-500.

37. *See id.* at 500. Sullivan also points out that large deficits and the corresponding expansion of debt affect government's ability and willingness to respond to economic crises, such as the current reluctance of the United States government to enact additional stimulus in the face of 9.6% unemployment. *Id.* at 501 (predicting the level of debt that will trigger an external debt default or restructuring is difficult); REINHART & ROGOFF, *supra* note 15, at 22-24 (stating that half of all defaults occur at debt levels below 60%, a fifth at debt levels below 40%, and only 16% at debt levels above 100%). Debt crises are also accompanied by falling GDP in the years preceding and the year of a debt crisis. *Id.* at 129-30. During a debt crisis, debt generally explodes partially due to efforts to recapitalize the banks, but mostly as a result of declining tax revenues caused by deep and prolonged output contractions. *Id.* at 224; *see* Leonard E. Burman, Jeffrey Rohaly, Joseph Rosenberg, & Katherine C. Lim, *Catastrophic Budget Failure*, 63(3) NAT'L TAX J. 561, 571 (2010).

38. Sullivan, *Part 1*, *supra* note 33, at 502.

39. Martin A. Sullivan, *Fiscal Crisis, Part 2: Catastrophe*, 129 TAX NOTES 647, 647 (2010) [hereinafter Sullivan, *Part 2*]. The idea is that debt that grows commensurately with GDP can be used to offset interest. *Id.* It is the stable debt-to-GDP ratio that is important. *Id.*

40. *Id.*

the debt-to-GDP to remain stable when interest rates are larger than the growth rate, the government must run a primary balance surplus.⁴¹ Sullivan points out that even with these mathematical conditions being met, there is a need for a great deal of faith in the financial markets not to push up interest rates, and under current policies, there is little to suggest that such hope is justified.⁴² In fact, Sullivan sees that there is a limit to politicians' willingness to cut spending or raise taxes to maintain the required stability.⁴³

While pinpointing that economic events are impossible, some commentators believe that when public debt exceeds 60% of GDP, a country is entering the "high risk" zone for budget failure.⁴⁴ Other danger points suggesting a "high risk" are when deficits exceed 3% of GDP, debt is primarily short term, and there is a need to continually roll the debt over.⁴⁵ If America is unable to sell its debt, both the U.S. and the world will face a financial meltdown, forcing the U.S. to close its 10% of GDP budget deficit in a crisis.⁴⁶ Closing such a budget gap would cause an immediate 10% to 25% drop in GDP and three years of inflation at 33% causing the worth of \$1 prior to the crisis to be worth \$0.01 after the crisis.⁴⁷

Such dire predictions may still be years away, providing an opportunity to put the U.S.'s economic house in order.⁴⁸ For over four decades, America has supported a liberal world order defended by the United States military.⁴⁹ America owes it to the

41. *Id.* at 647-48. This result is represented by the formula $PB - (i - g)D = 0$, where PB is the primary balance, i is the interest rate on government debt, g is the growth rate, and D is the accumulated debt. PB and D are expressed as ratio of GDP. *Id.* at 647.

42. *Id.* at 649.

43. *Id.* Sullivan points out that recent low-interest rates have resulted from inflow of savings from China and, even more recently, from the increase in savings from the worldwide recession and laments that these sources cannot be relied upon indefinitely. *Id.* at 650.

44. Leonard E. Burman et al., *supra* note 37, at 571 (remarking that the European Union requires members to have a debt to GDP ratio of less than 60%).

45. REINHART & ROGOFF, *supra* note 15, at xxv; *see also* Burman et al., *supra* note 37, at 572-73 and fig.6 (pointing out that \$2.5 trillion of U.S. public debt has maturity of less than one year as of March 2010). Ironically, current Federal Reserve Bank policy of purchasing \$600 billion of U.S. debt, known as qualitative easing, or QE2, is directed toward purchasing thirty-year debt, thereby causing debt held by others to be further weighted toward short term. *Id.* at 577.

46. *See* Burman et al., *supra* note 37, at 577 (providing mathematical analysis to show that closing a 10% budget gap would decrease output to Great Depression levels).

47. *Id.* at 575-79.

48. *Id.* at 579.

49. Domenici & Rivlin, *supra* note 22, at 95; *see* GRAETZ, UNNECESSARY RETURNS, *supra* note 22, at 23 (noting that America spends more on defense than all other nations combined). The United States spends twice the amount in terms of percentage of GDP on

rest of the world to live beyond recession. Many plans are being put forth to address the problem of exploding debt. Some of these will be explored in the next section.

III. RECENT PROPOSALS

A. *The Moment of Truth*

The Commission's report, "The Moment of Truth," adopts specific recommendations that promote growth, protect the disadvantaged, obtain productivity gains in Washington's activities, and reform and simplify the tax code.⁵⁰ The recommendations will reduce the deficit by \$4 trillion through 2020, reduce the deficit to 2.3% of GDP by 2015, reduce income tax rates, abolish the Alternative Minimum Tax, and cut back on tax expenditures. It will also cap revenues at 21% of GDP and get spending below 22%, ensure Social Security solvency, and stabilize the debt by 2014 and reduce it to 60% of GDP by 2023 and 40% by 2035.⁵¹ The major components of the recommendations include discretionary spending cuts, comprehensive tax reform, health care cost containment, mandatory savings, Social Security reforms to ensure long-term solvency and reduce poverty, and process changes.⁵² The following discussion will consider the Social Security, Medicare, Medicaid, and the tax system components.

The Commission looks at Social Security, both disability and retirement benefits, as "the keystone of the American social safety net."⁵³ Under current conditions, the system begins running annual deficits in 2015 excluding trust fund interest⁵⁴

military as any of its allies, and its total spending exceeds the total military spending of the rest of the nations combined. Domenici & Rivlin, *supra* note 22, at 94; GRAETZ, UNNECESSARY RETURNS, *supra* note 22, at 23.

50. *Moment of Truth*, *supra* note 22, at 12. The Commission viewed its mission in two parts: "to bring the budget into primary balance (balance excluding interest costs) in 2015, and to meaningfully improve the long-run fiscal outlook." *Id.* To achieve this mission, it set out ten separate "Guiding Principles and Values." *Id.* at 12-13.

51. *Id.* at 14.

52. *Id.* at 15-16.

53. *Id.* at 48.

54. *Id.* ("Although the system's revenues and expenditures are expected to return to balance temporarily in 2012, it will begin running deficits again in 2015 if interest from the trust fund is excluded . . ."). Since 1983, Social Security revenues have exceeded the amount of benefits paid out each year with the surplus being loaned to the federal government. ALLEN W. SMITH, THE LOOTING OF SOCIAL SECURITY: HOW THE GOVERNMENT IS DRAINING AMERICA'S RETIREMENT ACCOUNT 32-34 (2004). At some point in the future, these benefits will pay the money back to the trust fund with interest allowing for a future period when Social Security annual benefits will exceed revenues

and 2023 including interest with the trust fund being exhausted in 2037.⁵⁵ The Commission proposes to close the 1.92% of payroll seventy-five year shortfall projection, while doing more to reduce poverty among the very poor and very old.⁵⁶ First, the Commission proposes to make the benefit formula more progressive and provide an enhanced minimum benefit.⁵⁷ In addition to slowly extending the age for early and full retirement to sixty-four and sixty-nine by 2075 and raising the income base subject to the tax, the Commission would also provide a 5% enhancement of benefit for those living to age eighty-five to prevent a person from outliving his benefit and easier hardship claims for those requiring early retirement.⁵⁸ Interestingly, the Commission recommends a broad dialogue on the importance of encouraging private savings to supplement Social Security and provide some benefit for retirement and distribution to heirs at death.⁵⁹

The Commission views healthcare spending as the single largest long-term fiscal challenge primarily due to baby boomers' retirement, which will cause federal health care spending for

received. *Id.* at 35. Considerable debate has developed about whether the government will ever be able to repay the amount owed the trust fund and prevent benefits from being cut. *Id.* at 32-38; DEAN BAKER & MARK WEISBROT, SOCIAL SECURITY: THE PHONY CRISIS 22 (1999) (arguing that the system has already taken into account the retirement of the baby boom generation and will not have any problem through 2030). In general, benefit payments exceeded non-interest revenues in 2011 but not total revenues. BD. OF TRS., THE 2011 ANNUAL REPORT OF THE BD. OF TRS. OF THE FED. OLD-AGE AND SURVIVORS INS. AND FED. DISABILITY INS. TRUST FUNDS, H.R. DOC. NO. 112-23, at 2 (2011). In 2023, benefit payments will begin to exceed total revenues and will continue until 2038, when the trust fund will be exhausted. *Id.* at 3. Some commentators view repayment of the trust fund debt as while others assume there is no problem until the trust fund runs dry. See Charles Krauthammer, *Will Voters Buy Hoax That Is Social Security?*, INVESTORS BUS. DAILY, Mar. 11, 2011, at A15, available at <http://www.investors.com/NewsAndAnalysis/Article/565640/201103101838/Will-Voters-Buy-Hoax-That-Is-Social-Security-.aspx> [hereinafter Krauthammer, *Will Voters Buy Hoax*]; see also Alan D. Viard, *Social Security and the General Treasury: Who's Raiding Whom?*, 8 TAX NOTES 943, 943 (2011) (arguing that the trust fund will be repaid with interest but that various spending programs to supplement the income of persons paying Social Security taxes or receiving Social Security benefits have been paid through the general revenues thereby subsidizing Social Security).

55. *Moment of Truth*, *supra* note 22, at 48.

56. *Id.* The Social Security benefit formula is based on average lifetime income. *Id.* at 49. To determine an individual's benefit, add 90% of the first \$9,000, 32% of the next \$55,000, and 15% of the balance of the average lifetime income. *Id.* The proposed change would be determined by 90% of the first \$15,000, 30% of the next \$48,000, 10% of the next \$39,000, and 5% of the remaining average lifetime income. *Id.*; see generally FRANCINE J. LIPMAN & JAMES E. WILLIAMSON, SOCIAL SECURITY BENEFITS FORMULA 101: A PRACTICAL PRIMER, ABA SEC. OF TAX'N NEWS QUARTERLY 14 (2010).

57. *Moment of Truth*, *supra* note 22, at 49-50.

58. *Id.* at 50.

59. *Id.* at 53.

Medicare, Medicaid, Children's Health Insurance Program (CHIP), and the health insurance exchange subsidies to grow from 6% of GDP in 2010 to about 10% in 2035.⁶⁰ The Commission sees its projections as suspect because they reflect large "phantom" savings from the 23% Medicare physician payment cut that will never be put into effect and the unsustainable long-term care premiums for the Community Living Assistance Services and Supports Act (the "CLASS Act").⁶¹ The Commission proposes offsetting the physician payment cuts with other medical cuts and repealing or reforming the CLASS Act.⁶² Among the other Medicare changes is one to restrict first dollar Medicare gap insurance to require significant co-pays (e.g. the first \$500 plus one-half of the next \$5,000) and cut reimbursements for failure to collect co-pays.⁶³ Some Commissioners support a system of Medicare premium support, which includes restricting and eliminating states' ability to "game" the system.⁶⁴

The Commission's tax reform proposal, like many such proposals since 1986, would expand the tax base, lower the rates, and simplify the tax code. The target of the Commission's tax reform is the \$1.1 trillion tax expenditure budget reflecting numerous "spending" programs administered by the Internal Revenue Service that the Commission would severely limit to fund deficit reduction, significantly lower individual rates, and eliminate the Alternative Minimum Tax.⁶⁵

Tax expenditures retained include the most sacred of sacred cows such as mortgage interest and charitable deductions, which

60. *Id.* at 36.

61. *Id.* The Balanced Budget Act of 1997 included the Sustainable Growth Rate formula that would place limits on Medicare payments to physicians. *Id.* It was projected to save \$12 billion over the 1998-2007 period, but by 2002 the extent and complexity of physician payments accelerated and the required cuts in payment rates were much larger than expected. See Paul N. Van de Water, *The Sustainable Growth Rate Formula and Health Reform*, CENTER ON BUDGET AND POLICY PRIORITIES, Apr. 21, 2010, <http://www.cbpp.org/cms/index.cfm?fa=view&id=3166>. The result was that, since 2003, Congress prevented the full extent of the cuts from taking effect. See *Moment of Truth*, *supra* note 22, at 36. The CLASS Act established long-term care insurance as part of the 2010 Affordable Care Act (ACA). *Id.* at 37. Early beneficiaries pay a low premium but receive benefits many times larger such that the program will be in need of benefit reductions or premium increases that would make the program unattractive. *Id.*

62. *Id.* at 36-37.

63. *Id.* at 38.

64. *Id.* at 39-40.

65. See *id.* at 28. The Commission's plan provides three alternatives addressing tax reform. *Id.* at 29, fig.6. The alternative discussed here is the alternative that eliminates all tax expenditures with the savings being used to fund lower rates, except for \$80 billion in 2015 to deficit reduction. *Id.* at 29-30, 31 fig.7. This seems the most compelling solution.

will be converted to 12% tax credits limited to the interest only on a primary residence up to interest on a \$500,000 mortgage and charitable contributions above 2% of Adjusted Gross Income.⁶⁶ The exclusion for employer-provided health care is capped at a 75th percentile in 2014, frozen until 2018, and then eliminated by 2038.⁶⁷ The deduction for state and local taxes is eliminated, contribution limits on retirement accounts are limited to the lower of \$20,000 or 20% of income, the savers credit is expanded, and tax treatment of employer pensions remains the same as current law.⁶⁸ The EITC and the Child Credit are retained.⁶⁹ Most other tax expenditures are eliminated.⁷⁰ Individual rates are reduced to 12%, 22%, and 27%.⁷¹ Corporate tax rates are reduced to a flat rate between 23% and 29% with most tax expenditures eliminated.⁷² For the most part, the savings from elimination of tax expenditures is used to reduce rates rather than cut spending, leaving the bulk of deficit reduction to come from spending cuts.⁷³

Finally, the Commission recognizes that process reforms are necessary if any deficit reduction plan is to be effective.⁷⁴ One item is to gauge all federal programs to the “chain-weighted” Consumer Price Index for Urban Consumers, which more accurately adjusts prices for the manner in which consumers react to price changes.⁷⁵ In addition, a debt stabilization process would require the budget to be in primary balance after 2015 and authorize fast track procedures to insure compliance with the standards.⁷⁶ The Commission recommends changes to the

66. *Id.*

67. *Id.* The 40% excise tax on high cost plans (generally \$27,500 for families) that begins in 2018 is reduced to 12%. *Id.*

68. *Id.*

69. *Id.* (indicating that the current \$1,000 partially refundable child credit and the EITC of between \$457 and \$5,666).

70. *Id.* Interestingly, the tax incentives for education are not addressed by the Commission. *See id.*

71. *Id.* at 31 fig.7.

72. *Id.* at 32-33.

73. *See* Jeremy Scott, *Fiscal Commission Co-Chairs Target Tax Expenditures*, 129 TAX NOTES 753, 753 (2010) (suggesting that “everyone knows that at least some tax expenditures are untouchable”). Scott takes issue with critics who suggest the plan is a tax cut for the rich, pointing out that limiting the tax expenditure for mortgage interest and taxing capital gains and dividends certainly do not favor the high income taxpayers. *Id.*

74. *Moment of Truth*, *supra* note 22, at 16, 56-58 (recommending reforming the budget process to ensure the debt remains on a stable path, spending is capped, inflation is measured accurately, and other similar controls).

75. *Id.* at 56.

76. *Id.* at 56-57.

scoring methods and automatic triggers for unemployment benefits.⁷⁷

B. *Bipartisan Policy Center Plan*⁷⁸

On November 17, 2010, the nineteen-member Debt Reduction Task Force (“Task Force”) co-chaired by Senator Pete Domenici and economist Dr. Alice Rivlin,⁷⁹ issued its report, *Restoring America’s Future: Reviving the Economy, Cutting Spending and Debt, and Creating a Simple, Pro-Growth Tax System*. Like other plans, the Task Force recognizes the twin objectives of facilitating recovery from the recession and of addressing the unsustainable debt situation.⁸⁰

Both objectives are interdependent and thus any action must address them simultaneously.⁸¹ Addressing the recession and unemployment, the Task Force recommends a one-year “payroll tax holiday” that will cut taxes by almost \$650 billion and immediately add money to every employee’s paycheck, while reducing costs for employers and encouraging them to hire new workers.⁸²

Addressing the unsustainable debt situation is a long-term challenge. The Task Force proposes, as a first step, to balance the “primary budget,” which is the budget less interest payments, by 2014.⁸³ Second, its proposal will reduce the Debt-to-GDP ratio

77. *Id.* at 58.

78. The Bipartisan Policy Center was founded by former Senate Majority Leaders Howard Baker (R-TN), Tom Daschle (D-SD), Bob Dole (R-KS), and George Mitchell (D-ME). Domenici & Rivlin, *supra* note 22, at 2.

79. *Id.* at 2-3. The membership of the task force reflects broad leadership experience and diverse political views. *Id.* at 4-7. Thus, Domenici & Rivlin purport to reflect significant compromise across political lines. *Id.* at 8. The report states:

The Task Force members are former White House and Cabinet officials, former Members of Congress, former governors and mayors, business and labor leaders, economists and budget experts. They are Democrats, Republicans, and Independents. They are Americans from across the country, with widely diverse views about public policy and the role of government.

Id. at 9.

80. *Id.* at 8. For Domenici & Rivlin, the Task Force’s goals are to “recover from the deep recession that has thrown millions out of work, slashed home values and closed businesses across the country . . . [and to] take immediate steps to reduce the unsustainable debt that will be driven by the aging of the population, the rapid growth of healthcare costs, exploding interest costs, and the failure of policymakers to limit and prioritize spending.” *Id.*

81. *Id.*

82. *Id.* at 9. This would not result in a loss to the Social Security “trust fund,” since the fund would be credited with an amount equal to the loss of revenues. *Id.* at 26.

83. *Id.* at 10.

by 60% by 2020.⁸⁴ Also, by 2020, federal spending will be 23% of GDP, down from current 26%, and revenues will be at 21.4%, above the historical standard of 18%.⁸⁵

Furthermore, even using the Task Force's "moderate" assumptions, interest on the national debt is predicted to grow to \$1 trillion by 2020.⁸⁶ Interest payments at that level could produce a "death spiral" of increasing debt with increasing interest payments, which is a particularly disturbing projection since governments will hold a large portion of the debt that are not particularly supportive of U.S. interests.⁸⁷

The Task Force is aware that the debt crisis cannot be solved simply by cutting domestic discretionary spending, eliminating waste, fraud, and abuse, or raising taxes on high income Americans.⁸⁸ The problem is that "the actions needed to reduce the growth of the national debt and bring deficits back to manageable levels are all unpopular."⁸⁹ The Task Force proposes saving \$5.866 trillion from 2012 to 2020, which would include spending reductions of \$2.677 trillion, \$1.873 trillion in tax expenditure cuts, \$435 billion from increased revenues, and \$877 billion in total debt service savings.⁹⁰

Spending reductions to achieve these goals include freezing domestic discretionary spending and defense discretionary

84. *Id.* at 9-10. There is authority stating that historically, a debt to GDP ratio below 60% did not insure against debt crisis. *Id.* at 27 (citing REINHART & ROGOFF, *supra* note 15, at 24). Japan, which has experienced twenty years of fiscal stagnation, has a proposed 2011 deficit of 10% of GDP. Martin A. Sullivan, *Japan Cuts Corporate Rate, Puts Austerity on Hold*, 130 TAX NOTES 19, 20-21 (2011). For 2010, the IMF has estimated that the total debt will equal 130% of GDP, twice that of the United States. *Id.*

85. Domenici & Rivlin, *supra* note 22, at 16 (explaining how federal spending will be reduced); see also CONG. BUDGET OFFICE, LONG-TERM BUDGET OUTLOOK, *supra* note 7, at 14 (stating that federal revenues over the past forty years have averaged 18% of the GDP). This report further projects that by 2025, major entitlements and interest will consume all revenues. Domenici & Rivlin, *supra* note 22, at 12.

86. Domenici & Rivlin, *supra* note 22, at 11-12, 24.

87. *Id.* at 12-13. The Task Force's plan notes that the allocation of funds for the 2010 federal budget included 21% for Medicare and Medicaid, 20% for Social Security, 20% for defense, 17% for other mandatory spending, 6% for interest, and 16% for everything else including veterans' health care, homeland security, education and student aid, roads, energy, environment, and other items. *Id.* at 13-14. In light of the fact that the U.S. has never had more than a 4.4% growth in any decade since World War II, the economy most likely will not grow its way out of the deficit problem because it would take 6% annual growth for ten years to do so. See *id.* at 14. While increased debt will reduce productivity and endanger America's future, at some point America's creditors could lose confidence in its commitment to paying its debt, plunging the value of the dollar and "trigger[ing] runaway inflation and still higher interest rates in a potentially never-ending vicious cycle." *Id.* at 24.

88. *Id.* at 14.

89. *Id.* at 2.

90. *Id.* at 21.

spending for four and five years, respectively, and cap increases thereafter to the rate of GDP growth.⁹¹ Freezing the spending will force Congress to make decisions as to which programs are absolutely necessary and which can be eliminated or reduced.⁹² Other programs proposed to reduce spending would include cutting agriculture, reforming civilian and military pensions, raising or beginning to charge fees for certain services, and making various programs actuarially sound.⁹³ Finally, appropriate caps with effective enforcement need to be implemented to ensure compliance.⁹⁴

The Task Force states that “[b]y any reasonable standard [Social Security] has been the most successful antipoverty program in the nation’s history.”⁹⁵ The Social Security program provides both Old-Age and Survivors Insurance (OASI) and Disability Insurance (DI),⁹⁶ and Domenici & Rivlin recognize that its importance

in maintaining the economic well-being of elderly and disabled Americans cannot be overstated. According to the Social Security Administration (SSA), in 2008, Social Security benefits constituted 36.5 percent of total income for the elderly. A majority of aged beneficiaries attributed more than one-half of their income to benefits. Even more striking is the fact that a significant share of the elderly population (21 percent of married couples and 43 percent of unmarried individuals) relied on Social Security for the least 90 percent of their incomes. As such, Social Security has been a major force in reducing the elderly poverty rate from over 35 percent in 1959 to less than 10 percent in 2009 (SSA).⁹⁷

91. *Id.* at 19, 85-86, 95-105.

92. *Id.* at 92.

93. *Id.* at 19, 108-18.

94. *See id.* at 84-93 (noting current spending levels for federal programs and noting the importance to prioritize spending in applying the four-year freeze). Domenici & Rivlin describe a similar analysis for the freeze on defense spending. *Id.* at 94-105.

95. *Id.* at 70 (quoting President Franklin Roosevelt as stating: “[w]e can never insure one hundred percent of the population against one hundred percent of the hazards and vicissitudes of life, but we have tried to frame a law which gives some measure of protection to the average citizen and his family against the loss of a job and against poverty-ridden old age”).

96. *Id.*

97. *Id.* at 70 n.36.

Even though the proposals will increase revenues for both OASI and DI, the Task Force addresses OASI primarily leaving DI to be addressed in greater detail later.⁹⁸

Social Security would be strengthened to pay benefits over the next seventy-five years through modest benefits reductions and enhanced revenues.⁹⁹ Benefit reductions include adopting a more accurate cost of living index,¹⁰⁰ index benefits for longevity growth,¹⁰¹ and a “slight” reduction in the benefit replacement percentage for the top 25% of recipients from 15% to 10% over thirty years.¹⁰² Revenue increases are accomplished through broadening the payroll base subject to FICA tax over the next thirty-eight years to an amount that would cover 90% of all wages¹⁰³ (in current dollars from \$106,800 to about \$180,000)¹⁰⁴ and expanding coverage after 2020 to all state and local workers.¹⁰⁵ Revenue from the Social Security tax will also increase from phasing-out the exclusion from gross income of

98. *Id.* at 72-73.

99. *Id.* at 18-19, 72.

100. *Id.* at 75 (suggesting that the current measure, the Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W) which overstates inflation, be replaced with the “chain-weighted” Consumer Price Index for All Urban Consumers (CPI-U) which is estimated to grow 0.3 percentage points slower than the CPI-W).

101. *Id.* at 77 (explaining that the longevity index will commence in 2023 and reduce the benefit each year by 0.3%, which offsets about two-thirds of the additional cost associated with increased longevity). It will keep constant the ratio of estimated years in retirement to years of adult life prior to normal retirement. *See id.* at 77-78.

102. *Id.* at 76.

103. *Id.* at 74 (proposing to increase the Social Security wage base to 90% of income). However, such a proposal is not without its critics. *See* Mark J. Warshawsky, *The Fairness of Recent Social Security Tax Proposals*, 130 TAX NOTES 929, 930-31 (2011) (pointing out that such a proposal would unfairly shift the burden to middle-income taxpayers because recent income increases were weighted heavily for income earners above \$200,000). Warshawsky states,

The asymmetric pattern of earnings growth since 1983 has meant that those just above the current-law cap on earnings taxable wages are already carrying increased burdens to finance Social Security. Further raising the cap on taxable wages would simply target additional tax increases on those who have already been hard hit.

More broadly, any increase in payroll taxes will lead to a decline in retirement savings. This would be a bad outcome given our nations’ need to increase the domestic savings rate to finance the installation of productivity improving capital in our business, and to lessen our dependence on foreign sources of finance.

Id.

104. *See* Domenici & Rivlin, *supra* note 22, at 74 (noting that, upon retirement, the higher tax paid will return some additional benefits for those working in the form of a slightly higher benefit, which reflects the principle that workers get at least some return on all taxes paid).

105. *Id.* at 79.

employer-provided health insurance and other tax reform proposals.¹⁰⁶

The Task Force does not propose any change in the retirement age for early or full benefits.¹⁰⁷ Educating workers of the advantages of staying in the work force is another core objective of the Task Force that would reduce the Social Security burden and enhance the worker's overall retirement income.¹⁰⁸ Further, it does not propose an increase in the FICA tax rate; however, due to the particular difficulties with DI, the Task Force proposes an increase in the proportion of FICA allocated to DI, as well as an increase in minimum benefits for low-wage earners.¹⁰⁹

Health care costs have been growing at a rate that is 2% above GDP growth, and U.S. health care costs exceed that of other advanced countries who achieve comparable results.¹¹⁰ To begin controlling health care costs, the Task Force recommends the gradual elimination, over a ten year period, of the exclusion for employer provided health benefits beginning in 2018.¹¹¹ This action, it believes, will force health insurance purchasers to make cost-conscious decisions, whereas the current system contains few incentives to use efficient providers.¹¹² Elimination of the exclusion may result in employers dropping health insurance for employees, but this concern is alleviated to some extent by the ACA, which creates insurance exchanges with subsidies for individuals with incomes between 133% and 400% of the poverty line.¹¹³

Controlling the costs of Medicare involves four short-term changes: raising Medicare Part B premiums from 25% to 35% of

106. *Id.* at 72.

107. *See id.* at 78-79 (noting that indexing for longevity has the same effect as changing the retirement age).

108. *See id.* at 82-83 (noting that keeping workers in the work force will increase overall production and increase the resources workers would have when they retire).

109. *See id.* at 16-17; *see also id.* at 80 (proposing a minimum benefit beginning in 2012 of 133% of federal poverty level with thirty years of creditable experience and a 1% increase in monthly benefits each year from age eighty-one to eighty-five).

110. *Id.* at 44.

111. *Id.* at 47 (indicating that the exclusion encourages higher national health spending, leads to large revenue losses by the federal and state governments, and favors high income taxpayers who are more likely to have employer-provided health insurance). This proposal is the Task Force's major demand side strategy. *Id.* at 45. It would replace the excise tax instituted under the ACA and disallow any further contributions to Health Savings Accounts (HSAs). *Id.* at 48-49.

112. *Id.* at 47 ("The effect of the subsidy is to make private health care more expensive, which increases spending in Medicare, Medicaid and other public programs. . . .").

113. *See id.* at 48, 50.

program costs over five years, increasing rebates from pharmaceutical companies, modernizing Medicare's co-payment structure, and bundling Medicare's payments for post-acute care.¹¹⁴ In the long-term, the Task Force would convert Medicare to a "premium support" in 2018, using 2017 support levels that would not be permitted to grow faster than a five-year moving average plus 1%.¹¹⁵ Historically, such costs have risen 1.7% above GDP growth.¹¹⁶ If costs grow faster than rate of Medicare increases, then participants would pay the difference or chose a less expensive plan provided by Medicare exchanges.¹¹⁷ Individuals with the lowest incomes will not be affected by the changes to Medicare, since their premiums will be paid by Medicaid.¹¹⁸

Medicaid in the short term would be made subject to managed care principles as a cost-saving measure.¹¹⁹ In the longer term, the Task Force is proposing the implementation of cost containment incentives to get the government to decide Medicaid costs.¹²⁰ Under current practices, states and federal government work at cross purposes in an attempt to shift the costs to the other party.¹²¹ The result has been to allow Medicaid costs to become the fastest growing component of the health care field, and one that is pushing the states to the point of insolvency.¹²² The point of the proposal is to clearly allocate authority between the federal government and the states and let

114. *Id.* at 51-54.

115. *Id.* at 58.

116. *Id.* at 55 (recognizing that premium support can create a choice between traditional Medicare or a new private plan offered on a federal Medicare Exchange that may offer lower premiums). Sharing the cost may also be an option to reduce costs proposed by the Task Force:

Asking beneficiaries to pay more for their Medicare coverage (or shift to a lower-cost plan) mirrors what has happened in private insurance over the past decade, with increases in patient cost-sharing to keep premium growth from exceeding income growth by too large a margin. Employers have generally opted to increase patient cost-sharing rather than increase the percentage of the premium that employees contribute. The former keeps employees enrolled in the plan and encourages more judicious use of health services.

Id. at 56.

117. *Id.*

118. *Id.*

119. *Id.* at 57-59 (proposing to remove barriers so that persons who are eligible for both Medicare and Medicaid will be able to enroll in managed-care programs).

120. *Id.* at 60-65.

121. *Id.* at 60-61 (describing the background of federal and state incentives that began to diverge in 1980 such that states sought to push the costs of Medicaid onto federal government and vice versa).

122. *Id.* at 64 (pointing out that the federal-state conflict has resulted in providing incentives for Medicaid costs to grow faster than if one party were responsible for managing program costs).

each government take action to control costs.¹²³ This proposal is presented as one way to reduce the annual growth rate of Medicaid by 1%.¹²⁴ Other reforms such as medical malpractice reform or imposing an excise tax on the manufacture or importation of sugar or high fructose sweetened beverages are other suggestions the Task Force put forth to reduce health care costs.¹²⁵

This tax reform is intended to create a simple, pro-growth tax system.¹²⁶ It eliminates most deductions and credits and uses the savings to reduce the rates for individuals from current rates that currently rise as high as 35% down to the two rates of 15% and 27%; for corporations, the rate decreases from 35 to 27%.¹²⁷ The mortgage interest and charitable contribution deductions would be replaced with refundable 15% tax credits.¹²⁸ The tax credit on mortgage interest is limited to \$25,000 in interest on a primary residence and is paid directly to the lender.¹²⁹ Qualified charities would receive a grant of \$15 for every \$85 in donations.¹³⁰ Thus, the taxpayer does not need to file a return to receive the benefit of these credits.

Changes to the mortgage interest and charitable deductions favor low-income taxpayers while reducing the benefit to higher income taxpayers.¹³¹ Other benefits to assist low-income taxpayers include replacing the current Child Tax Credit and Earned Income Tax Credit (EITC) with a universal child tax credit of \$1,600 and an earnings credit of 21.3% of the first \$20,300 of earnings for each worker to be prepaid through automatic adjustments to the taxpayer's withholdings.¹³²

123. *Id.*

124. *Id.* (noting the need to eliminate the conflict between states and the federal government seeking to shift costs to the other party while recognizing the potential of Medicaid to push the states to insolvency).

125. *Id.* at 17-18.

126. *Id.* at 16-17.

127. *Id.* The major tax reform proposals and the tax expenditures that are proposed to be retained are summarized in Exhibits A and B, respectively. *Id.* at 126-28. Because of the simplification of the tax system, only 50% of the tax units would be required to file a return. *Id.* at 127.

128. *Id.* at 33-34.

129. *Id.* at 33 (noting that most tax incentives act as "upside down subsidies" in that they benefit high-income taxpayers because the benefit increases as the taxpayers marginal tax increases). The authors note that even the deduction for state and local sales, income, and property taxes would be eliminated. *Id.* at 34.

130. *Id.*

131. *Id.* (emphasizing that these provisions will likely increase home ownership and may benefit charities favored by low-income taxpayers).

132. *Id.* at 35.

Recognizing the “bewildering” variety of tax-favored plans that support retirement savings, the Task Force repeals them all but allow individuals and employers a combined contribution limit of 20% of earnings up to a maximum of \$20,000 annually.¹³³ Wealthy individuals would no longer be allowed to build up tax free retirement assets, and individuals in the 15% tax bracket would get a refundable tax credit.¹³⁴

These changes would include (1) repeal of the Alternative Minimum Tax; (2) elimination of the standard deduction and the personal exemption; (3) taxation of capital gains and dividends as ordinary income with a \$1,000 exclusion for capital gains; and (4) using a more accurate measure of inflation for adjusting the Tax Code.¹³⁵ Educational tax incentives would be repealed but could be replaced by grants through the Department of Education.¹³⁶

The series of changes already mentioned would simplify the Tax Code but would not raise revenues sufficient to curtail the debt, as demands for healthcare and retirement needs rise to support an aging population.¹³⁷ To meet this need, the Task Force would institute a “Debt Reduction Sales Tax” (DRST) of 6.5% to “reduce the debt and secure America’s economic future.”¹³⁸ The DRST is a credit-invoice type VAT that would tax about 75% of all personal consumption but would exempt

Government services, services produced by charitable organizations, educational activities, the imputed value of financial services . . . and government subsidies to health care [*e.g.* Medicare and Medicaid expenses]. Housing rents will be untaxed, but sales of new homes and rental properties will be taxable. All other consumer goods and service, including privately funded

133. *Id.* at 37.

134. *Id.* (stating that the remaining plan would allow a build-up of funds to purchase an annuity to replace a significant part of pre-retirement earnings). Under IRC § 25B, a 50% savers credit is granted for contributions to retirement savings plans up to \$2,000. I.R.C. § 25B(a) (2006). For joint return filers, it is phased out for taxpayers with incomes greater than \$30,000 and completely eliminated for taxpayers with incomes above \$50,000. *Id.* § 25B(b)(1).

135. *Id.* at 30.

136. *See id.* at 36.

137. *Id.* at 38-39 (recognizing that while the proposed reforms will make a fairer and more efficient tax system by broadening the income tax base, lowering the rates, and strengthening provisions for low- and moderate-wage working families and retirees, they do not provide revenues to lower debt or support a growing number of retirees).

138. *Id.* at 17. Even though consumption taxes generally are regressive the task force believes other changes proposed will make its overall proposal more progressive. *See id.* at 31 n.7.

healthcare costs, food and beverages, clothing, legal and accounting services, and many other items not typically captured by state retail sales taxes, will be included in the tax base.¹³⁹

The Task Force also recognizes that the budget and its enforcement process must be reformed with rigid limits on exempt emergency spending and strict enforcement by the Office of Management and Budget to keep expenditures within the caps and enforce pay-as-you-go (“PAYGO”) standards.¹⁴⁰ Combined, these actions would reduce the deficit by \$84 trillion from 2012 to 2040.¹⁴¹

C. *The Roadmap for America’s Future*

On January 27, 2010, Congressman Paul D. Ryan (R-WI) issued an update of his 2008 comprehensive evaluation of America’s economic future, which provides his alternative to the government-centered ideologies prevailing in Washington.¹⁴² Entitled “A Roadmap for America’s Future,” the proposal has three key objectives: providing health and retirement security, lifting the debt burden, and promoting American job creation and competition.¹⁴³ Congressman Ryan sees the current fiscal path of the Federal Government as unsustainable in that it will lead to spending, deficits, and debt that will overwhelm the budget, weaken America’s competitiveness, and threaten the survival of the government’s major benefit programs.¹⁴⁴

139. *Id.* at 40 (pointing out that the proposed DRST would follow countries like Australia, Canada, and New Zealand, which recently adopted broad based VATs instead of countries like the United Kingdom and France, which had adopted the tax earlier and had tax bases that were “riddled with exceptions”).

140. *Id.* at 119-21 (noting the success of the Budget Enforcement Act of 1991 in mandating across-the-board cuts in spending when preset limits were exceeded except when the President and Congress deemed an emergency existed).

141. *Id.* at 21 (showing that the savings include an additional \$24 trillion in tax revenues, \$26 trillion in spending policy reductions, and \$34 trillion in debt service savings).

142. Paul D. Ryan, *A Roadmap for America’s Future Version 2.0; A Plan To Solve America’s Long-Term Economic and Fiscal Crisis*, i (2010), <http://www.roadmap.republicans.budget.house.gov/Plan/> [hereinafter *Roadmap*].

143. *Id.* at iii.

144. *Id.* at 13-15 (seeing America as having reached the “tipping point,” which, if present policies are continued, the country will be unable to change course and return to traditional values of self-reliance, family, faith, and community). Ryan finds recent programs, such as the \$787 billion stimulus, the December 2009 \$150 billion addition, the TARP extension into the automobile and insurance company bailouts, and new housing programs, cap and trade, financial market regulation, and health care reform, needlessly increase the deficit and create unwise policy. *Id.* at 3-6.

For several decades, fiscal experts have warned of the untenable and overwhelming nature of the Federal Government's budgetary trends. The threat comes entirely from domestic entitlement programs, as clearly reflected in a report by the Congressional Budget Office.¹⁴⁵ The report, looking forward seventy-five years, shows that within the next several decades, the government's current fiscal path will lead to catastrophic levels of debt, even if Congress imposes substantial tax increases.¹⁴⁶

The Roadmap's major components include Social Security, Medicare, health care, tax reform, and job training. Its objective is to move away from "progressive" ideology of growing personal dependency on government for basic needs toward a restoration of national character rooted in individual initiative, entrepreneurship, and opportunity consistent with the realities of the 21st century.¹⁴⁷ While some commentators see Social Security as a modest problem that is years away,¹⁴⁸ Congressman

145. CONG. BUDGET OFFICE, LONG-TERM BUDGET OUTLOOK, *supra* note 7, at 7.

146. *Roadmap*, *supra* note 142, at 9-10 (outlining the economic parameters that will lead to the debt crisis, such as the CBO projection that by 2033 the fiscal gap, or revenue shortfall, will equal 5.4% of GDP). The Roadmap continues:

Unfunded Liabilities. Another way of viewing the government's disastrous budgetary situation is by looking at its fiscal position the way a private company would. To do so, analysts focus on the "Unfunded liabilities" of the Federal Government's major benefit programs. . . . The problem is most acute in Medicare. Like Social Security, Medicare faces the daunting demographic challenge of supporting the baby boomers as they retire. But its much larger problem is that of medical costs, which are rising at roughly double the rate of growth in the economy. Today Medicare has an unfunded liability of \$38 trillion over the next 75 years. . . .

Id. at 10-11. The unfunded, seventy-five year Social Security liability is currently at \$5 trillion, but by 2014 the numbers will be \$43 trillion for Medicare and \$14 trillion for Social Security. *Id.* at 21.

147. *Id.* at 3 ("But over time, Americans have been lured into viewing government — more than themselves, their families, their communities, their faith — as their main source of support; they have been drawn toward depending on the public sector for growing share of their material and personal well-being.").

148. See, e.g., Mark Miller, *It's Time to Protect Social Security*, AARP THE MAGAZINE, Sept./Oct. 2011, <http://www.aarp.org/work/social-security/info-08-2011/protect-social-security.5.html>. Mr. Miller states:

Th[e] debate [over Social Security's financing] . . . links Social Security to the ballooning federal deficit, although the program plays no direct role in the nation's debt and currently enjoys an enormous surplus. . . . So, what's the problem? . . . [T]he system is bracing for a wave of boomer retirements that, combined with today's longer life spans, will exhaust the program's surplus funds over the next 25 years. At that point, Social Security would have only enough funds from current revenue to pay out about 75 cents on every dollar of promised benefits. . . . Here's the good news: There's time to implement small changes that can put Social Security in balance for the long term. Think of Social Security as a gigantic battleship that turns slowly: the sooner we start making adjustments, the smaller the required changes.

Ryan sees it as a current problem that will grow worse as years pass.¹⁴⁹ As the Social Security system begins paying out more than it takes in, the system will begin drawing on the general revenues to redeem the debt owed the Social Security trust fund, which can only be provided if programs are cut, taxes are raised, or deficits are increased.¹⁵⁰ Today, life expectancies approach eighty years, and people are retiring at age sixty-four years compared to 1945 when life expectancy approached sixty-five years, and people were retiring at seventy years.¹⁵¹

Under the *Roadmap*, Social Security would remain the same for individuals age fifty-five and older, but workers younger than fifty-five would have an option to invest a portion of their Social Security taxes in personal retirement accounts that would have the contribution guaranteed against loss even after inflation by the federal government.¹⁵² The amount permitted to be invested in private accounts gradually increases from 2% of the first \$10,000 of annual payroll and 1% of payroll above that amount up to the Social Security earnings limit.¹⁵³ The maximum contribution gradually increases so that by 2042, the percentages will be 8% on an inflation adjusted level and 4% percent on payroll above that level.¹⁵⁴ The personal accounts will become the property of the owner and can be passed on at death. The *Roadmap* concludes:

Id. at paras. 1, 3-5. Miller continues by noting that the shortfall looks scary, but Social Security isn't unaffordable in the context of the huge U.S. economy. *See id.* para.2. Closing the projected shortfall in Social Security includes raising revenue (lifting the wage cap from \$106,800 to \$190,000 to closer 31% of the gap or raising the rate from 6.2 to 6.7% to eliminate about 50% of the gap) or adjusting benefits (raising the retirement age to seventy by 2040 to close almost 65% of the gap or indexing the benefits for longevity by paying lower benefits as average life expectancy increase to close 21% of the gap). *Id.* paras. 9-13.

149. *Roadmap*, *supra* note 142, at 32-33. "For several decades, fiscal experts have warned of the untenable and overwhelming nature of the Federal Government's budgetary trends. The threat comes entirely from domestic entitlement programs . . ." *Id.* at 7. "The longer that policy action on the budget is put off, the more costly and difficult it will be to resolve the long-term budgetary imbalance." *Id.* at 22; GRAETZ, UNNECESSARY RETURNS, *supra* note 22, at x (stating that once our economy recovers and resumes real growth, both substantial reductions in anticipated government spending and tax increase will be necessary to address this looming disaster. The first major tax-policy challenge of the twenty-first century has become the need to address the nations' unsustainable fiscal condition.); *see* Domenici & Rivlin, *supra* note 22, at 71.

150. *See generally Roadmap*, *supra* note 142, at iii-vii (pointing out that to pay benefits that exceed revenues, the government will either cut other programs, raise taxes, cut Social Security benefits, or run ever larger deficits).

151. *Id.* at 56.

152. *Id.* at v.

153. *Id.* at 54.

154. *Id.* The *Roadmap* suggests using a form of "progressive" indexing which is a combination of wage and price indexing. *Id.* at 55.

The benefits of personal accounts are tilted in favor of low-income individuals who do not have disposable income to invest. As a result, these individuals will be able to join the investor class for the first time. As Social Security benefits become an individual's property, the government no longer will be able to raid this money to pay spending on other programs.¹⁵⁵

The Roadmap guarantees a Social Security benefit of not less than 120% of federal poverty level and 150% if the beneficiary participates in the option to invest a portion of his contribution in private accounts.¹⁵⁶ Furthermore, currently the initial benefit is based on "wage indexing,"¹⁵⁷ but the Roadmap will change this initial benefit to "progressive price indexing," which is a weighted combination of wage and price indexing that is 100% wage indexing for individuals with income of \$27,700 to 100% price indexing for those making more than \$149,900.¹⁵⁸ After the initial benefit is determined, the benefit will be adjusted for cost-of-living increases in the same manner as it is currently.¹⁵⁹ There would also be a gradual increase in retirement age to age seventy about the end of the century.¹⁶⁰

The Roadmap's key to health care is the recognition that "ownership of health insurance must be shifted away from third parties to those who are actually using it."¹⁶¹ To address medical care, the Roadmap provides separate health care plans for the general public, Medicaid recipients, and Medicare recipients.

To provide for the general public's health care, the employee exclusion for employer-provided medical insurance would be replaced with a refundable tax credit that would be paid directly to a health insurance company designated by the individual.¹⁶² The amount of the refundable tax credit is \$2,300 for individuals and \$5,700 for families.¹⁶³ Universal access would be guaranteed, and insurance plans would meet certain standards for transparency and fairness.¹⁶⁴ States would establish high-

155. *Id.*

156. *Id.*

157. *Id.* at 55-56.

158. *Id.* at 56.

159. *Id.*

160. *Id.*

161. *Id.* at 44.

162. *Id.*

163. *Id.*

164. *Id.* (acknowledging that everyone with a Social Security number would be eligible for the tax credit that which would be refundable and "advanceable"). A new

risk pools, and broad interstate purchasing would be permitted.¹⁶⁵ Individuals and families selecting policies costing less than the amount of the credit would receive the saving refunded, and those choosing a policy costing more than the credit would pay the difference.¹⁶⁶ Other process changes would be implemented to keep the costs of health insurance under control.¹⁶⁷

Medicaid participants would have the same refundable tax credits but will receive an additional Medicaid payment that will provide Medicaid recipients nearly \$11,000 in medical benefits.¹⁶⁸ The additional payment will be split between the state and federal governments.¹⁶⁹ The SCHIP population will become eligible for the tax credit, while no program changes are proposed for the long-term care and disability populations.¹⁷⁰

Persons currently under age fifty-five would be subject to a new Medicare program in which, upon reaching age sixty-five, would allow them receive a means-tested risk adjusted payment of \$11,000 per year — the average amount Medicare currently pays per beneficiary.¹⁷¹ This payment would be made directly to the healthcare provider designated by the participant.¹⁷² If the selected plan costs less than the amount of the payment, the participant receives the difference, and if the plan costs exceed the payment, the participant pays the difference.¹⁷³ In addition, fully-funded Medical Savings Accounts (“MSA”) would be made available to assist low-income individuals with paying deductibles, and tax-free MSAs would be available for others.¹⁷⁴ To keep the system solvent, the program would take an

agency modeled on the Securities Exchange Commission would be charged with bringing transparency to the market place for health insurance policies and restoring consumer confidence. *Id.* at 47-48.

165. *Id.* at 45-46.

166. *Id.* at 71.

167. *Id.* at 48-49. For example, the Roadmap encourages small businesses to enter association plans, facilitates the adoption of health information technology, and proposes medical liability reform. *Id.* at 48.

168. *Id.* at 49.

169. *Id.*

170. *Id.* at 50.

171. *Id.* at v, 50-51. Means testing is implemented for those with annual incomes above \$80,000 (\$160,000 for couples). *Id.* at 51. Beneficiaries with annual incomes between \$80,000 and \$200,000 (\$160,000 to \$400,000 for couples) receive a benefit of 50% of the full payment amount, while those with incomes above \$200,000 (\$400,000 for couples) receive 30% of the full amount. *Id.*

172. *Id.*

173. *Id.*

174. *Id.*

automatic reduction in the payments for certain fee-for-service payments.¹⁷⁵

The Roadmap sees the existing federal income tax as “notoriously complex,” unfair, and the source of much economic distortion by causing individuals to make tax motivated decisions to work, save, invest, and spend instead of making rational economic decisions benefiting the family.¹⁷⁶ The Roadmap’s tax reform proposal takes the form of giving taxpayers a choice between the current system or a new simplified system with two rates of 10% and 25%, along with a generous standard deduction and personal exemptions that would have no special tax deductions, credits, or exclusions, except for a healthcare credit.¹⁷⁷ The Roadmap’s tax reform proposal eliminates the alternative minimum tax and promotes saving and investment by eliminating taxes on dividends, interest, and capital gains.¹⁷⁸

To promote competitiveness and attract businesses to the United States, the Roadmap would eliminate the corporate income tax and replace it with a “business consumption tax” (“BCT”) of 8.5% that would be border adjustable.¹⁷⁹ The BCT is a subtraction method tax on the value added in a business.¹⁸⁰ It will allow a business to determine its tax liability by subtracting its total purchases from its total sales and then remitting the tax to the government.¹⁸¹ The Roadmap uses the subtraction method because it is purportedly easier to administer than the credit-invoice method.¹⁸²

The Roadmap consolidates job training programs and interacts with states to provide necessary training to prepare for success in the global economy.¹⁸³ The Roadmap merely notes Congress’ steady increase in programs to assist in paying for educational opportunities, but it does not evaluate the effectiveness of these opportunities.¹⁸⁴ Instead, it recommends

175. *Id.* at 52.

176. *Id.* at 57.

177. *Id.* at v-vi. The 10% rate would be on the first \$50,000 income for a single person and \$100,000 for a married couple. *Id.* at vi. Personal exemptions and standard deduction for a family of four would be \$39,000. *Id.* at vi-vii. Further the Roadmap would allow one changeover between the systems during one’s lifetime. *Id.* at 57.

178. *Id.* at vi.

179. *Id.* at 59-60.

180. *Id.* at 59.

181. *Id.*

182. *Id.* at 59.

183. *Id.* at 64.

184. *See id.* at 66-67.

monitoring to insure that job training goals are being efficiently achieved.¹⁸⁵

Overall, the CBO has scored the *Roadmap* to eliminate long-term deficits and eventually the federal debt, while holding federal taxes to no more than 19% of GDP.¹⁸⁶ Proposals to reform the budget process to make it more difficult to circumvent the restrictions imposed under the *Roadmap*.¹⁸⁷

D. *Michael J. Graetz and the Competitive Tax Plan*

One notable voice in the tax reform debate is Professor Michael J. Graetz, who has been a long-time and influential contributor on this important topic. His 2008 book, *100 Million Unnecessary Returns: A Simple, Fair, and Competitive Tax Plan for the United States* (the “Competitive Tax Plan”), although predating the debt crisis, has been re-issued in paperback with a new introduction addressing the debt crisis and re-emphasizing the need for tax reform along the lines proposed in his book.¹⁸⁸ Graetz sees the necessity for new taxes as well as reduced spending as the solution to the debt crisis.¹⁸⁹ His Competitive Tax Plan is designed to address the needs of a modern tax system, while leaving the reform of entitlements to others.¹⁹⁰

The Competitive Tax Plan is a seven point plan designed to encourage savings and investment in the United States, eliminate 100 million of the 140 million tax returns filed each year, reduce the corporate tax rate to as low as 15% (the lowest in the world), avoid transitional issues normally associated with conversion to a consumption tax, reduce the use of the tax code as a social policy instrument, keep the United States as a low-tax

185. *Id.* at 18. This includes an evaluation of the Workforce Investment Act of 1998, which consolidated a number of job-training programs. *Id.* at 63.

186. *Id.* at 19-20.

The *Roadmap* charts a path of fiscal sustainability first by gaining control of explosive spending growth. . . . Under this plan, Federal spending peaks in 2033 at 24.1 percent of GDP. With revenue projections never exceeding 19 percent of GDP, this means the largest deficit faced under this plan is 5.1 percent of GDP. Although this number is large . . . , recent history shows that it is sustainable for a short period.

Id. at 18-19.

187. *Id.* at 66-67.

188. GRAETZ, UNNECESSARY RETURNS, *supra* note 22, at xi-xiii.

189. *Id.* at xii.

190. *Id.* (“We simply cannot allow projected ongoing deficits and the additional borrowing they produce to occur. Once our economy recovers and resumes real growth, both substantial reductions in anticipated government spending and tax increases will be necessary to address this looming disaster.”).

country, and harmonize the United States tax system with those of other nations.¹⁹¹

The principal actions that would achieve these objectives are the introduction of a broad-based 10% to 14% VAT,¹⁹² elimination of the income tax on families earning less than \$100,000 (\$50,000 for single taxpayers), and reduction of the rate to 25% while maintaining popular tax expenditures,¹⁹³ and reduction of the corporate income tax to 15%.¹⁹⁴ The Competitive Tax Plan is revenue and distributional neutral and retains current progressivity.¹⁹⁵ To reduce the regressive nature of a VAT, the plan would either introduce a “smart card” or adjust the payroll tax¹⁹⁶ to provide benefits to low-income families in a manner currently being implemented through the EITC and the partially refundable child tax credit.¹⁹⁷

Like other commentators, Graetz is concerned about loss of productivity¹⁹⁸ and the spiraling debt of recent years.¹⁹⁹ He also recognizes that the future is likely to require more spending as

191. *Id.* at 80, 108-09, 124, 161, 204, 208, 210-11.

192. *Id.* at 83.

193. *Id.* at 107.

194. *Id.* at 125.

195. *Id.* at xi. Graetz further notes:

One has to go back at least to the 1920s to find a chasm so big between the ultra-wealthy and the least well-off in our society. Any serious restructuring of our tax system must surely retain as one of its basic principles the progressive tax structure we have relied on for nearly a century. And if more progressivity is desired, the Competitive Tax Plan [*i.e.* the proposed VAT] can be modified to eliminate or reduce certain income tax deductions or add higher rates at the very top of the income scale. Care must be taken, however, to ensure that the plan encourages robust economic growth.

Id. at xv-xvi.

196. *Id.* at 181.

197. *Id.* at 179.

198. *Id.* at x. Graetz notes that “[f]rom 1946 through 1973, when OPEC quadrupled the price of oil, the economy grew by an average of 3.8% a year and unemployment averaged 4.5%. Since 1973, our economy has grown more slowly, and so have the wages of middle-income Americans.” *Id.* at xix.

199. *Id.* at xi-xii. Graetz notes that the federal deficit in 2008 was \$455 billion, 3.1% of gross domestic product (GDP), and \$1.4 trillion in 2009, 10% of GDP. *Id.* at xi. In 2009, the total federal debt grew from \$10 trillion to \$12 trillion and included an increase in debt to the public by \$1.7 trillion to \$7.5 trillion or 53% of GDP. *Id.* at xi-xii. Nearly half of this public debt is owed to foreigners. *Id.* at xii. Graetz noted the projected 2008 federal deficit of \$98 billion. *Id.* at xx. Further, in speculating on whether the 2001 and 2003 Bush tax cuts would be extended, he stated, “[i]f Congress fails to act, income tax rates will rise, as will tax rates on capital gains and dividends, and people will lose many other current benefits including credits for children and relief from marriage penalties.” *Id.* at xxi.

the population ages.²⁰⁰ For him, the answer to the fiscal crises is a 10% to 14% VAT,²⁰¹ although he recognizes that higher rates may be necessary if the crisis deepens.²⁰² Graetz sees the introduction of the VAT and a \$100,000 exemption to the income tax, which will eliminate 100 million tax returns, as an opportunity for Congress to reevaluate its habit of addressing every social issue through tax exemptions, deductions, and credits.²⁰³ Certainly, there would be fewer taxpayers seeking to influence politicians to keep tax expenditures.²⁰⁴

The principal difficulty with introducing a VAT is the regressive nature of a sales tax. The most common way to alleviate the regressive feature of this tax is to provide exemptions for food, medicine, medical care, education, rent, and certain clothes.²⁰⁵ This method also does not require individuals to file returns.²⁰⁶ However, as exemptions are instituted, the tax becomes more complex, and a higher rate is required to obtain the same revenue.²⁰⁷

Viewing Social Security as a great American success, Graetz emphasizes the importance of retaining a social safety-net.²⁰⁸ He goes to great lengths to develop a system that will continue the support of low-income taxpayers if the EITC and child credits are eliminated²⁰⁹ when the Competitive Tax Plan is implemented.²¹⁰

200. *Id.* at 7 (“People age eighty-five or older now constitute less than 2% of the population; they will account for 5% in 2040. Today many people retire for about one-third of their lives.”).

201. *Id.* at 211.

202. *Id.* at xiii.

203. *Id.* at 104. Graetz uses President George W. Bush’s 2007 proposal for health savings accounts and a health insurance “standard deduction,” which would extend health coverage to a mere 5 million of the 45 million uninsured, as an example of the ridiculous lengths to which politicians go in their quest to solve problems with the income tax. *Id.*

204. *Id.* at 210. Graetz believes that a 10% to 14% percent VAT, used to replace the income tax when combined with state sales taxes, will produce a rate high enough to reduce the opportunity for the Federal government to increase the VAT rate further. *Id.* at 211.

205. *See id.* at 166-67.

206. *See id.* at 166.

207. *See id.* at 166-67.

208. *Id.* at 162 (recognizing that protecting low- and middle-income taxpayers has troubled all tax reform proposals that rely on a consumption tax base).

209. *Id.* at 170-71. The Competitive Tax Plan preserves progressivity by taxing the high-income earners and using a payroll tax adjustment for low- and moderate-income families to reduce their tax burden. *Id.* Offsetting the regressivity by the EITC would be expensive because it is estimated that between \$10 and \$11 billion is claimed by people who do not qualify for them. *Id.* at 171. Current law allows advance payments through employer offsets against payroll taxes. *See id.* at 171-72; I.R.C. § 3507 (2006) (describing the advanced payment program for EITC); *see also* EDMUND S. PHELPS, REWARDING WORK: HOW TO RESTORE PARTICIPATION AND SELF-SUPPORT TO FREE ENTERPRISE 112-16

While exemptions may be politically necessary to a VAT's adoption, Graetz would prefer a system whereby the former refundable tax credits are structured as a payroll tax adjustment²¹¹ or a "smart card"²¹² to deliver the benefits to low-income taxpayers.²¹³ By redressing the burdens of the VAT directly to the recipient, it is unnecessary for the recipient to file an income tax return, although some application would need to be filed to establish the individual's qualification for the benefit.²¹⁴

IV. MAJOR CONCERNS IMPACTING THE SOLUTION

The fact that the Federal government has allowed the country's financial condition to approach the point of meltdown is

(1997) (proposing a system of graduated tax subsidies to reward employers of low-wage workers).

210. *Id.* at xi. Graetz compares the potential success of his plan by comparing it to the success of President Franklin Roosevelt in instituting the Social Security system. *Id.* at xvii. Also, he recognizes that while the tax system must promote economic growth and well-being, it must do so in a way that protects:

American workers' incomes from what Franklin D. Roosevelt called the "hazards and vicissitudes of life." Meeting these challenges . . . will depend on courageous political leadership from our presidents and members of Congress. . . . With his grand and enormously successful Social Security experiment, FDR demonstrated that important and progressive public policies can be financed and sustained even with a tax that is not itself progressive. That experiment may be one we will soon have to repeat. The Competitive Tax Plan that I have proposed in this book would be an important step toward addressing all the difficult challenges I have discussed here.

Id.

211. *See id.* at 175 ("The British have demonstrated that refundable credits can be delivered through increased paychecks without the need for workers to file annual tax returns. A one-time application may or may not be necessary to demonstrate eligibility, depending on the information requirements of the credit. And workers may be asked to verify their family circumstances . . .").

212. *See id.* at 178-80 (noting the use of such cards in the European Union and suggesting that the technology is available to use the card to deliver benefits to the individual under a multitude of federal programs depending on the individual's status, income, family size and other qualifications).

213. *See id.* at 180-81 (describing Earned Income Tax Credit delivery methods, such as payroll adjustments and smart cards, which can potentially reduce regressive impacts on low-income taxpayers). Graetz identifies three criteria for delivering benefits to deserving low-income taxpayers. First, they must be directed to those who need it without wasting resources on those who do not. *Id.* at 162. Second, costs in providing relief must be addressed. *Id.* Finally, benefit delivery must be kept administratively simple. *Id.*

214. *See id.* at 168 (using the Fair Tax "Prebate" program as an example of how to check eligibility by describing the program's process for identifying which taxpayers qualify for tax benefits). Interestingly, Graetz proposes no adjustment for retirees under a theory that cost of living adjustments of social Security would largely offset the effect of the VAT. *Id.* at 177. Further, under the Competitive Tax Plan, the retiree would be exempt from the income tax so long as his Social Security, pension, IRA distributions, and other income did not exceed the \$100,000 limit to file a return. *Id.*

shocking, but the government's inability to move back from this point of disaster because of political gridlock is a cause for radical change. Moreover, the fact that entitlements are on auto pilot must be changed and responsibility for a person's future must be shifted back to the individual. Government, under the pretext of "helping" and giving the impression that the help is free, has taken over, dominated and inflated the cost of housing, education, health care, and retirement.²¹⁵ This occurs through direct spending as well as through tax expenditures. In spite of this support, the costs of home ownership, health care, education, and retirement are beyond the reach of the majority of Americans.²¹⁶

A. *An Upside Down Savings Cycle*

In general, responsible adults have a relatively predictable pattern of savings. Once they marry and begin planning for a family, a young couple immediately thinks about health and life insurance protection and uses a portion of their income for those purposes.²¹⁷ As they start to plan for children, they save for the purchase of a home.²¹⁸ Once children arrive, they begin planning

215. See *supra* notes 94-96 and accompanying text. The impact of the Internal Revenue Codes on housing, education, health care, and retirement planning is seen in the level of tax expenditures set out in the next section. See *infra* notes 227-311 and accompanying text.

216. See Martin A. Sullivan, *Mortgage Deduction Heavily Favors Blue States*, 130 TAX NOTES 364, 364 (2011) (noting that the mortgage interest deduction heavily benefits the income earners in the higher tax brackets). Education costs grow in excess of the inflation rate. Shamik Trivedi, *Do Student Loan Deductions Offer Too Little, Too Late?*, 132 TAX NOTES 495, 495 (2011). More than 46.3 million people are without health insurance, the vast majority of which are "working individuals and children of working individuals who earn less than 200 percent of the federal poverty level." Daniel L. Mellor, *The Individual Mandate Tax: Healthcare's Toothless Watchdog*, 130 TAX NOTES 105, 107-08 (2011). The great majority of baby boomers are ill-prepared financially for retirement. MARK MILLER, THE HARD TIMES GUIDE TO RETIREMENT SECURITY: PRACTICAL STRATEGIES FOR MONEY, WORK, AND LIVING 4 (2010).

217. Tax incentives of health insurance are centered on employer-provided health care under I.R.C. § 106, so that under current tax policy, an employed couple will likely not have to provide independent coverage. See I.R.C. § 106 (2010) (stating that, generally, "gross income of an employee does not include employer-provided coverage under an accident or health plan"). The need to provide life insurance coverage arises when an individual has another person who is dependent on his income. MATERIALS ON FAMILY WEALTH MGMT. 490-91 (William J. Turnier & Grayson M.P. McCouch eds., 2005) [hereinafter FAMILY WEALTH MGMT]. Life insurance premiums, whether term insurance or whole life insurance, are largely determined by health and age; thus, the earlier in life the insurance is purchased the lower the cost. *Id.* at 493-94, 499.

218. Traditional borrowing for home ownership has required a 20% down payment that must be paid in "verifiable" funds, which are funds that do not represent additional borrowing by the borrower. *Id.* at 368-70. One of the elements of the recent and continuing "subprime" crisis resulted from eliminating many of the traditional rules for down payments and income verification. *Id.* at 365; see GRETCHEN MORGENSON &

for the payment of educational costs.²¹⁹ Later in life, after their children are educated and self-supporting, the couple begins planning for retirement and the needs they will have after their formal work life ends.²²⁰

Each step of the way is impacted by federal incentives, such as the exclusion of employer health insurance from gross income, the mortgage interest deduction supporting homeownership, and the tax free build-up and use of college savings plans under I.R.C. § 529 or retirement savings plans under I.R.C. § 401(k).²²¹ To take advantage of these plans, the couple must have sufficient income beyond their basic needs.²²²

In considering whether to save for a home, the couple is immediately confronted with the fact that they are already saving effectively 15.3% of their earnings for Social Security and Medicare.²²³ This 15.3% is a savings for retirement and retiree

JOSHUA ROSNER, RECKLESS ENDANGERMENT: HOW OUTSIZED AMBITION, GREED, AND CORRUPTION LED TO ECONOMIC ARMAGEDDON 3 (2011).

219. Many of the tax-motivated incentives described in the section on education below, such as education savings plans under I.R.C. § 529, allow for tax-free buildup of value, which is maximized the longer the funds are allowed to grow. See I.R.C. § 529(c)(1) (2010). Other education tax incentives reduce current income, such as the Hope and Lifetime Learning Credits under I.R.C. § 25A; these credits will reduce taxes at the time the child's tuition is paid and therefore do not require as much advance planning. See I.R.C. § 25A(c) (2010).

220. The income of most families is limited and allocated to immediate needs. See Laura Bruce, *High Income, Low Net Worth Could Doom Retirement*, BANKRATE.COM, para. 4 (2007), http://www.bankrate.com/brm/news/retirement/20071002_high-income_low-net-worth_a2.asp (stating the reason given by middle and upper-middle class earners for low savings is "that they need the money to pay bills"). When those needs have been met, planning is possible for the next need; although, under many tax incentives to save for retirement, such as popular plans under I.R.C. § 401(k), the tax-free build-up of value over time is an integral part of the savings plan, which is maximized the earlier the contribution is made. See MARK MILLER, *THE HARD TIMES GUIDE TO RETIREMENT SECURITY: PRACTICAL STRATEGIES FOR MONEY, WORK, AND LIVING* 4 (2010). Unfortunately, people have failed to take full advantage of I.R.C. § 401(k) plans, which have replaced many of the traditional defined benefit plans. *Id.* at 3. Thus, these people are unprepared for retirement. *Id.*

221. Details of these benefits are covered in the following sections. See *infra* notes 219-20, 259-61, and 288 and accompanying text.

222. Many of the tax expenditures discussed below involve tax deductions or credits that reduce the amount of tax a taxpayer owes, but does not benefit anyone who does not have a tax liability, although some tax expenditures are partially or fully refundable. See, e.g., I.R.C. § 25A (2010) (expanding the Hope Scholarship Credit to allow a maximum credit of \$2,500 and made it refundable to the extent of 40% of the credit). This provision was extended through 2011 and 2012 under section 103(a)(2) of the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (P.L. 111-315). See *id.* (stating that the credit applied to "any taxable year beginning in 2009, 2010, 2011, or 2012").

223. DANIEL SHAVIRO, *MAKING SENSE OF SOCIAL SECURITY REFORM* 10 (2000). The rate of contribution is 7.65% on the employee side after tax and 7.65% on the employer side for the employee pre-tax. *Id.* Economically, the employee pays 15.3%, of which one-half is pre-tax and one-half post tax since presumably his pay would be 7.65% higher if

healthcare that is forty years away.²²⁴ There may also be incentives to assist in getting into a home without the need to save, such as a first-time homebuyer's credit and incentives to borrow for a larger house than the buyer would ordinarily purchase.²²⁵ Of course, the young couple's plans may be delayed by other government programs that helped them get an

the employer were not required to match the employee contribution. *Id.* Shaviro is technically correct when he calculates an overall rate of 11.5% for the 6.2% Social Security component which, when added to the 6.2% amount paid by the employer, rather than a combined rate of 12.2%. *Id.* at 11. Suggesting that it is necessary to adjust for the exclusion of the employer's portions, Shaviro makes the following calculation:

For example, suppose I earn \$10,000 that is subject to the payroll tax but to no other taxes or withholding. The employer and I each nominally pay \$765 to the government. The employer thus pays out a total of \$10,765, while I receive \$9,235. To say that I bear the entire tax is to say that I would otherwise have received the full \$10,765. Thus, the tax I have really borne is \$1,530 out of \$10,765, or approximately 14.2 percent. In addition, adjusting for the exclusion of the employer share, the annual ceiling on wages that are subject to Social Security tax is about \$78,150 (for 1999), not \$72,600.

Id. at 10-11, 159 n.2. Further, "[t]he effective rate of Social Security tax is complicated by interactions with other taxes at various levels of government." *Id.* at 11, 159 n.3. In 2011, the Social Security portion of the 7.65% payroll tax was 6.2% on the first \$106,800 in taxable wages, and the Medicare portion was 1.45% on all taxable wages. *Id.* at 11; *see also* Social Security Administration, *2011 Social Security Changes* (2010), <http://www.socialsecurity.gov/pressoffice/factsheets/colafacts2011.pdf> (stating that the 2011 Social Security ceiling is \$106,800).

224. *See* FAMILY WEALTH MGMT, *supra* note 217, at 581-82, 687-89 (describing benefit eligibility ages for Social Security and Medicare, respectively). As noted above, the Social Security and Medicare taxes total 15.3% (technically 14.2%), which is a form of forced savings for retirement income and retirement medical benefits under Medicare. SHAVIRO, MAKING SENSE OF SOCIAL SECURITY REFORM, *supra* note 223, at 10. An individual currently qualifies for full Social Security benefits at age 66 and for Medicare at age 65. *Id.*

225. Housing and Economic Recovery Act of 2008, Pub. L. No. 110-289, § 3011, 122 Stat. 2654. Taking advantage of incentives may be a matter of timing. As enacted under the Housing and Recovery Act, first-time home buyers could receive a 10% credit up to \$7,500 on the purchase of a new home during 2008, but the credit had to be repaid beginning in 2010, in fifteen equal installments. *Id.* The American Recovery and Reinvestment Act of 2009 increased the amount of the credit to \$8,000 and eliminated the requirement for repayment if the house was used as a primary residence for three years. Pub. L. No. 111-5, § 1006, 123 Stat. 115. The Worker, Homeownership, and Business Assistance Act of 2009 extended the deadline for purchases into 2010. Pub. L. No. 111-92, § 11, 123 Stat. 2984. The IRS has found the credits to be a source of fraud and confusion in tax compliance. Nicole Duarte, *TIGTA Report on Housing Credit Fraud Confirms Analysts' Fears*, 127 TAX NOTES 1434, 1434 (2010); Nicola M. White, *Home Buyer Credit Repayment Rule Frustrates Recipients*, 130 TAX NOTES 1005, 1006 (2011). The Tax Reform Act of 1986 limited deductions for most consumer interest. Pub. L. No. 99-514, § 142, 100 Stat. 2085. The exception was qualified residence interest which included interest on a loan up to \$1,000,000 on the acquisition of a residence and on loans up to \$100,000 on home equity loans secured by the residence. I.R.C. § 163(h) (2006). Leaving the door open for the deduction of qualified residence interest created an incentive to keep the home mortgaged and use the funds for otherwise non-deductible purposes such as auto-loans. The opening is seen by some as the beginning of the real estate bubble that burst in 2008. MORGENSON & ROSNER, *supra* note 218, at 3-4.

education and that created debt that may have to be paid back before they can begin saving for the home or education for their children.²²⁶ Rather than putting 15.3% away for retirement, they may prefer to simply repay their school loans or provide a down payment on a home. Our young couple has been forced to save for retirement when their immediate need is for health care, housing, and paying off student loans. However, there are other programs to help with these needs.

B. *Tax Expenditures*

Each year, the Treasury Department is required to prepare a Tax Expenditure Budget identifying specific tax revenues lost as a result of provisions “of the Federal tax laws which allow a special exclusion, exemption, or deduction from gross income or which provide a special credit, a preferential rate of tax, or a deferral of tax liability.”²²⁷ The Tax Expenditure Budget identifies individual and corporate tax expenditures by year and over a five-year period.²²⁸ Studying the Tax Expenditure Budget reveals the enormous complexity of federal support for various activities as well as the high cost to the federal treasury.²²⁹

226. Bridget J. Crawford, Shamik Trivedi, & Kimberly Bliss, *Educational Tax Benefits: More Please*, 129 TAX NOTES 1323, 1329 (2010) (recognizing that students have become burdened with loan repayments Congress passed College Cost Reduction and Access Act (P.L. 110-84) in 2007, which created an opportunity for students to have the unpaid amount of their loans forgiven after ten years of public service employment).

227. JOINT COMM. ON TAXATION, 110TH CONG., ESTIMATES OF FEDERAL TAX EXPENDITURES FOR FISCAL YEARS 2010-2014 3 (2010) (citing Congressional Budget and Impoundment Control Act of 1974, Pub. L. No. 93-344, § 3(3), 88 Stat. 297). Tax expenditures listed reflect values estimated December 15, 2010, based on provisions in the Federal tax law enacted through that date. *Id.* at 17. Accordingly, the estimates do not include the impact of the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010, Pub. L. No. 111-312, 124 Stat. 3296 (the “2010 Tax Legislation”) that was passed by the United States Senate on December 15, 2010 and the House of Representatives on December 16, 2010, and signed by the President on December 17, 2010. TAX RELIEF, UNEMPLOYMENT INSURANCE REAUTHORIZATION AND JOB CREATION ACT OF 2010, RIC MODERNIZATION ACT OF 2010, AND OTHER RECENT TAX ACTS, LAW, EXPLANATION AND ANALYSIS 3 (2010) [hereinafter EXPLANATION OF THE 2010 TAX LEGISLATION]. The 2010 Tax Legislation, Pub. L. No. 111-312, §§ 101-102 extended certain provisions of the Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. No. 107-16 [hereinafter EGTRRA] and the Jobs and Growth Tax Relief Reconciliation Act of 2003, Pub. L. No. 108-27 [hereinafter JGTRRA], both of which were scheduled under Senate rules to sunset on December 31, 2010. EXPLANATION OF THE 2010 TAX LEGISLATION, *supra* note 227, at 3.

228. See JOINT COMM., ESTIMATES OF FEDERAL TAX EXPENDITURES FOR FISCAL YEARS 2010-2014, *supra* note 227, at 4 (noting that the Budget Act uses the term tax expenditures to refer to special tax provisions contained in the Federal income taxes on individuals and corporations); see also *id.* at 4-9 (describing the methods used for determining individual and corporate tax expenditures).

229. JOINT COMM. ON TAXATION, BACKGROUND INFORMATION ON TAX EXPENDITURE ANALYSIS AND HISTORICAL SURVEY OF TAX EXPENDITURE ESTIMATES 10-12 (2011)

Evaluating tax expenditures is not a question of general tax policy; rather, it is a question of spending policy such that traditional notions of horizontal and vertical equity are inapplicable.²³⁰

The overall Tax Expenditure Budget is over \$1 trillion annually.²³¹ Items affecting health care, housing, education, and retirement include (in Billions of dollars for fiscal year 2011 ending September 30, 2011): exclusion of employer contributions for health care, \$117.3; exclusion of Medicare Parts A, B, and D benefits, \$63.6; deduction of mortgage interest on owner-occupied housing, \$ 93.8; deduction for property taxes on real property, \$22.8; exclusion of capital gains on sales of principal residences, \$16.5; credits for tuition to post-secondary education – Hope and Lifetime Learning credits, \$7.7; exclusion of pension contributions and earnings \$105.8; and individual retirement arrangements, \$16.3.²³² Other important tax expenditures include: the exclusion of charitable deductions to educational institutions, \$6.0; child credit for children under age 17, \$24.7; and earned income tax credit, \$52.4.²³³

The lost tax revenue by reason of support for housing, education, health care, and retirement is significant but is only part of the equation of support in these areas. Federal support through direct spending in these areas is also significant.²³⁴ Unfortunately the help provided by the Federal government overwhelms and inflates prices in each area.²³⁵

[hereinafter JOINT COMM. ON TAXATION, BACKGROUND INFORMATION ON TAX EXPENDITURE ANALYSIS]. The Tax Reform Act of 1986 (P.L. 99-514) is considered one of the most comprehensive revisions of the Federal income tax in history and reflected Congress' attempt to eliminate various tax expenditures and other preferences, broaden the tax base, and lower the rates. *Id.* at 26. The Joint Committee on Taxation then identifies over 150 new tax expenditures that have been added since the Tax Reform Act of 1986. *Id.* at 18-25. It also notes that, once adopted, tax expenditures tend to stay in place for a long time. *Id.* at 16.

230. See Martin J. McMahon, Jr., *Taxing Tax Expenditures?*, 130 TAX NOTES 775, 777 (2011) (citing STANLEY S. SURREY & PAUL R. MCDANIEL, TAX EXPENDITURES, 81 (1985)).

231. See *Moment of Truth*, *supra* note 22, at 28 (noting that Washington has riddled the system with countless tax expenditures amounting to \$1.1 trillion a year and suggesting that the current system drives up health care costs).

232. JOINT COMM., ESTIMATES OF TAX EXPENDITURES FOR FISCAL YEARS 2010-2014, *supra* note 227, at 39, 47, 49.

233. *Id.* at 45, 47, 50.

234. See FAMILY WEALTH MGMT., *supra* note 217, at 360, 470-76.

235. See McMahon, *supra* note 230, at 787. The inefficiency and inequity of tax expenditures and their capitalization in the price of goods is noted: "Because some significant portion, but almost certainly not all, of the benefit of many tax expenditures obtained by engaging in market transactions with third parties is capitalized into market prices, these types of tax expenditures are doomed to cause both inefficiency (that is, create economic distortion) and inequity." *Id.* at 786.

Tax expenditures are often called “up-side down” subsidies because those most benefiting from them are individuals who are in the higher tax brackets.²³⁶ If, as the analysis of American Paternalism recognizes, there is merit in federal assistance to the less fortunate in society, then elimination of most, if not all, tax expenditures will only serve to make the system simpler and more progressive.²³⁷ For this reason, many advocates of tax reform urge repealing most tax expenditures.²³⁸ Tax expenditures allow one a choice in spending so long as the choice is one favored by the federal government.²³⁹

C. Housing

Currently, the United States and much of the developed world is recovering from the bursting of a housing bubble.²⁴⁰ In the United States, it was caused by incredibly low-interest rates

236. Miranda Perry Fleischer, *Generous To A Failure? Fair Shares and Charitable Giving*, 93 MINN. L. REV. 165, 193 (2008); see, e.g., William A. Sullivan, *The Rich Get 100 Times More Mortgage Subsidy Than the Poor*, 130 TAX NOTES 1110, 1110 (2011) (pointing out that the high-income taxpayers benefit most from the mortgage interest deduction because they have larger houses and mortgages, only itemizers take the deduction, and they have higher marginal tax rates). Sullivan concludes, “[S]o it is fair to say that among tax experts, there is a consensus that the mortgage interest deduction should be trimmed . . . But you will not hear any members of Congress calling for reduction in the mortgage interest deductions.” *Id.* at 1111.

237. See Butler, *supra* note 1, at 523. The One Fund Solution balances the need for a minimum support system through required contributions to a government fund with the flexibility of individual accounts all of which is financed through the elimination of tax expenditures. *Id.* The President’s Fiscal Commission called for the elimination of most tax expenditures and concluded:

Lower rates, broaden the base, and cut spending in the tax code. The current tax code is riddled with \$1.1 trillion of tax expenditures: backdoor spending hidden in the tax code. Tax reform must reduce the size and number of these tax expenditures and lower marginal tax rates for individuals . . . thereby simplifying the code, improving fairness, reducing the tax gap, and spurring economic growth. . . .

Maintain or increase progressivity of the tax code. Though reducing the deficit will require shared sacrifice, those of us who are best off will need to contribute the most. Tax reform must continue to protect those who are most vulnerable, and eliminate tax loopholes favoring those who need help least.

Moment of Truth, *supra* note 22, at 28.

238. See, e.g., *Moment of Truth*, *supra* note 22, at 15; see also Domenici & Rivlin, *supra* note 22, at 31.

239. See David Cay Johnston, *Making Tax Simple*, 130 TAX NOTES 347, 347 (2011) (“So the mortgage interest deduction, executive deferrals, small business write-offs, and subpart F all have to be examined for real reform to have a chance. So will all those finely detailed provisions for various industries, especially oil and gas.”). Taking it a step further, Johnston points out that real tax reform “must address realization and deferral and whether people should be allowed to live tax free by borrowing against appreciated, but untaxed, assets.” *Id.* at 349.

240. See BRIAN S. WESBURY, IT’S NOT AS BAD AS YOUR THINK: WHY CAPITALISM TRUMPS FEAR AND THE ECONOMY WILL THRIVE 56-61 (2010).

held low by the Federal Reserve Bank, aggressive lending practices supported by Freddy Mac and Fanny Mae guaranteeing loans with little or no money down, interest only financing, and even financing in excess of appraised value.²⁴¹ It has been the American dream to own a home and, as a result, public policy has favored providing incentives toward reaching this dream.²⁴²

The most sacred of the tax expenditures is the tax deduction for mortgage interest, which covers interest on a home equity loan for a primary residence and a second residence.²⁴³ Other incentives supporting home ownership are the first time home buyer's credit, the deduction for real estate taxes, and the exemption of gains up to \$500,000 on sale of property used as a primary residence for only two years.²⁴⁴ The effect of these

241. *Id.* at 53-65. Wesbury describes the causes of the subprime crisis as a "Government-Sponsored Crisis" and states:

The idea that greedy bankers, unprodded by government incentives, were just writing mortgages, packaging mortgages, selling mortgages, and encouraging others to do the same all for the commissions and bonuses has never been true. The government encouraged this market to develop and hardly ever seemed to worry about it. As long as interest rates were low and banks could securitize assets into triple-A-rated pools, investors were willing to buy them. This finally changed when the Fed lifted rates enough to bring it to a stop.

Id. at 63.

242. See generally FAMILY WEALTH MGMT., *supra* note 217, at 338-39. Of particular importance to homeowners from a tax policy standpoint is that the consumption value of the home (i.e. the rental value) is not imputed to the owner-occupier, thereby creating a significant advantage over those renting their home. See generally DEPT OF TREASURY, BLUEPRINTS FOR TAX REFORM 85-89 (1997) (discussing the impact of income tax provisions on owner-occupied housing). Current proposals to change the "sacrosanct" mortgage interest deduction to a tax credit, during a depressed housing market no less, have incurred substantial resistance. See Nicola M. White, *As Budget Gap Widens, Mortgage Deduction Comes Under Fire*, 131 TAX NOTES 1144, 1144 (2011).

243. See White, *supra* note 242, at 1144; 26 I.R.C. §§ 163(h)(3), 163(h)(4)(a)(i) (West 2006). The inefficiency and inequity of the mortgage interest deduction is noted: "The home mortgage interest deduction can serve as a quintessential example of the lose-lose nature of tax expenditure subsidies. From an efficiency perspective, investment capital is diverted from other uses into an increased stock of owner-occupied homes." McMahon, *supra* note 230, at 786. McMahon further summarizes, "experts have concluded that the deduction for home mortgage interest 'is unlikely to influence the home ownership rate,' but that it does lead to overconsumption of owner-occupied housing by those who were already inclined to own homes." *Id.* at 787 (quoting Edward L. Glaeser & Jesse M. Shapiro, *The Benefits of the Home Mortgage Interest Deduction*, 17 TAX POL'Y & THE ECON. 37, 40 (2003)).

244. See RICHARD J. WOOD, FAMILY TAX LAW 209 (2010) (describing the first-time home buyer credit under I.R.C. § 36, which Congress extended to 2010). Speculation in housing was in no small measure caused by I.R.C. § 121, which excluded up to \$500,000 in gain on the sale of a property that had been used as a principle residence for periods aggregating two years or more during the previous five year period preceding the sale. I.R.C. §§ 121(a), 121(b)(1)(2)(A) (2006). A lower limit of \$250,000 applied if the taxpayer did not file a joint return, which created a strong incentive for single taxpayers to marry in the year of sale. *Id.* § 121(b)(1)-(2). Further, the exclusion could be applied every two years. *Id.* § 121(b)(3).

incentives has been to distort the residential real estate market with the unintended consequence of raising the prices of residential real estate beyond the reach of many young couples and the creation of a real estate bubble that brought the world to a near financial meltdown. Moreover, in more sober times these tax incentives have primarily benefited high-income taxpayers.²⁴⁵

While there are plenty of fingers pointing at many participants in the housing bubble, the fact is that the housing boom of the mid-2000s generated incredible profit making for real estate agents, mortgage brokers, housing speculators, investment banks, and others, resulting in the near collapse of the world's financial structure and the need for trillion dollar bailout measures for banks, Fanny Mae, Freddy Mac, AIG and others.²⁴⁶ The Federal Reserve was forced to bring interest rates to zero with unintended consequences of causing senior citizens on fixed incomes to suffer by receiving zero interest on their once secure money market funds, bank CDs, and Treasury notes and bonds.²⁴⁷

D. Education

For years, the average American family has depended on government support to help cover the rising cost of higher education.²⁴⁸ While limited targeted educational support

245. William G. Gale, Jonathan Gruber, & Seth Stephens-Davidowitz, *Encouraging Home Ownership Through the Tax Code*, 115 TAX NOTES 1171, 1171 (2007). Finding that the mortgage interest deduction's primary effect was to raise housing prices, the authors cite studies suggesting that the price of housing is increased about 10% by reason of the deduction. *Id.* at 1179. Other studies suggest there is no impact when the experimental model is based on an infinitely elastic long-term supply of housing. *Id.*

246. See REINHART & ROGOFF, *supra* note 15, at 208, 210. See generally WESBURY, *supra* note 240, at 53-65 (describing the development of the subprime crisis and attributing the cause to the federal government). Wesbury states that "[t]he bottom line is that government policy creates many more problems than most people ever understand. But when government does damage, it is often able to blame someone else." *Id.* at 55.

247. WESBURY, *supra* note 240, at 122.

248. JOSEPH HURLEY, THE BEST WAY TO SAVE FOR COLLEGE: A COMPLETE GUIDE TO 529 PLANS, 1-9 (2011). Hurley states,

In 2004, the median annual earnings of full-time workers ages 25-34 with at least a bachelor's degree was 53 percent higher than those with only a high school diploma or equivalent. Between 1980 and 2008 the earnings of the first group rose 6.45% (after inflation), while the earnings of the second group fell by 16.44%.

Id. at 1 n.1 (citations omitted). He then points out that, over the past ten years, tuition and fees at four-year public institutions have risen 72% while those of private four-year colleges and public two-year colleges risen only 35% and 31%, respectively, after adjusting for inflation, and that since 1980, college prices have been rising at a rate of two to three times the increase in the Consumer Price Index. *Id.* at 2-3. He then points out that the average American family is on track in 2010 to cover only 16% of total college costs. See *id.* at 5. After describing traditional means families have used to provide for such costs he

programs such as the GI Bill may be successful,²⁴⁹ the expansion of that support to the entire population²⁵⁰ does not necessarily multiply its success.²⁵¹

Today, college students and their parents are given tax credits, tuition deductions, state-sponsored qualified tuition programs, subsidized and unsubsidized loans, grad plus loans, Pell Grants, and other methods of direct and indirect support for students.²⁵² In 2010, the U. S. Department of Education took over as the exclusive originator of federally-backed student loans.²⁵³ Educational tax incentives are enormously complex, there is constant pressure for more, and they continue to grow each year.²⁵⁴ Tuition rates have increased 6% to 9% during any 17-year period from 1958 to 2001, which equates to 1.2 to 2.1 times the rate of general inflation.²⁵⁵ Ironically, one possible, but controversial explanation for the accelerated increase would be the existence of the tax incentives themselves.²⁵⁶ Colleges are able to capture the benefits of the tax incentives by reducing local

outlines the benefits of state sponsored plans under I.R.C. § 529 which is the subject of his book. *Id.* at 5-8.

249. See Sheldon S. Cohen, *The Erwin N. Griswold Lecture*, 14 AM. J. TAX POL'Y 113, 121 (1997).

250. *Id.* ("Putting a program in the internal revenue code opens it up for everyone . . .").

251. *Id.* Using the tax code to provide financial assistance for college clutters up the tax code and leads to economic waste. *Id.* Such programs are educational in nature and would be best administered by the Department of Education, not the IRS. *Id.*

252. See Crawford et al., *supra* note 226, at 1331-32; FAMILY WEALTH MGMT., *supra* note 217, at 418-64, 466-76.

253. Student Aid and Fiscal Responsibility Act, Pub. L. No. 111-152, 124 Stat. 1071 (2010) (effectuating the federal takeover of the student loan program).

254. See Crawford et al., *supra* note 226, at 1333-38 (providing a detailed description of the many tax incentives available for education). Recent economic turmoil has led to an increased need for higher education tax incentives from the government. *Id.* at 1331. Government student aid programs increased by more than 128% between 1997 and 2007. HURLEY, *supra* note 248, at 4.

255. *The Smart Student Guide to Financial Aid*, FINAID.ORG, para. 1, <http://www.finaid.org/savings/tuition-inflation.phtml> (last visited Nov. 20, 2011).

256. Compare William J. Bennett, *Our Greedy Colleges*, N.Y. TIMES, Feb. 18, 1987, para. 3, <http://www.nytimes.com/1987/02/18/>

[opinion/our-greedy-colleges.html?pagewanted=1](http://www.nytimes.com/1987/02/18/opinion/our-greedy-colleges.html?pagewanted=1) ("[I]ncreases in financial aid in recent years have enabled colleges and universities blithely to raise their tuitions, confident that Federal loan subsidies would help cushion the increase."), with Bridget Terry Long, *What is Known About the Impact of Financial Aid?: Implications for Policy*, NAT'L CTR. FOR POSTSECONDARY RESEARCH 30-34 (2008), http://www.postsecondaryresearch.org/1/a/document6963_LongFinAid.pdf (in response to William J. Bennett's article, Terry suggests that there are no "robust" results that support the conclusion that colleges have responded to federal aid by raising tuition). However, some research supports the conclusion that colleges have responded to state aid in that manner. *Id.* at 32.

student aid.²⁵⁷ As a result, students may not realize an actual benefit from the tax incentives.²⁵⁸

While much educational support is structured to benefit low-income students and families, tax law has created a loophole for wealthy individuals to pay for the higher education needs of their children and grandchildren with untaxed income through § 529 plans.²⁵⁹ Under these plans, the only limitation on the amount contributed is that it cannot exceed the cost of a qualified higher education.²⁶⁰ Section 529 allows wealthy taxpayers to shelter large sums of money for use in educating family members.²⁶¹

257. McMahan, *supra* note 230, at 787 (“[T]he credits for higher education tuition payments have resulted in greater increases in college tuition than otherwise would have occurred, thereby shifting some of the benefit to colleges and universities.”).

258. Deborah H. Schenk & Andrew L. Grossman, *The Failure of Tax Incentives for Education*, 61 TAX L. REV. 295, 358 (2008) (noting that it is possible for colleges to capture the benefits of tax incentives by reducing financial aid, which would cancel out the benefit of the tax incentives for students); *see also id.* at 299–305 (describing tax subsidies for higher education including Hope and Lifetime Learning Credits, deduction for Qualified Tuition, interest on education loans, qualified tuition programs, and other tax incentive programs).

259. *See* I.R.C. § 529 (2006). Section 529 plans are state-operated plans that permit the establishment of either prepaid tuition plans, which provide for the purchase of tuition credits that can be used in future years, or a college savings plan, in which contributions are invested in a variety of investment options depending on the state and plan manager. *See* FAMILY WEALTH MGMT., *supra* note 217, at 423-30. The tuition plans have become more expensive in recent years as college tuition costs have increased, and investment returns have been less than needed to provide for the expected tuition costs. *See* Chris Umpierre, *Prepaid College Prices Mount*, TIMES OF TEXAS, October 16, 2011, para. 4, <http://www.news-press.com/article/20111017/NEWS0104/111016025/Prepaid-college-prices-mount>. Distributions under Section 529 plans are exempt from income tax under amendments to the section under the Economic Growth and Tax Relief Reconciliation Act of 2001 (popularly known as the “Bush Tax Cuts”) and made permanent under the Pension Protection Act of 2006 (the “PPA”). Advance Notice of Proposed Rulemaking, 73 Fed. Reg. 3441 (Jan. 18, 2008) (to be codified at 26 C.F.R. pt. 1). Section 1304(b) of the PPA added Section 529(f) providing that the Secretary shall proscribe regulations to carry out the purpose of Section 529 and prevent abuse of the purpose. *See* Advance Notice of Proposed Rulemaking, 73 Fed. Reg. 3441, 3442 (Jan. 18, 2008) (describing and giving examples of potential abuses involving the gift and the generation skipping transfer taxes); *see also* HURLEY, *supra* note 248, at 22.

260. I.R.C. § 529(b)(6) (requiring plans to provide safeguards to prevent contributions on behalf of a designated beneficiary exceeding those necessary to provide for the qualified higher education expenses of the beneficiary). Joseph Hurley notes an IRS private letter ruling approving a limit based on four years of undergraduate expenses, three years of graduate school expenses, and the availability of many plans with contribution limits in excess of \$300,000. HURLEY, *supra* note 248, at 44.

261. *See* HURLEY, *supra* note 248, at 121-22. While most people will stay within the annual gift tax exemption amount (currently \$13,000 per donee), contribution limits exceeding \$300,000 are likely to be attractive only to wealthy taxpayers. *Id.* at 121. The costs payable under Section 529 plans include are tuition, fees, room and board and similar costs at qualified higher education institutions. I.R.C. § 529(e)(3). Special programs have been established for students from low income families. *See* Carol Zeiner, *Section 529 Prepaid College Tuition Scholarships: Help in Uncertain Economic Times*, 55 WAYNE L. REV. 1061, 1076 (2009) (proposing that states facilitate use of 529 plans to

Everyone must have a college degree regardless of cost and regardless of how inflated that cost may become, how high unemployment rates among college graduates, or how alarming the default rate on student loans. Nevertheless, Congress will continue to provide the means to achieving that degree whether or not it prepares the student to earn an income.²⁶² Indeed, creating a generation of young people with student loans they cannot repay may be the next financial bubble to burst.²⁶³

receive private contributions to provide scholarships for economically disadvantaged students).

262. See generally *For-Profit Colleges: Undercover Testing Finds Colleges Encouraged Fraud and Engaged in Deceptive and Questionable Marketing Practices: Hearing before the S. Comm. On Health, Education, Labor, and Pensions*, 111th Cong. 7 (2010) (statement of Gregory D. Kutz, Managing Director, Forensics Audits and Special Investigations, U.S. Government Accountability Office) (noting many fraudulent practices practiced by for-profit education institutions qualifying for participation in student loan programs). The report found that of the \$105 billion in funding for the 2008-09 school year under Title IV of the Higher Education Act of 1965, as amended ("Title IV"), approximately 23%, or \$24 billion, went to students attending for-profit schools. *Id.* at 2. It further noted that of the 2,000 for-profit colleges eligible to participate in Title IV programs, fourteen publicly-traded corporations had enrollment of 1.4 million students; one of which with 443,000 students. *Id.* at 1. The report also noted that earlier reports had concluded that students who attended for-profit colleges were more likely to default on federal student loans than students from other colleges. *Id.* at 5.

263. See Michael Barone, *Will Higher Ed Be Next Bubble to Burst Open?*, INVESTORS BUS. DAILY, Jul. 21, 2011, at A13 (noting that a true bubble is when something is overvalued and intensely believed, such as the higher education, which he sees as now combining rising cost and dubious quality); see also Jenna Ashley Robinson, *Is Higher Education Worth It? Or Is It the Next Big Bubble?*, INVESTORS BUS. DAILY, Jul. 24, 2011, at A11 (questioning whether graduates from college with a bachelor's degree can expect to earn about sixty-six percent more income over a forty-year working life than the typical high school graduate while suggesting that the gap between college graduates and high school graduates has been narrowing since 2001); Alex Tabarrok, *College Has Been Oversold*, INVESTORS BUS. DAILY, Oct. 20, 2011, at A13 (noting that the number bachelor's degrees awarded in visual and performing arts, psychology, journalism, and other humanities in 2009 has doubled over the past twenty-five years even though half of all humanities graduates end up in jobs not requiring a college degree, while the number of graduates in scientific fields such as microbiology, mathematics, and chemical engineering has remained about the same as twenty-five years ago); Michael C. Macchiarola & Arun Abraham, *Options for Student Borrowers: A Derivatives-Based Proposal to Protect Students and Control Debt-Fueled Inflation in The Higher Education Market*, 20 CORNELL J. L. & PUB. POLY 67, 69 n.3 (2010); Maulik Shah, *The Legal Education Bubble: How Law Schools Should Respond to Changes in the Legal Market*, 23 GEO. J. LEGAL ETHICS 843, 846-48 (2010) (evaluating several models to address the increasing cost of legal education). Indeed, there are considerable costs to the states associated with students attending the first year of college and then failing to return the second year. An American Institutes for Research report found:

[D]uring the five years between 2003 and 2008 . . .

- States appropriated almost \$6.2 billion to colleges and universities to help pay for the education of students who did not return for a second year.
- States gave over \$1.4 billion and the Federal government over \$1.5 billion in grants to students who did not return for a second year.

E. Healthcare

Healthcare has been the subject of intense debate since 2009 and 2010 and will likely continue through the 2012 presidential campaign. The Patient Protection and Affordable Care Act of 2010²⁶⁴ and Health Care and Education Reconciliation Act of 2010²⁶⁵ (jointly referred to as the “Affordable Care Act” or the “ACA”) are projected to expand coverage to 32 million people by 2016, while reducing the deficit by \$124 billion from 2010 to 2019 and by \$1.0 trillion during its second decade.²⁶⁶ These CBO figures are highly debated, but the CBO report is constrained by the parameters set by Congressional leadership. Current efforts are under way to repeal all or part of the ACA, and the CBO has issued a letter to the effect that repeal would negate a potential deficit decrease by \$210 billion over the period 2012-2021.²⁶⁷ Nevertheless, whatever the impact of ACA, health-care costs and the government’s healthcare spending will increase and most likely put continuing pressure on the deficit.²⁶⁸

That federal spending on healthcare has caused an inflation of health care costs is undeniable. The Task Force sees tax subsidies for employer-provided healthcare as encouraging overly comprehensive plans with few cost containment measures that make health care costs increase, which has the effect of

Mark Schneider, *Finishing the First Lap: The Cost of First-Year Student Attrition in America’s Four-Year Colleges and Universities*, 2010 AM. INST. FOR RESEARCH, Oct. 2010, at 1, http://www.air.org/files/AIR_Schneider_Finishing_the_First_Lap_Oct101.pdf. The report further predicts that 30% of students who start college in the fall will not return the next year and that “only about sixty percent of students graduate from ‘four-year’ colleges and universities within six years.” *Id.* at 2.

264. Patient Protection and Affordable Care Act, Pub. L. No. 111-148, 124 Stat. 119 (2010).

265. Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, 124 Stat. 1029 (2010).

266. See CBO’s *Analysis of the Major Health Care Legislation Enacted in March 2010: Hearing on H.R. 2 Before the H. Subcomm. on Health, Committee on Energy and Commerce*, 112th Cong. 1-3 (2011) (statement of Douglas W. Elmendorf, Director, Cong. Budget Office).

267. See *id.* at 2; see also Letter from Douglas W. Elmendorf, Director, Cong. Budget Office, to Honorable John Boehner, Speaker H.R. (Jan. 6, 2011) (discussing the budgetary impact of H.R. 2, the Repealing the Job-Killing Health Care Law Act, as introduced on January 5, 2011).

268. Statement of Douglas W. Elmendorf, *supra* note 266, at 7 (recognizing that the ACA will increase federal commitment to health care by about \$464 billion over the 2012-2021 period). Further, the statement indicates that the ACA will reduce the deficit by approximately one-half percent of GDP from 2022 to 2031, but cautions that its estimates could be quite different if key provisions of that original legislation are subsequently changed or not fully implemented. *Id.* That projected savings are unlikely to be realized is not improbable because Congress is often unwilling to allow program cuts to take place when the time comes. See CBO, 2011 LONG-TERM BUDGET OUTLOOK, *supra* note 7, at 2, 7 (discussing the “alternative fiscal scenario”).

increasing spending in the areas of Medicare, Medicaid, and other public programs as well.²⁶⁹ It would build its healthcare changes on provisions of the ACA that provide subsidies for low-income people to obtain health care through state-sponsored health insurance exchanges that provide federal subsidies for certain individuals and families that could potentially provide more efficient insurance markets for individuals and families.²⁷⁰

The Commission pointed out that virtually all health economists recognize that its proposal to phase out the exclusion for employer-provided healthcare insurance will help decrease the growth in health care spending.²⁷¹ The Commission went further, stating,

Commission members, and virtually all budget experts, agree that the rapid growth of federal health care spending is the primary driver of long term-deficits. Some Commission members believe that the reforms enacted as part of ACA will “bend the curve” of health spending and control long-term cost growth. Other Commission members believe that the coverage expansions in the bill will fuel more rapid spending growth and that the Medicare savings are not sustainable. The commission as a whole does not take a position on which view is correct²⁷²

Rep. Ryan’s Roadmap makes the same point:

But if rising private health costs drive the growth of Medicare and Medicaid spending, *the converse also is true*: Medicare and Medicaid themselves contribute in their own way to medical inflation.

269. See Domenici & Rivlin, *supra* note 22, at 50.

270. *Id.* Patient Protection and Affordable Care Act provides that the subsidy will be in the form of a refundable tax credit that will be paid in advance to permit the taxpayer to purchase the health insurance. I.R.C. § 36(B) (2010). Because the subsidies in 2014 will be available to families with incomes up to 400% of the federal poverty level the law establishes six tiers and provides percentages which the taxpayer must pay toward such insurance. *Id.* The required payment varies from 2% for incomes up to 133% of the poverty level to 9.5% for incomes in the 300% to 400% of the poverty level. *Id.* For example, an individual with an income of \$88,000 (400% of the poverty level) would be required to contribute approximately \$8,350 (9.5% of \$88,000) toward the \$11,500 premium for a family of four. The difference \$3,140 (\$11,500 less \$8,350), is the amount of the subsidy which will vary from 96% of premiums for incomes up to 150% of the poverty level and 35% of premiums for incomes up to 400% of poverty level. EXPLANATION OF THE 2010 TAX LEGISLATION, *supra* note 227, at 184-87.

271. See Moment of Truth, *supra* note 22, at 41.

272. *Id.*

These two programs account for roughly 37 percent of all health care spending nationally Another 10 percent comes from other public programs, including those of State and local health departments, the Department of Veterans Affairs, and workers' compensation. Such large infusions of government funds inevitably stoke rising medical costs.²⁷³

Health care costs for every American are rising at rates above that of inflation.²⁷⁴ Many of these increases in healthcare costs result from tax expenditures,²⁷⁵ from Medicare spending on Part A which is financed through the Medicare payroll tax, and from spending by enrollees in Medicare Parts B and D who pay premiums for such coverage that is heavily subsidized by general revenues.²⁷⁶ As such, enrollees are likely to see their Part B and D premiums and coinsurance taking a larger share of their Social Security and other income.²⁷⁷ The 2010 Annual Report of the Social Security and Medicare Boards of Trustees ("Trustees 2010 Report")²⁷⁸ reports substantial improvement in the Part A funding as a result of anticipated program efficiencies and additional tax revenues from the ACA.²⁷⁹ Parts B and D are seen as "adequately" financed because of automatic financing from general revenues.²⁸⁰ Part B is expected to grow at an average annual rate of 7.5% (through 2016) and Part D at 9.7% (through 2017), while the average annual growth rate for the economy as a

273. *Roadmap*, *supra* note 142, at 26. Rep. Ryan sees the heart of the health care problem as government tax subsidies and programs that create third-party payment systems that insulate the consumer from prices and market forces. *Id.* at 27.

274. *See* Moment of Truth, *supra* note 22, at 36; Domenici & Rivlin, *supra* note 22, at 46; *Roadmap*, *supra* note 142, at 25-27.

275. Rep. Ryan notes particularly the impact of tax subsidies on the increasing costs of healthcare. *Roadmap*, *supra* note 142, at 27-30.

276. *See* BD. OF TRS., *supra* note 54, at 37-38.

277. *Id.* Supplemental Medical Insurance is made up of Medicare Parts B and D. *Id.* at 1. Part B provides payment for physicians. *See id.* at 37. Part D, on the other hand, provides drug benefits. *See id.* at 134; Graetz, UNNECESSARY RETURNS, *supra* note 22, at 23 (pointing out that the Medicare drug benefit which was added in 2003 was the first time a major new entitlement was enacted without providing a funding source).

278. BD. OF TRS., *supra* note 54, at 88. Projections and conclusions in the Annual Report are qualified by the recognition that all such projections and conclusions reflect current law while Congress is "virtually certain" to override some of the cost saving measures in current law. *Id.* at 95.

279. *Id.* at 7-8. However, total Medicare expenditures are projected to increase from 3.5 percent of GDP in 2009 to 6.4 percent of GDP in 2084. *Id.* at 8. The ACA imposes an additional Part A tax of 0.9% on payroll over \$200,000 for individual filers and \$250,000 for joint return filers. *Id.* at 10.

280. *See id.* at 8-9.

whole is 5.2%.²⁸¹ Everyone should have access to health care, but the government has yet to demonstrate the ability to provide that care on an efficient and cost-effective manner over the long-term.

F. Retirement Savings

Traditional retirement planning consisted of three prongs: Social Security, an employer's pension plan, and individual savings.²⁸² Retirement savings under the second prong include qualified defined benefit plans²⁸³ covering large employee groups²⁸⁴ that permit an immediate tax deduction of employer contributions, while excluding the value of such benefits from an employee's income until benefits are taken by the employee at retirement.²⁸⁵ Nonqualified retirement plans established for executive employees are funded by employers who are denied a deduction until benefits are actually paid to the executive who recognizes no income until received at retirement.²⁸⁶ Defined contribution plans²⁸⁷ can allow both pre- and post-tax

281. See *id.* at 142 (assuming that Congress continues to override the physician fee reduction). The report's 75-year prediction for hospital insurance (Part A) increased the projected deficit from 0.66% of taxable payroll to 0.79% of taxable payroll. See *id.* The report indicates that monthly premiums for Part B increased from \$96.40 in 2009 to \$110.50 for 2010 and \$115.40 for 2011. See *id.* at 33. Additionally, Social Security benefits did not increase for 2010 and 2011 due to low inflation. See *id.* However, because a hold-harmless provision prevents Social Security benefits from decreasing when Part B premium increase, the premium increases only impacted new enrollees, high-income enrollees not subject to the hold-harmless provision, and state Medicaid programs, which in total constitute approximately 25% of enrollees. See *id.* The report expected Social Security recipients to receive between a 0.6 to 1.2% benefit increase for 2012, but the Social Security Administration has indicated recently that the increase will be between 3.5 and 3.7% for 2012. See *id.* at 34; Donna Gehrke-White, *Social Security Checks to Increase 3.6% in January*, SUN SENTINEL (Fort Lauderdale, FL), October 19, 2011, at 1A. Much of the anticipated increase will be taken up by the Medicare Part B premium increases. See *id.*; see also Jeff Ostrowdki, *The Squeeze on Social Security: Retirees Feel Pinched as Costs Rise but Incomes Don't*, PALM BEACH POST, March 31, 2011 at A1, A4 (noting that, on average, Social Security recipients spend 9% of their benefits on Medicare Part B and 3% on Medicare Part D).

282. See FAMILY WEALTH MGMT., *supra* note 217, at 565; RICHARD N. BOLLES & JOHN E. NELSON, WHAT COLOR IS YOUR PARACHUTE? FOR RETIREMENT: PLANNING NOW FOR THE LIFE YOU WANT 25-26 (2007).

283. See FAMILY WEALTH MGMT., *supra* note 217, at 592-93.

284. See *id.* "Employees do not have individual accounts in defined benefit plans; they have only a right to receive the promised benefit." *Id.* at 593.

285. See *id.* at 588, 592.

286. See Rev. Proc. 92-64, 1992-2 C.B. 422 (providing a model grantor trust for use in executive compensation arrangements popularly known as "rabbi" trusts).

287. See FAMILY WEALTH MGMT., *supra* note 217, at 592 ("A defined contribution plan, also known as an individual account plan, is a plan in which each participant has a separate account.").

contributions.²⁸⁸ If the contributions are pre-tax, benefits are taxed upon distribution at retirement.²⁸⁹ However, if the contributions are post-tax, distributions will be exempt from tax.²⁹⁰ Facilitating the third prong are a series of tax motivated individual retirement accounts²⁹¹ that provide pre-tax and post-tax contribution options, and are taxed in a similar manner as defined contribution plans.²⁹²

Tax expenditures supporting employer-provided retirement plans and individual retirement plans totaled over \$100 billion in 2010 and could reach more than \$700 billion between 2010 and 2014.²⁹³ Because of the progressive nature of the federal income tax, the maximum benefits under these retirement plans inures to the benefit of high-end taxpayers.²⁹⁴ Like other tax expenditures, these plans are considered upside-down subsidies.²⁹⁵

288. *See id.* at 602 (“[A]n employer can design a 401(k) plan to include a ‘Roth’ feature, which allows the employee to elect to include a 401(k) contribution in taxable income in the year of contribution in exchange for a permanent income tax exclusion for qualified distributions from the plan.”).

289. *See id.*

290. *See id.* at 602, 618.

291. *See id.* at 616 (noting three examples of non-employment based retirement vehicles: the individual retirement account (IRA); the Roth IRA; and the health savings account (HSA)).

292. *See id.* at 616, 618, 622-23. Health Savings Accounts are savings vehicles available to individuals covered by an employer sponsored “high-deductible health plan.” *See id.* at 621. If participants contribute to the account in excess of their expenses, they are able to accumulate funds to be used during retirement. *See id.* at 623. Distributions from the HSA retirement account are tax-free if used for health care and there is not minimum lifetime distribution requirement. *See id.*

293. *See* JOINT COMM., ESTIMATES OF TAX EXPENDITURES FOR FISCAL YEARS 2010-2014, *supra* note 227, 49-50. The Joint Committee Print incorporates the extension of the 2001 and 2003 Bush era tax cuts that would decrease the amount of the tax expenditures for calendar years 2011 and 2012. *See id.* at 1-2; *see also* JOINT COMM. ON TAXATION, ESTIMATED BUDGET EFFECTS OF THE “TAX RELIEF, UNEMPLOYMENT INSURANCE REAUTHORIZATION, AND JOB CREATION ACT OF 2010” SCHEDULED FOR CONSIDERATION BY THE UNITED STATES SENATE FISCAL YEARS 2011-2020 1-2 (Comm. Print 2010).

294. *See* STANLEY S. SURREY, PATHWAYS TO TAX REFORM: THE CONCEPT OF TAX EXPENDITURES 136 (1973) (using a number of tax expenditures to illustrate that “tax incentives make high-income individuals still better off and result in the paradox that we achieve our social goals by increasing the number of tax millionaires”).

295. *See id.* “This criticism — that tax incentives produce inequitable effects and upside-down benefits — is valid as to the general run of tax incentives.” *Id.* Following his description of the virtues and vices of tax incentives Professor Surrey concludes:

[T]he asserted disadvantages — waste, inefficiency, and inequity — are true of most tax incentives existing or proposed because of the way they are structured or grew up. The whole approach to tax incentives — one of rather careless or loose analysis, failure to recognize that dollars are being spent, or to recognize the defects inherent in working within the constraint of the positive tax system — has produce very poor programs. But *if* the problems were recognized and *if* care were taken to design tax incentive programs that one would be willing to

Social Security, the basic building block of retirement, was originally established to provide a measure of protection to prevent the average citizen from being poverty-ridden during old age.²⁹⁶ During the early 1970s, benefits were greatly increased and indexed for 100% automatic annual COLA adjustments, making Social Security “a massive and indiscriminate middle-class welfare program.”²⁹⁷ By the mid-1980s, it was obvious that long-term solvency of the system was in doubt.²⁹⁸ The result originated with the Greenspan Commission, which recommended a gradual increase in the retirement age to sixty-seven, limited taxation of benefits, and suggested an increase in the earning to be subject to the payroll tax.²⁹⁹ The result of these changes was to create a surplus that would be put into a trust fund for use when the baby boomer generation began to retire and benefit payments would exceed revenues.³⁰⁰

defend in substantive terms if the programs are cast as direct expenditures, programs, then these disadvantages would not be involved, except to the extent that they are inherent in Government assistance itself.

Id. at 140 (emphasis in original). The National Commission on Fiscal Responsibility and Reform reached a similar conclusion and called for the repeal of most tax expenditures. *See* Moment of Truth, *supra* note 22, at 29; *see also* JOINT COMM. ON TAXATION, ESTIMATES OF FED. TAX EXPENDITURES FOR FISCAL YEARS 2010-2014, *supra* note 227, at 33-53 (Table 1. - Tax Expenditure Estimates By Budget Function, Fiscal Years 2010-2014).

296. PETERSON, WILL AMERICA GROW UP, *supra* note 20, at 48; RAVI BATRA, GREENSPAN'S FRAUD: HOW TWO DECADES OF HIS POLICIES HAVE UNDERMINED THE GLOBAL ECONOMY 15 (2005); *see* BOLLES & NELSON, *supra* note 282, at 25-26 (suggesting that before Social Security retirement was relatively unknown and that now, as a result of increasing prosperity, retirement is so common that it taken for granted); Shaviro, MAKING SENSE OF SOCIAL SECURITY REFORM, *supra* note 223, at 58.

297. PETERSON, WILL AMERICA GROW UP, *supra* note 20, at 94-95, 98-99. Peterson indicated that many of these changes were enacted with little or no debate in Congress. *Id.* at 99-101.

298. BATRA, *supra* note 296, at 16, 26-27 (suggesting that the national alarm at the long-term under funding of Social Security was generated by politicians for the purpose of bringing down the budget deficit without raising the income or corporate tax).

299. *Id.* at 17-18. Batra sees the results of the Greenspan Commission as a fraud because the revenues were used to fund general budget shortfalls. *Id.* at 19. However, Michael Graetz sees the commission as a model that could be used to solve the present problem. GRAETZ, UNNECESSARY RETURNS, *supra* note 22, at 135.

300. BATRA, *supra* note 296, at 18-19. *But see* Krauthammer, *Will Voters Buy Hoax*, *supra* note 54, at A15; Charles Krauthammer, *Social Security: A Classic Case of Debt Denial*, INVESTORS BUS. DAILY, Mar. 21, 2011, at A19 [hereinafter Krauthammer, *Debt Denial*] (refuting the claim that the Social Security trust fund is solvent through 2037). It is argued that for the last twenty-five years, the general treasury has raided the Social Security trust fund by borrowing the surplus. BATRA, *supra* note 296, at 21. This has been refuted on the basis that such borrowing will be repaid with interest and that by supplementing the income of Social Security beneficiaries with general revenues the contrary is true that the Social Security system has raided the general treasury. Viard, *supra* note 54, at 945-48. This occurs, for example, by allowing a deduction for the employer contribution to Social Security and one-half the self-employment tax. *Id.* at 947-48.

Social Security is divided between Old Age and Survivors Insurance (OASI) and Disability Insurance (DI), which are often combined and designated as OASDI.³⁰¹ Employee and matching employer contributions totaling 15.3% of covered payroll are divided between OASI at 5.3% and DI at 0.9% each.³⁰² Separate trust funds are maintained for OASI and DI.³⁰³ The Trustees' 2011 Report indicates that the OASI trust fund will be exhausted in 2036 and the DI trust fund in 2018.³⁰⁴

Social Security is considered the most successful entitlement program and has been said to demonstrate that a highly regressive tax can be used to provide a highly progressive benefit schedule.³⁰⁵ That Social Security provides a universal benefit that is not means tested has accounted for its near uniform support. Critics have pointed out the following: 1) the real rate of return of Social Security is between 1 and 2% compared to at least 7% in the market since 1926; 2) the current system is unfair to minorities whose life expectancies are shorter than non-minorities; 3) workers have no legal rights to the monies paid into Social Security; and 4) Social Security benefits are not inheritable.³⁰⁶ Because of these criticisms and projected

301. BD. OF TRS., *supra* note 54, at 1.

302. *Id.* at 5.

303. *Id.* at 1.

304. *Id.* at 3.

305. GRAETZ, UNNECESSARY RETURNS, *supra* note 22, at 131.

306. *Roadmap*, *supra* note 142, at 34-35; see *Moment of Truth*, *supra* note 22, at 55 fig.13. The estimated real return on Social Security for the average individual currently paying into the system is 1% to 2%, whereas for younger workers the return is likely to be negative. *Roadmap*, *supra* note 142, at 34. Further, the real rate of return is higher for low-wage workers and lower for high-wage workers because of the progressive nature of the benefit scheme. DANIEL SHAVIRO, MAKING SENSE OF SOCIAL SECURITY REFORM, *supra* note 223, at 74 ("The existing Social Security system also engages in considerable redistribution, an area of greater overlap with other tax-transfer programs such as the income tax and welfare systems. Here, Social Security appears on balance to transfer resources in the right direction (from richer to poorer people) due to its effects both within a given age cohort under constant tax and benefit rules, and between age cohorts given how these rules have changed over time. . . ."). See LIPMAN & WILLIAMSON, *supra* note 56, at 11 (discussing the calculation of Social Security benefits). A single, sixty-four-year-old man with an average lifetime wage of \$43,100 who invested his lifetime Social Security and Medicare taxes into a fund earning a 2% real annual rate of return, once he turned sixty-five and calculated the present value of his expected return discounted at a rate of 2% real interest rate, the value of the Social Security taxes in the fund would be \$290,000 and the value of the expected Social Security benefits would be \$256,000, whereas the value of his Medicare taxes in the fund would be \$55,000, and the value of the expected Medicare benefits would be \$161,000 for a total amount in the fund of \$345,000 and a total combined benefit of \$417,000. See C. Eugene Steuerle & Stephanie Rennane, *Social Security and Medicare Taxes and Benefits over a Lifetime*, URBAN INSTITUTE, June 2011, tbl.2, <http://www.urban.org/url.cfm?ID=1000455>. Steuerle and Rennane provide additional examples for a single female, different marital statuses, earnings levels, and different years at which the recipient turned 65. *Id.* at tbls. 2-9.

shortfalls in revenues, proposals have been made to allow participants to elect to contribute a portion of their Social Security taxes to private investment accounts while protecting the individual with a limited federal guarantee.³⁰⁷ President Bush made such a proposal in 2005 but failed to garner sufficient Congressional support³⁰⁸ because such proposals (referred to as “privatization” proposals) are seen as undermining the basic purpose of the Social Security system.³⁰⁹ Furthermore, making up for the revenue shortfall when funds are diverted to investment funds is impractical.

Plans to stabilize Social Security funding generally focus on increasing the retirement age up to age seventy, raising the wage base on which the tax is levied to include 90% of all wages, increasing the tax rate to 15%, and means testing the benefit.³¹⁰ The immediate problem for the federal budget is not that the Social Security trust fund will be exhausted in 2040, but that the trust funds have no actual funds and must be repaid from general revenues, thereby increasing the pressure on the federal government to borrow.³¹¹

307. See, e.g., *Roadmap*, *supra* note 142, at 53-54.

308. GRAETZ, UNNECESSARY RETURNS, *supra* note 22, at 23.

309. Patricia E. Dilley, *Taking Public Rights Private: The Rhetoric and Reality of Social Security Privatization*, 41 B.C. L. REV. 975, 1014-15 (2000) (“Possibly the most important conclusion that can be drawn from looking at these arguments as a whole is that the private account system has a fundamentally different purpose, as well as a different ethos, from that of Social Security. All of the advantages claimed by the private account system over the public system derive from individual risk, trading the surety of at least moderate income that has underwritten the modern institution of retirement for the possibility of greater wealth in retirement (and in inheritance). Adequate retirement income is assumed as a necessary byproduct of the superior capital accumulation of the private account system, and the risk of not having sufficient equity to last until death is deemed worth taking for the sake of greater potential returns.”); Lewis D. Solomon & Geoffrey A. Barrow, *National Issues: Privatization of Social Security: A Legal and Policy Analysis*, 5 KAN. J.L. & PUB. POL’Y 9, 17 (1995) (stating that “[f]ull privatization has been attacked as radical and reckless by powerless lobbies intent on preserving the status quo”).

310. See PETER A. DIAMOND & PETER R. OSZAG, *SAVING SOCIAL SECURITY: A BALANCED APPROACH* vii-xxiv (2005); PETERSON, *WILL AMERICA GROW UP*, *supra* note 20, at 167-73.

311. See PETERSON, *WILL AMERICA GROW UP*, *supra* note 20, at 44 (suggesting the so-called “trust fund” should be called the “distrust fund”); Krauthammer, *Will Voters Buy Hoax*, *supra* note 54, at A15; Krauthammer, *Debt Denial*, *supra* note 300, at A19 (stating the Social Security trust fund contains essentially nothing because it is funded by “special issue bonds” or “intergovernmental bonds” that have no real economic value); Sean Higgins, *Defenders Say Social Security is Healthy*, INVESTORS BUS. DAILY, May 17, 2011, at A1 (noting that, although the government will have to borrow \$5 trillion to repay the principal and interest in the trust fund to maintain benefits, once trust fund is exhausted, presumably in 2035, benefits would have to be automatically cut unless Congress acts to restore them).

Everyone needs retirement security, but the government's refusal to make the program actuarially sound leaves everyone in doubt about the likelihood they will enjoy a comfortable retirement. Indeed, government-generated inflation (particularly medical inflation) and erratic tax policy challenges even the most sophisticated retiree. Perhaps we should inform the average man that he will need \$2 million to retire comfortably and urge him to begin saving immediately.

G. *The Value-Added Tax (the "VAT") as a Second Income Tax*

By dominating housing, education, health care, and retirement, the federal government has transformed itself into the trustee of a discretionary support trust distributing trillions of dollars annually for the health, support, maintenance, and welfare of its wards, the American public.³¹² Carrying such burden and seemingly unable to turn down any request for additional support, it is no surprise that government is seeking additional sources of revenue. The income tax has such complexity that an estimated \$300 billion annual "tax gap"³¹³ of uncollected tax has been created. Believing that the income tax cannot be fixed, there are many voices lining up to support the introduction of a value-added tax ("VAT") in the United States.³¹⁴

Three of the four comprehensive plans considered in the prior part of this article proposed the adoption of a VAT as a solution for the short fall in revenues. Only the Deficit Commission failed to recommend a VAT, preferring instead to eliminate most tax expenditures as a way to lower income tax rates.³¹⁵ Of those proposing a VAT, it is presented as a simple solution merely to create a federal sales tax because it is consistent with the tax systems of our principal trading partners.³¹⁶ However, each proposal must grapple with the more complex issue of how to alleviate the regressive nature of a VAT. A simple VAT, like a simple income tax, is considered an unfair

312. See Domenici & Rivlin, *supra* note 22, at 88-90 (describing the impact of tax expenditures on housing, education, health care, and retirement and the listing of numerous direct spending programs funded at over \$1 billion in these areas in 2010).

313. GRAETZ, UNNECESSARY RETURNS, *supra* note 22, at 88.

314. See generally Harley Duncan & Walter Hellerstein, *VAT and the Tax-Exempt Sector: Unique U.S. Issues*, 129 TAX NOTES 1373, 1373 (2010) (addressing issues on how to handle goods and services provided by non-profit and governmental entities under a VAT).

315. Drew Pierson, *VAT Lacked Support on Fiscal Commission, Odintz Says*, 129 TAX NOTES 1301, 1301 (2010).

316. GRAETZ, UNNECESSARY RETURNS, *supra* note 22, at 80.

tax.³¹⁷ To alleviate the unfairness, the VAT becomes ever more complex, as it is riddled with exempt products, reduced rates, rebates, and exempt individuals.³¹⁸ Keeping the tax base broad and the rate low may seem simple, but is really quite difficult.

Advantages generally associated with a VAT are that it does not include tax savings and investment, does not provide an incentive to shift investment overseas, does not affect the cost of producing various goods, and is easily coordinated with tax systems of other nations.³¹⁹ In particular, the VAT can be rebated on exports and will be charged against imported goods.³²⁰ Most plans follow the practice of countries recently adopting VATs and propose using a broad base for their consumption tax to avoid the complexities experienced by countries that have allowed their VATs to be riddled with exemptions.³²¹

There is some thought that the states will welcome the VAT because it would be an opportunity to expand their sales tax base that has been eroded by things such as internet sales.³²² Moreover the states can piggyback their sales tax, which may have the tendency to limit the growth of the tax rate.³²³

Most arguments for the adoption of a VAT have not changed since the 1970s. Back then Stanley Surrey, a former Assistant Secretary of the Treasury and originator of the Tax Expenditure Budget, argued that the United States had the most efficient tax collection in the world and adoption of a VAT would be an administrative step backward.³²⁴ What may have changed today is that the excessive use of the income tax system to solve every social and economic problem has undermined the efficiency of our once heralded voluntary tax collection system.³²⁵ On balance, the

317. Domenici & Rivlin, *supra* note 22, at 40-41 (discussing the regressive burden of the tax and arguing that merely substituting a sales tax for an income tax would continue to make the tax system less progressive).

318. See GRAETZ, UNNECESSARY RETURNS, *supra* note 22, at 165-67.

319. Domenici & Rivlin, *supra* note 22, at 39; see also GRAETZ, UNNECESSARY RETURNS, *supra* note 22, at 211-12 (arguing that his "Competitive Tax Plan" would make the United States one of the most attractive countries for saving and investing in the world).

320. Domenici & Rivlin, *supra* note 22, at 40. The Task Force is quick to point out that, contrary to some assertions, this rebate does not constitute an export subsidy or import tax under international trade agreements. *Id.*

321. *Id.* (identifying Australia, Canada, and New Zealand as having recently adopted the tax and Great Britain and France as having adopted the tax earlier).

322. See *id.* at 41.

323. *Id.*

324. Gordon T. Butler, Comment, *The Value-Added Tax: A New \$40 Billion Tax for the United States?*, 50 TEX. L. REV. 267, 303 (1972).

325. See Alan Schenk, *Prior U.S. Flirtations With VAT*, in THE VAT READER – WHAT A FEDERAL CONSUMPTION TAX WOULD MEAN FOR AMERICA 52, 54-55 (Tax Analysts, 2010)

default position may be that adopting a new tax is politically easier than eliminating the complexity of the income tax.

H. *Congressional Ability to Keep Any Plan of Action*

One of the most important questions in any solution is Congressional ability to follow through and not alter and undermine any course of action determined. Certainly emergencies are reason to alter course, but not every unexpected event is an “emergency” calling for modification of the planned budget. The deficits caused by President Reagan’s tax cuts in 1981 took nearly twenty years to erase after adding more than \$7 trillion to the national debt.³²⁶ In an effort to control these deficits, Congress first enacted the Gramm-Rudman-Hollings Balanced Budget Act of 1985,³²⁷ then the Budget Enforcement Act of 1990,³²⁸ the tax increases under the Omnibus Budget

(describing prior considerations of a VAT for the U.S. as a replacement for the income tax); *see also* GRAETZ, UNNECESSARY RETURNS, *supra* note 22, at 213 (arguing that his Competitive Tax Plan would use the “time-tested” VAT to stabilize government funds).

326. *See* GRAETZ, UNNECESSARY RETURNS, *supra* note 22, at 19 (pointing to President Reagan’s borrowing and spending policies as the origin of the current national debt). Graetz notes that the Treasury department has concluded that “a permanent reduction in taxes . . . would lead to an unsustainable accumulation of debt.” *Id.* at 21 (quoting OFFICE OF TAX ANALYSIS, U.S. DEP’T OF THE TREASURY, A DYNAMIC ANALYSIS OF PERMANENT EXTENSION OF THE PRESIDENT’S TAX RELIEF 5 (2006)). One author reflected on the efforts to reign in uncontrollable deficits as follows:

Bipartisanship succeeded in 1997 because the American people were squarely behind the goal of a balanced budget. Following the fiscal implosion of 1981, budgetary responsibility became a driving domestic political force. In the 1980s, not a year went by without congressional leaders trying to repair the damage. That momentum was amplified by the presidential campaigns of Ross Perot, the bold fiscal actions of President George H. W. Bush, the 1992 campaign of President Bill Clinton (It’s the economy, stupid!), the Democrats-alone deficit reduction of 1993, and the Republican Contract with America. Second, each party had taken its turn at deficit reduction while also trying to advance its political goals What both parties learned the hard way was that behind the laudable goal of balancing the budget were a bunch of tough policy choices guaranteed to make many important constituencies unhappy

JOHN L. HILLEY, THE CHALLENGE OF LEGISLATION: BIPARTISANSHIP IN A PARTISAN WORLD 226 (2007).

327. Balanced Budget and Emergency Deficit Control Act of 1985, Pub. L. 99-177, Title II, 99 Stat. 1038 (1985) (codified as amended at 2 U.S.C. § 901 (2011)); Senate Budget Committee, *Committee History*, para. 13, <http://www.senate.gov/democratic/index.cfm/committee-history> (last visited Nov. 19, 2011); *see also* Emergency Deficit Control Reaffirmation Act of 1987, Pub. L. 100-119, Title I, 101 Stat. 754 (1987)(codified as amended at 2 U.S.C. § 901 (2011)).

328. Omnibus Budget Reconciliation Act of 1990, Pub. L. 101-508, 104 Stat. 1388 (1990). The Act enacted budget caps on annually appropriated spending and a “pay-as-you-go” (“PAYGO”) process under which spending increases must be accompanied by a tax increase or spending cut and a tax cut must be accompanied by a spending cut or a tax increase elsewhere. *Id.* at § 13204.

Reconciliation Act of 1993,³²⁹ and finally the Balanced Budget Act of 1997,³³⁰ a compromise between President Clinton and the Republican Congress.³³¹ These efforts resulted in about four years of modest budget surpluses³³² and a projection of a \$5.7 trillion unified budget surplus at the time of President George W. Bush's inauguration.³³³

329. Omnibus Budget Reconciliation Act of 1993, Pub. L. 103-66, 107 Stat. 312 (1993).

330. Balanced Budget Act of 1997, Pub. L. 105-33, 111 Stat. 251 (1997).

331. See generally HILLEY, *supra* note 326, at 226-27 (describing the political and economic considerations that resulted in the Balanced Budget Act of 1997).

332. Whether the "fleeting emergence of the budget surplus" by 2000 was the result of the Budget Act of 1997 was the subject of dueling editorials. Compare Newt Gingrich, *Gingrich: If it comes to a Shut Down, the GOP hould Stick to its Principles*, WASH. POST, FEB. 27, 2011, para. 14, www.washingtonpost.com/opinions/gingrich-if-it-comes-to-a-shutdown-the-gop-should-stick-to-its-principles-/2011/02/24/ABju26L_story.html (claiming the failed government shutdown in 1995 set the stage for the historic success of the Balanced Budget Act of 1997 that led to the first four consecutive years of budget surpluses since the 1920s), with Robert S. McIntyre, *McClatchy: Sorry, Newt. You Never Balanced the Budget*, CITIZENS FOR TAX JUSTICE, paras. 4-5 (Mar. 18, 2011, 10:37 AM), http://www.centredaily.com/2011/03/15/258471_sorry-newt-you-never-balanced.html (claiming the stage was set for the surpluses prior to passage of the Balanced Budget Act of 1997 and, in fact, that act contributed to the lessening of the surpluses during those years); see also Robert S. McIntyre, *Remembering the 1986 Tax Reform Act*, 133 TAX NOTES 351, 357 (2011) (repeating the claim of his op-ed piece); JOEL SLEMROD & JON BAKIJA, TAXING OURSELVES: A CITIZEN'S GUIDE TO THE DEBATE OVER TAXES 26 (2008) (calling the surpluses "fleeting"); DANIEL N. SHAVIRO, TAXES, SPENDING, AND THE U.S. GOVERNMENT'S MARCH TOWARD BANKRUPTCY 140-46 (2007) [hereinafter SHAVIRO, MARCH TOWARD BANKRUPTCY] (describing the efforts, primarily in the 1980s and 1990s, to use budgetary rules to return the nation to a balanced budget). For fiscal years 1998-2001, the federal budget showed surpluses of \$69.3, \$125.6, \$236.2, and \$128.2, respectively (in billions of dollars), but only in 1999 and 2000 were there "modest" On-Budget surpluses of \$1.9 billion and \$86 billion, respectively. Office of Management and Budget, Historical Table, Table 1.1- Summary of Receipts, Outlays, and Surpluses or Deficits: 1789-2016, www.whitehouse.gov/omb/budget/Historicals (last visited Oct. 22, 2011). The Off-Budget Surpluses (primarily Social Security surpluses) for the four fiscal years were \$99.2, \$123.7, \$149.8 and \$160.7, respectively (in billions of dollars). *Id.* Among other notable provisions, the Balanced Budget Act of 1997 contained the Sustainable Growth Rate Formula that sets limits on doctor's reimbursement under Medicare. *Moment of Truth*, *supra* note 22, at 36. Although the formula was projected to save significant revenues in Medicare by 2002, the complexity and volume of physician's services led Congress in 2003 and subsequent years to limit the amount of cuts under the formula. William M. VanDenburgh and Nancy B. Nichols, *Fiscal Commission's Report Frames budgetary Debate*, 130 TAX NOTES 447, 449 (2011) (recognizing that congressional budgets play a "game" in assuming certain health care cost savings, such as that from the Sustainable Growth Rate Formula that they know will never be realized); *Moment of Truth*, *supra* note 22, at 36-37 (assuming a permanent fix to the Sustainable Growth Rate Formula that requires unrealistic cuts in physician reimbursements); see also *id.* at 10 (noting that the CBO's Alternative Fiscal Scenario reflects current policy which is the current baseline adjusted for the likely continuation of the Bush income and estate tax cuts, the AMT fix, and the Medicare "Doc Fixes").

333. Warren Rojas, *Bush Stays Strong on Tax Cut, Outlines Budget*, 130 TAX NOTES 1127, 1127 (2001).

At the time of President Bush's inauguration, Chairman Greenspan was wondering what to do when the national debt was paid off. He did not have to wonder long, as President Bush's 2001 and 2003 tax cuts, unpaid-for wars in Iraq and Afghanistan, unpaid-for drug benefits under Medicare, and other actions not only consumed the projected surplus but resulted in deficits that grew the national debt an additional \$5 trillion.³³⁴ That trend would continue under President Obama and thereafter into the indefinite future.³³⁵

The Tax Reform Act of 1986 was viewed as a bipartisan legislative triumph of base broadening and rate lowering.³³⁶ The results were tax rates of 15% and 28%, capital gains being taxed as ordinary income, real estate tax shelters being shut down by new passive activity loss limitations, the deduction of state sales tax and consumer loan interest were eliminated, among other significant changes.³³⁷ The 1986 Act was revenue and distribution neutral.³³⁸ While many commentators consider the 1986 Act as a triumph of bipartisan politics,³³⁹ its primary changes were rapidly undermined.³⁴⁰ President George H. W.

334. See SHAVIRO, *MARCH TOWARD BANKRUPTCY*, *supra* note 332, at 72-75 (providing a "capsule history" of budget deficits); see also Ezra Klein, *Doing the math on Obama's deficits*, WASHINGTONPOST.COM, Jan. 31, 2012, para. 15, http://www.washingtonpost.com/business/economy/ezra-klein-doing-the-math-on-obamas-deficits/2012/01/31/gIQAnRs7fQ_story_1.html (finding that "beginning in 2001 and ending in 2009, George W. Bush added more than \$5 trillion to the deficit").

335. See CONG. BUDGET OFFICE, *THE BUDGET AND ECONOMIC OUTLOOK: FISCAL YEARS 2011 TO 2021*, 20 tbl.1-6, 133 tbl.E-1 app. E (2011); *Moment of Truth*, *supra* note 22, at 10 ("We have arrived at the moment of truth, and neither political party is without blame.").

336. Meg Shreve, *Tax Analyst Exclusive: Conversations: Bill Bradley*, 133 TAX NOTES 303, 303 (2011); cf. JEFFREY H. BIRNBAUM & ALAN S. MURRAY, *SHOWDOWN AT GUCCI GULCH: LAWMAKERS, LOBBYISTS, AND THE UNLIKELY TRIUMPH OF TAX REFORM* xiv (1987). Senator Bradley, a Rhodes scholar and former star forward for the New York Knickerbockers professional basketball team, initiated the discussion of tax reform in 1982 with his proposal to sharply reduce rates and broaden the tax base by eliminating many tax preferences and advocated for it for four years before it was finally enacted. *Id.*; see also SHELDON D. POLLACK, *THE FAILURE OF U.S. TAX POLICY: REVENUE AND POLITICS* 98-106 (1996) (observing that the Tax Reform Act of 1986 has "been widely hailed as the most significant tax-reform legislation in the history of the federal income tax"); Michael J. Graetz, *Tax Reform 1986: A Silver Anniversary, Not a Jubilee*, 133 TAX NOTES 313, 313 (2011) [Hereinafter Graetz, *Tax Reform*].

337. Graetz, *Tax Reform*, *supra* note 336, at 315-18 (generally discussing the provisions of the act and their importance to tax policy).

338. *Id.* at 315.

339. See, e.g., *id.* at 314 (stating "TRA 1986 was the product of an uneasy marriage of two contrary ideological and political camps"); BIRNBAUM & MURRAY, *supra* note 336, 280-90.

340. See Victor Thuronyi, *Progressive Corporate Tax Reform*, 130 TAX NOTES 1303, 1304 (2011); Graetz, *Tax Reform*, *supra* note 336, at 318 ("The complexity of the 1986 act, coupled with its failure to adopt and maintain a coherent vision of equity, made it

Bush introduced a 31% rate in 1990 that likely cost him reelection in 1992.³⁴¹ President Clinton raised rates by introducing 33%, 36%, and 39.6% rates in 1993³⁴² and compromised with Republicans to enact significant reductions in capital gains rates in 1997.³⁴³ Professor Graetz was no fan of the 1986 Act and points to the ease with which it was unwound as a reason to support his Competitive Tax Plan, which he believes would provide a more stable system than has been heretofore implemented.³⁴⁴

These incidents demonstrate the difficulty in achieving permanent reform through Congress. Following the Commission's report calling for \$4.0 trillion in deficit reduction through 2020,³⁴⁵ Congress and the President proceeded immediately to pass an extension of the Bush Era tax cuts for two years with other changes to the tax code at a cost of \$857

unstable. Even if it would, Congress could not resort to principle as a basis for resisting change."). Graetz concludes, "The 1986 tax reform gave our income tax a good cleansing, but its ink had hardly dried before Congress started adding new tax breaks and raising rates." *Id.* at 321.

341. Omnibus Budget Reconciliation Act of 1990, Pub. L. No. 101-508, 104 Stat. 1388 [hereinafter OMBR 1990]; SLEMROD & BAKIJA, *supra* note 332, at 26; MICHAEL J. GRAETZ, *THE U.S. INCOME TAX: WHAT IT IS, HOW IT GOT THAT WAY, AND WHERE WE GO FROM HERE* 162-63 (1999). OMBR 1990 reintroduced a capital gains rate differential by keeping the maximum capital gains rate at 28% when it raised the maximum rate on ordinary income to 31%. Andrew J. Hoerner, *Taxes Raised 'Marginally' on Well-To-do Filers*, 49 TAX NOTES 599, 599 (1990); Sheldon Pollack, *Revenge of the 80th Congress*, 129 TAX NOTES 819, 823 (2010); Graetz, *Tax Reform*, *supra* note 336, at 316. OMBR 1990 also lifted the cap on Medicare wages from \$53,400 to \$125,000. See Ian K. Loudon, *Bush Quietly Signs Budget Bill*, 49 TAX NOTES 744, 744 (1990). Historic Medicare tax rates are found at <http://www.ssa.gov/OACT/ProgData/taxRates.html> (last visited Feb. 4, 2012) and historic Medicare wage base subject to such tax rates which was the same as that for OASDI from 1966 until 1990 when it was raised to \$125,000 for 1991, \$130,200 for 1992, and \$135,000 for 1993, are found at <http://www.ssa.gov/OACT/COLA/cbb.html> (last visited Feb. 4, 2012). The wage cap was eliminated by the Omnibus Budget Reconciliation Act of 1993, Pub.L. No. 103-66, 107 Stat. 312, § 13207 ("OMBR 1993"); see Tax Analysts, *Special Supplement: A Tax Bill Baedeker – A Guide to the 1993 Tax Law*, 60 TAX NOTES 812, 821 (1993).

342. Tax Analysts, *Special Supplement: A Tax Bill Baedeker – A Guide to the 1993 Tax Law*, 60 TAX NOTES 812, 815 (1993); SLEMROD & BAKIJA, *supra* note 332, at 26.

343. Taxpayer Relief Act of 1997, Pub. L. No. 105-34, 111 Stat. 788; see McIntyre, *Sorry, Newt*, *supra* note 332, para. 9.

344. GRAETZ, *UNNECESSARY RETURNS*, *supra* note 22, at 26-27. He further states:

Even those who applauded the 1986 act as a wildly successful tax reform must concede now that this legislation was not a stable solution. Over time, many of its reforms have been reversed. Its broad income tax base and low rates have been transformed into a narrower base with higher rates. How can anyone remain optimistic about fixing the income tax without radical surgery? What the nation needs is a new and better tax system, one that is far simpler, less intrusive for the American people, fair, and more conducive to savings, investment and economic growth.

Id. at 103.

345. *Moment of Truth*, *supra* note 22, at 14.

billion.³⁴⁶ The important point is that structural changes are required to make it difficult to deviate from the plan.

I. *Return to the 1990s Budget Enforcement*

The Commission wants to enforce its spending caps by allowing the Senate a point of order to recommit any bill exceeding prescribed budget caps and by requiring the CBO to abate spending that exceeds those caps.³⁴⁷ It also requires the President to propose annual war spending limits, budget honestly for catastrophes, and eliminate the abuse of emergency spending to avoid caps.³⁴⁸ The Commission would require tax increases as well as spending cuts, but would require that the spending cuts come first.³⁴⁹ Professor Graetz is skeptical that Congress will observe any general tax reform, but believes that introducing a \$100,000 exemption to the income tax will be a sufficiently high level to make tax expenditures less attractive.³⁵⁰ Further, he believes that setting the rate of the VAT at 10% to 14% would be sufficiently high to make it politically unpalatable to try and justify a further rate increase.³⁵¹ If the state sales tax rate is added to the national VAT in the United States, the total sales tax would approach 20%, which would be consistent with

346. JOINT COMM. ON TAXATION, ESTIMATED BUDGET EFFECTS OF THE “TAX RELIEF, UNEMPLOYMENT INSURANCE REAUTHORIZATION, AND JOB CREATION ACT OF 2010,” SCHEDULED FOR CONSIDERATION BY THE UNITED STATES SENATE, FISCAL YEARS 2011-2020 8 (2010) [hereinafter JOINT COMM. ON TAXATION, FISCAL YEARS 2011-2020]; see Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010, Pub. L. No. 111-312, 124 Stat. 3296.

347. *Moment of Truth*, *supra* note 22, at 22.

348. *Id.* at 22-24.

349. *Id.* at 28. This is reminiscent of President Reagan’s 1981 and President George W. Bush’s 2001 tax cuts that promised spending cuts that never materialized. See, e.g., McIntyre, *Remembering the 1986 Tax Reform Act*, *supra* note 332, at 352 n.4; Tax Analysts, *Undaunted, Republicans Push Tax Cuts While Deficit Projections Grow*, 96 TAX NOTES 1285, 1285 (2002); see also Stephen E. Shay, *Jobs, Deficit Reduction, Revenues, and Fundamental Tax Reform*, 133 TAX NOTES 213, 215 & n.18 (2011) (noting the impracticality of relying solely on spending cuts to restore fiscal balance).

350. See GRAETZ, UNNECESSARY RETURNS, *supra* note 22, at 105-06.

By eliminating 100 million tax returns a year, the plan would drastically reduce compliance costs and headaches for the American people. . . . No politician would ever urge bringing all these people back into the income tax, absent some genuine catastrophe. After all, it took World War II to persuade Congress originally to extend the income tax to the masses.

Id. at 210.

351. See *id.* at 211 (“Starting, as I have proposed here, with a 10 to 14 percent VAT to fund income tax relief greatly reduces the opportunities for the federal government to use the VAT as a pocketbook for additional spending. I have urged that we enact a VAT rate high enough (given existing state sales taxes) to leave only a relatively limited scope for future increases.”).

the rate in effect in many European countries.³⁵² The Peterson-Pew Commission on Budget Reform issued a report in November 2010 addressing these issues and suggested setting binding limits on tax expenditures.³⁵³ It also suggested that if Congress exceeded the budget goals, tax increases would take effect automatically through the use of a debt trigger.³⁵⁴ As noted above, each of the plans discussed emphasize the need for enforceable mechanisms to prevent Congress from circumventing the limits. In this regard, there are numerous proposals for a balanced budget amendment to the U.S. Constitution as the most effective way to restrain Congressional spending.³⁵⁵

J. *Retirement and Health Care Planning is Challenging
Even for the Experts*

Planning for retirement is a complex matter. Prior to the enactment of the Employee Retirement Income Security Act of 1974 (“ERISA”), an employer could institute a defined benefit pension plan for its employees and had great flexibility on making provision to pay a retirement benefit to his employees when they reached a certain age or fulfilled certain longevity requirements.³⁵⁶ After ERISA, with its minimum funding

352. *Id.* at 189 (noting that a federal sales tax could “readily coexist” with state sales taxes and that states could easily “piggyback” the federal sales tax). VAT rates in some of America’s trading partners include: Belgium, 21%; China, 17%; France, 19.6%; Germany, 19%; Greece, 19%; Ireland, 21.5%; Israel, 15.5%; Japan, 5%; Spain, 16%; and United Kingdom, 15%. See Leah Durner, Bobby Bui, and Jon Sedon, *Why VAT Around the Globe?* 125 TAX NOTES 929, 933-34 (2009) (listing VAT rates of other countries). The article describes the experience of Australia, Canada, and India, three countries with sub-national independent taxing authorities that recently adopted VATs, Australia, 2000, 10%; Canada, 1991, 5%; and India, 2005, 12.5% and suggests that their experience would be applicable to the United States. See *id.* at 931-34.

353. See Eric Kroh, *Fiscal Commission Draft Would Eliminate All Tax Expenditures*, 129 TAX NOTES 755, 756 (2010); see also The Peterson-Pew Comm’n on Budget Reform, *Getting Back in the Black*, 8, 30-31 (2010).

354. See *id.* at 9 box 3, 15. The report also provides a history of budget enforcement acts and budget triggers. See *id.* at 10 box 4, 16-17 box 6.

355. See Drew Pierson, *No Debt Ceiling Endgame in Sight as Tax Push is Abandoned*, 132 TAX NOTES 470, 471 (2011); Richard J. Cebula, *The Pursuit of an Effective Balanced Budget Amendment*, 132 TAX NOTES 1046, 1047-49 (2011).

356. See Kathryn J. Kennedy, *Pension Funding Reform: It’s Time to Get the Rules Right (Part I)*, 108 TAX NOTES 907, 909-10 (2005). Employers had numerous ways to fund retirement obligations including a PAYGO, which could create problems for the employer if too many employees began collecting pensions. See *id.* at 910. Perhaps a better approach would be for the employer to accumulate a lump sum to pay to the employee at retirement. See *id.* at 910-11. With the passage of ERISA, with its “actuarially sound principles” for minimum funding levels on defined benefit plans, termination provisions, and certain guarantees, the employer had a whole new set of rules to follow in establishing the defined benefit plan. *Id.* at 909 & n.8. Kennedy states that “Congress intended that pension plans should be funded in a regular fashion.” *Id.* at n.8.

requirements, the employer will find that his funding costs vary because of changing ages and salaries of employees, asset valuations, as well as amortization of anticipated unfunded actuarial liabilities imposed all of which imposed significant burdens on the employer and some uncertainty on the part of the employee.³⁵⁷ Then if the employer has promised retiree health coverage, it must consider the projected rate of growth in the cost of health care.³⁵⁸ As is evident from the record of bankruptcy and near bankruptcy, these retiree costs overwhelm private employers, labor unions, state governments, and the federal government.³⁵⁹ Examples from Europe are Greece and France,³⁶⁰ but states like California are also straining under the weight of retiree obligations.³⁶¹ One wonders at the liberality of states that greatly expanded benefits using inflated return on investment calculations to justify the expansion during prosperous 1990s, as if the stock market would show double-digit returns forever.³⁶²

The trend away from defined benefit plans to defined contribution plans is a reflection of the uncertainty faced by corporate pension managers.³⁶³ The risk of loss is being shifted to the individual in an effort to limit the employer's responsibility to a fixed payment, leaving the planning of an investment risk to

357. See *id.* at 912.

358. See TERESA GHILARDUCCI, WHEN I'M SIXTY-FOUR: THE PLOT AGAINST PENSIONS AND THE PLAN TO SAVE THEM 229 (2008).

359. See Kathryn J. Kennedy, *The Demise of Defined Benefit Plans for Private Employers*, 121 TAX NOTES 179, 180 (2008) [hereinafter Kennedy, *Defined Benefit Plans*]. In 2004, the Pension Benefit Guarantee Corporation established under ERISA to guarantee private pensions estimated that pension plans of financially weak companies were unfunded to the amount of \$96 billion, Congress then passed the Pension Protection Act of 2006 (P.L. 109-280) ("PPA"). *Id.* The thrust of the PPA was to accelerate the funding of certain employer plans with the result that fewer plans were being created and many plans being terminated. *Id.*

360. Buttonwood, *Old-age tension: Increasing the retirement age is inevitable and better than the alternatives*, THE ECONOMIST, Oct. 14, 2010, para. 13, <http://www.economist.com/node/17254452> (describing the global aging problem and suggesting that the raising the retirement age to age seventy is the preferable solution and almost inevitable).

361. See The Pew Center on the States, *The Trillion Dollar Gap: Underfunded State Retirement Systems and the Roads to Reform*, at 23 (2010). The pension liability for each state is itemized and the funding status noted. *Id.* at 4; Jason Hoppin, *Pain and promise of public pensions*, SANTA CRUZ SENTINEL, May 14, 2011, para. 1, http://www.santacruzsentinel.com/ci_18052701.

362. See Buttonwood, *Old-age Tension*, *supra* note 360, paras. 3-6 (discussing the underfunding of state pension funds, and identifying the year states are likely to run out of pension funds); Buttonwood, *A Trillion Here, \$500 Billion There*, THE ECONOMIST, Oct. 15, 2011, para. 1-3, www.economist.com/node/21532298 (discussing the impact of quantitative easing by central banks on the huge shortfalls in pension plans and the need for future retirees to save, particularly because the return on investment assets is low).

363. Ghilarducci, *supra* note 358, at 116-17 (describing the trend toward defined contribution plans, and the advantages and disadvantage of such plans).

the individual employee.³⁶⁴ If governments and major employers cannot carry the burden of retirement obligations, are individual in a better position to make the decisions? Possibly self-interest may be a reason to believe that they can make those decisions, particularly, if it is clear that the moneys are secure to the individual. Regardless of whether the individual wants such a responsibility, he must bear that burden if he wants a lifestyle in retirement that requires more than the modest benefit provided by Social Security.

Nevertheless, the task of planning for a couple's retirement will be daunting. The problem for the individual is determining the extent of private savings needed to fund retirement.³⁶⁵ To make that determination, the individual must project his life expectancy and that of his spouse, the rate of return on investments, the rate of inflation on expenses, the expected medical expenses, and the level of taxation.³⁶⁶

Consider a sixty-six year old married couple earning a combined \$60,000 at retirement, who desire to replace 80% of their pre-retirement earnings (\$48,000) in retirement. Assuming that each spouse's wage indexed earning had been \$30,000, their combined Social Security benefit at age sixty-six would be approximately \$30,000 annually.³⁶⁷ They estimate they need

364. *Id.* at 122-30 (describing the longevity risk, inflation risk, and investment risk, which are being shifted to the employee in a defined contribution plan). *Id.* at 112-14; Kennedy, *Defined Benefit Plans*, *supra* note 359, at 200-01 (stating that there are coping strategies for companies with underfunded plans to deal with the drastic acceleration of the minimum funding rules and other provisions of the PPA); *Private Pensions For Public Spending*, INVESTORS BUSINESS DAILY, May 11, 2011, at A12, <http://news.investors.com/Article/571953/201105111841/Private-Pensions-For-Public-Spendin.htm>.

365. BOLLES & NELSON, *supra* note 282, at 23-35. The authors note three "surprises" for retirement savings that make it difficult to adequately plan: 1) maintaining your standard of living will require a higher annual income in retirement than you imagine, 2) you will probably need more years of retirement income than you think, and 3) access to medical care will cost more than you imagine. *Id.* at 40-44.

366. See Domenici & Rivlin, *supra* note 22, at 8-14 (describing the risks assumed by the employee when his employer switches from a defined benefit plan to a defined contribution plan).

367. LIPMAN & WILLIAMSON, *supra* note 56, at 10-11 (describing the method of calculating the benefit). Specifically, each spouse's AIME is \$2,500 (\$30,000 per year), so that the Primary Insurance Amount is the sum of \$674 (90% of the first \$761) plus \$556 (32% of \$1,939 [\$2,500 minus \$761]) for a total monthly benefit for each spouse of \$1,230, which is \$29,531 for the two spouses combined. *Id.* Since our couple has reached their full retirement age of 66, they qualify for full retirement benefits under Social Security; although, if they had applied between ages 62 and 66, their benefit would have been reduced by up to 75%. SOCIAL SECURITY ONLINE, *Retirement Planner, Retirement benefits by year of birth*, available at www.socialsecurity.gov/retire2/agereduction.htm (last visited Oct. 23, 2011).

\$18,000 of income each year to fulfill their retirement plans.³⁶⁸ An annuity with no guaranteed minimum payout for their joint lives paying \$18,000 annually would cost the couple \$260,000.³⁶⁹ If they wanted to provide for inflation by purchasing the annuity with a 3% annual cost of living increase, it would cost them \$350,000.³⁷⁰

Achieving this level of savings after tax would be a challenge. More than likely, the bulk of the couple's retirement funds will have been accumulated over the fifteen or twenty years prior to retirement through investment in retirement accounts over which they held investment power.³⁷¹ In an inflation free world, a couple earning an investment return of 5% per annum would need to save \$16,220 per year for fifteen years to accumulate \$350,000 if they waited until age fifty-one to begin saving for their retirement at age sixty-six.³⁷² However, if they began to save when they were twenty-five years old and saved for forty years, they would only need to save \$2,897 per year.³⁷³ Perhaps with sufficient training our couple will be capable of making and carrying out such a plan at age twenty-five.

368. The couple desires an annual income of \$48,000 for retirement and will receive \$30,000 from Social Security, leaving a need for an additional \$18,000 of income. The basic retirement formula is to "[t]ake the PIA on your AIME, adjust for your retirement age and spousal benefits, and then just index it." SHAVIRO, *supra* note 223, at 13. AIME is the average wage-indexed monthly earnings (highest thirty-five years); PIA is Primary Insurance Amount (90% of first \$749, 32% of the next 4,517, and 15% of balance up to \$7,928) and FRA is Full Retirement Age (e.g. age sixty-six for those born from 1943 to 1954, and sixty-seven for those born after 1960). LIPMAN & WILLIAMSON, *supra* note 56, at 11. The benefit formula is highly progressive such that in 2011, someone with the highest AIME of \$7,928 (\$95,136, maximum average/wage-indexed annual earnings that have been subject to Social Security tax for the last thirty-five years) would receive a benefit of \$28,704 annually (approximating 30% of his AIME), while an average wage earner with an AIME of \$4,517 (\$54,204 annually) would receive \$22,560 annually (approximating forty-two percent of his AIME), and someone with an AIME of \$30,000 would receive \$14,897 (50% of AIME). *Id.*

369. Consumer Reports Money Adviser, Immediate annuity shopping, June, 2009, at 8, 9 (indicating the cost of such an annuity in April, 2009 is \$100,000 for a monthly payment of approximately \$580).

370. *Id.* at 9 (indicating the cost of an annuity in April, 2009 is \$100,000 for a monthly payment of approximately \$425 with a 3 percent annual cost-of-living increase).

371. See Ghilarducci, *supra* note 358, at 121-22 (discussing accumulation risks such as failure to begin saving at an early age); BOLLES & NELSON, *supra* note 282, at 33-36 (discussing why it is hard to save).

372. See Future Value of Ordinary Annuity, www.principlesofaccounting.com/ART/fv.pv.tables/fvofordinaryannuity.htm (last visited Oct. 23, 2011) (using standard future value of an annuity table, the factor for fifteen periods at 5% per year is 21.57856, so that to accumulate \$350,000 to purchase an annuity would require investing \$16,220 per year for fifteen years).

373. *Id.* (using standard future value of an annuity table, the factor for 40 periods at 5% per year is 120.7998, so that to accumulate \$350,000 to purchase an annuity would require investing \$2,897 per year for forty years).

K. *Will the 112th Congress Address the Debt Crisis?*

Throughout the 2010 midterm election season, Republican candidates called for significant spending cuts to reduce the federal deficit and for the permanent extension of the 2001 and 2003 Bush era tax cuts.³⁷⁴ Oblivious to their inconsistency, Republican candidates in 2010 could give no credible response when questioned about which programs could be cut or why extending the tax cuts, estimated to cost \$4.0 trillion over ten years, would not undermine their goal of deficit reduction.³⁷⁵

In December 2010, after the Fiscal Commission issued its report, *Moment of Truth*, calling for action to reduce the deficit by \$4.0 trillion by 2020, Senate Republicans, during the lame duck session, refused to allow any legislation through the Senate until the Bush era tax cuts were extended.³⁷⁶ In response, Republicans and the President reached a compromise. The Democrats had resisted extending the tax cuts for families with incomes over \$250,000, but in the end agreed to a full two-year extension.³⁷⁷

374. See Republicans in Congress, *A Pledge to America*, 16, 19-23 (2010), www.gop.gov/resources/library/documents/solutions/a-pledge-to-america.pdf [hereinafter *Pledge to America*]; Eric Kroh, *Senate Vote on Bush Tax Cuts Postponed Until After Midterms*, 128 TAX NOTES 1308, 1311 (2010) (reporting on the Pledge to America and Democrat's calling it a rehash). Making the tax cuts permanent was a perennial proposal. See Sheldon D. Pollack, *Revenge of the 80th Congress*, 129 TAX NOTES 819, 819 (2010); Eric Kroh, *Obama, Democrats Open to Compromise on Expiring Tax Cuts*, 129 TAX NOTES 651, 652 (2010) (quoting Republican Congressional leaders on the need to permanently extend all the Bush tax cuts). In his 2002 State of the Union address on January 29, 2002, President Bush, whose tax cuts were criticized as heavily favored high end tax taxpayers but provided an immediate advance tax cut in the form of a \$250 check to middle and low-income taxpayers stated, in applauding his policies,

Good jobs depend on sound tax policy. Last year, some in this hall thought my tax relief plan was too small; some thought it was too big. But when the checks arrived in the mail, most Americans thought tax relief was just about right. Congress listened to the people and responded by reducing tax rates, doubling the child credit and ending the death tax. For the sake of long-term, growth, and to help Americans plan for the future, let's make these tax cuts permanent.

George W. Bush, President of the United States, State of the Union Address 137 (Jan. 29, 2002), www.gpoaccess.gov/sou/index.html.

375. See Chuck O'Toole, *Lawmakers Cede No Ground on Bush Tax Cuts*, 129 TAX NOTES 863, 863 (2010) (quoting Senator Reid on the cost of extending the Bush Tax Cuts and noting Republican refusal to allow any vote unless all of the tax cuts are extended); Meg Shreve, *Conversations: Patrick J. Tiberi*, 122 TAX NOTES 1444, 1446 (2009) (quoting Rep. Tiberi, R-OH and Member of the Ways & Means Committee stating, "[w]e don't have a revenue problem in Washington, we have a spending problem"); see also Martin A. Sullivan, *Economic Analysis: Taxes Must Rise*, 127 TAX NOTES 369, 370-71 (2010) (expressing the view that spending cuts are impractical and that the Republicans will be unable to demonstrate that the public will support any significant spending cuts).

376. Chuck O'Toole, *House Passes Tax Cut as Negotiations Begin*, 129 TAX NOTES 1051, 1051 (2010).

377. *Id.* at 1052; Eric Kroh, *Democrats Wary of Obama's Tax Cut Compromise with GOP*, 129 TAX NOTES 1159, 1159 (2010) [hereinafter Kroh, *Democrats Wary*].

In exchange, the Republicans agreed to a massive extension of Democratic sponsored provisions, the result of which was the passage of the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (the “Tax Relief Act of 2010”),³⁷⁸ a bill carrying a price tag of \$857.8 billion over ten years, most of which will be expended during calendar years 2011 and 2012.³⁷⁹

The compromise legislation included temporary relief under the Estate and Gift Tax and the AMT.³⁸⁰ It also included an extension of a number of tax credits and other provisions.³⁸¹ The make-work-pay credit adopted in 2009 was allowed to expire, and in its place the legislation instituted a one-year, 2% reduction in the employee side of the Social Security tax.³⁸²

Specific costs during the fiscal years of 2011, 2012, and 2013 (in billions of dollars) of the Act’s provisions are as follows: Temporary Extension of Tax Relief, \$391.7; the AMT Relief, \$170.2; the Estate and Gift Tax Relief, \$61.9; the Temporary Extension of Investment Incentives, \$114.0; Temporary Extension of Unemployment Insurance Benefits, \$56.3; 2 Temporary Payroll Tax Reduction (for Employee Side of OASDI), \$111.7; and Temporary Extension of Certain Expiring Provisions (comprising almost seventy-five individual provisions), \$45.2.³⁸³ The total cost in these three fiscal years is \$916.8 billion.³⁸⁴

A cynical view of the compromise, in which the Republicans claimed victory, is that to extend the 33% and 35% tax brackets for high-income taxpayers over two years, at a cost of \$60.8 billion, the Republicans agreed to at least \$210.5 billion in relief for Democratic causes such as extending unemployment

378. See Kroh, *Democrats Wary*, *supra* note 377, at 1159; Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010, Pub. L. No. 111-312, 124 Stat. 3296 (2010).

379. JOINT COMM. ON TAXATION, FISCAL YEARS 2011-2020, *supra* note 346, at 8. The bulk of the spending will be expended during fiscal years 2011, 2012, and 2013. *Id.* The fiscal year begins on the first day of October. Congressional Budget and Impoundment Control Act of 1974, P.L. 93-344, Title III, § 300, 88 Stat. 306.

380. Kroh, *Democrats Wary*, *supra* note 377, at 1159 (describing the estate tax rates and exemption levels); Eric Kroh, *Tax Cut Compromise Clears Hurdles, Passes Congress*, 129 TAX NOTES 1279, 1279-80 (2010) (expressing Democratic concerns over the estate tax provisions of the compromise).

381. Chuck O’Toole, *Tax Cut Compromise Leaves Some Extenders Behind*, 129 TAX NOTES 1281, 1281 (2010).

382. Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010, § 601, 124 Stat. 3296 (2010).

383. JOINT COMM. ON TAXATION, ESTIMATED BUDGET EFFECTS OF THE “TAX RELIEF, UNEMPLOYMENT INSURANCE REAUTHORIZATION, AND JOB CREATION ACT OF 2010,” 1-8 (2010).

384. *Id.* at 8.

insurance, a payroll tax reduction, and extending expiring tax provisions, which the Republicans opposed.³⁸⁵ Further, the \$111.7 billion OASI payroll tax reduction will not impact the Social Security trust fund, since the trust fund will receive “transfers from the General Fund of the United States Treasury equal to any reduction in payroll taxes attributable to this provision.”³⁸⁶

The central message from Washington is that once a tax cut or a spending bill train is moving, everyone better come on board before it leaves the station. To reiterate, if legislation from the lame duck session of the 111th Congress is indicative of what to expect in the 112th Congress, it is worth repeating the old Republican belief that if “you win on the tax issue, you win all issues.” Additionally, it is worth questioning “what gets a politician elected.” The answer rests with “tax cuts and increased spending,” which can be simplified as advice to their newly elected members of Congress, “never vote against a spending bill or for a tax increase.”³⁸⁷

385. See Jeremy Scott, *Tax Cut Compromise Overcomes Lukewarm Liberal Resistance*, 129 TAX NOTES 1277, 1277 (2010) (noting that the estate tax compromise was a benefit the Republicans did not expect).

386. JOINT COMM. ON TAXATION, TECHNICAL EXPLANATION OF THE REVENUE PROVISIONS CONTAINED IN THE “TAX RELIEF, UNEMPLOYMENT INSURANCE REAUTHORIZATION, AND JOB CREATION ACT OF 2010” SCHEDULED FOR CONSIDERATION BY THE UNITED STATES SENATE 63-64 (2010). Critics point out that this 2% tax holiday favors higher income workers since a person earning \$40,000 annually would see a savings of \$800, while someone earning the maximum covered wage of \$106,800 would see a savings of \$2,136. See Nicola M. White, *Payroll Tax Holiday Plan Draws Criticism From Left*, 129 TAX NOTES 1304, 1304-05 (2010).

387. Michael J. Graetz, *Politics and Policy of the Estate Tax – Past, Present, and Future*, 130 TAX NOTES 1357, 1358 (2011) (quoting a comment by Grover Norquist, President of Americans for Tax Reform); Robert Michaelsen, *The National Debt Crisis*, 121 TAX NOTES, 745, 745 (2008) (explaining how spending in one Congressman’s district can get a Congressman in another district elected). One commentator understood the irony of the situation and put it this way:

On the surface, what’s going on with tax policy in Washington right now seems crazy. A Democratic president whose enemies call him a socialist makes a deal with Republicans that sells out both his party and the very tax promises that won him the election, while Republican leaders who say that debt is our overwhelming domestic problem insist on borrowing tens of billions of dollars to give tax savings to the riches among us. The polls, at the same time, show the public overwhelmingly favors ending tax cuts for high earners.

David Cay Johnston, *Reasons, Rules, and Riots: Our Societal Panic*, 129 TAX NOTES 1389, 1389-90 (2010) (explaining this irrational policy as the result of a societal panic beginning with the opening of China by President Nixon in 1971 that opened the door to the loss of manufacturing jobs and marked the beginning of the era of American abundance and the emergence of the belief that each generation would do better than the last and by working hard and playing by the rules you would prosper).

L. *Other Considerations*

The Tax Reform Act of 1986 was the result of a six year process that began in the early 1980s when Senator Bill Bradley (D-NJ) proposed to broaden the income tax base and lower the rates.³⁸⁸ Although not an original idea, Bradley pressed his idea on Congress throughout the early 1980s.³⁸⁹ The consensus for reform from the 1970s through the 1980s grew as Republicans and Democrats put forth proposals for change.³⁹⁰ The same approach is being proposed today, but there are forces aligned against tax reform that seem overwhelming.³⁹¹ The embedded “sacred cows” of tax expenditures, such as the mortgage interest deduction, the charitable deduction, and deduction of state and local income taxes, which cater to high income taxpayers, are supported by powerful lobbies.³⁹² While many tax expenditures benefit primarily high-income families, the tax system is also used to make income transfers to the poor. While welfare reform in the 1990s reduced the cost of “welfare as we knew it,” the Tax

388. See *supra* note 336 and accompanying text.

389. See *supra* note 336 and accompanying text; Calvin H. Johnson, *Two Years of the Shelf Project*, 126 TAX NOTES 513, 516 (2010) (recognizing that the 1986 Tax Reform Act, like all great tax reform bills, was preceded by a “serious systematic study by the Treasury”).

390. See William E. Simon, *Foreword* to DEP’T OF THE TREASURY, BLUEPRINTS FOR BASIC TAX REFORM, paras. 2, 7-8 (1977); OFFICE OF THE SECRETARY, DEP’T OF THE TREASURY, Vol. 1 OVERVIEW, TAX REFORM FOR FAIRNESS, SIMPLICITY, AND ECONOMIC GROWTH vii (1984); OFFICE OF THE SECRETARY, DEP’T OF THE TREASURY, *Preface* to Vol. 2 GENERAL EXPLANATIONS OF THE TREASURY DEP’T PROPOSALS, TAX REFORM FOR FAIRNESS, SIMPLICITY, AND ECONOMIC GROWTH iii (1984); OFFICE OF THE SECRETARY, DEP’T OF THE TREASURY, *Preface* to Vol. 3 VALUE-ADDED TAX, TAX REFORM FOR FAIRNESS, SIMPLICITY, AND ECONOMIC GROWTH 1 (1984).

391. *Moment of Truth*, *supra* note 22, at 28 (proposing that tax reform should be based on broadening the tax base and using the savings to lower the rates); see also Eric Kroh, *Congress Adjourns Without Vote on Bush Tax Cuts*, 129 TAX NOTES 33, 34-35 (2010) (commenting on Senator Wyden’s statement that his tax plan, the Wyden-Gregg proposal, conformed to the model of the Tax Reform Act of 1986 which led to millions of new jobs); see GRAETZ, UNNECESSARY RETURNS, *supra* note 22, at 24, 27 (asserting that the Tax Reform Act of 1986 was neither revolutionary nor stable and that most experts now agree that it was a promise that failed); see also Graetz, *Tax Reform*, *supra* note 336, at 319-21. The report of the Volcker Commission on tax reform proposed a number of provisions for simplification and consolidation of the system but was under instructions to exclude options that would raise taxes on families with income of less than \$250,000 a year and not to recommend a major overarching tax reform as was done in the Tax Reform Act of 1986. THE PRESIDENT’S ECONOMIC RECOVERY ADVISORY BOARD, THE REPORT ON TAX REFORM OPTIONS: SIMPLIFICATION, COMPLIANCE, AND CORPORATE TAXATION v (2010).

392. See Eric Kroh, *Tax Expenditures Deserve Scrutiny, Panelists Say*, 128 TAX NOTES 11, 11 (2010); see Jeremy Scott, *Week in Review: The True Cost of Homeownership*, 127 TAX NOTES 361, 361 (2010) (suggesting it is time to reconsider the mortgage interest deduction which is seen as benefiting only high-income taxpayers); see also Bruce Bartlett, *Misunderstanding Tax Expenditures and Tax Rates*, 129 TAX NOTES 931, 931-32 (2010) (criticizing the National Commission’s proposal to cut tax expenditures).

Code has exploded with programs for the poor that cost far more than the old welfare system.³⁹³ The EITC, refundable child credits, American Opportunity Tax Credit, and others are all part of a complex set of rules designed to redistribute money to an ever expanding number of persons in need.³⁹⁴

393. See Adam Carasso & Eugene Steuerle, *Growth in the Earned Income and Child Tax Credits*, 98 TAX NOTES 401, 401 (2003) (noting that the growth of the earned income and child tax credits already exceed the expenditures of Aid to Families With Dependent Children and the Temporary Assistance to Needy Families); Dennis J. Ventry, Jr., *Welfare by Any Other Name: How We Can 'Save' the EITC*, 114 TAX NOTES 955, 956-57 (2007) (supporting the EITC but warning that it should not be seen as a panacea for welfare needs and noting that Republicans see it as a reward for working while Democrats see it as an antipoverty program). The purpose of the EITC has been explained as follows:

The EITC originally was enacted primarily to reduce the burden of Social Security taxes on the working poor. It was used in 1986, in 1990, and again in 1993, however, to help remove people with poverty-level incomes from the income tax rolls and to provide a subsidy to low-wage workers. . . . Increasing, the EITC is seen . . . as a way to help assure minimum standard of living to the working poor. Thus, some have advocated the EITC as . . . the primary way to transfer government benefits to the working poor. . . .

MICHAEL J. GRAETZ & DEBORAH H. SCHENK, FEDERAL INCOME TAXATION: PRINCIPLES AND POLICIES, 427-28 (Robert C. Clark et al. eds., 6th ed. 2009).

394. See generally I.R.C. §§ 32, 24(d), & 25A(g)(6) (2010). All or a portion of these credits are refundable, which creates an opportunity for fraud. See David van den Berg, *IRS Considering Strategies for Reducing Refundable Credit Fraud*, 131 TAX NOTES 927, 927 (2011) (noting that improper payment of refundable credits have cost taxpayers more than \$106 billion in less than a decade). However, it is unlikely Congress will eliminate tax expenditures. Eric Kroh, *Fiscal Commission Draft Would Eliminate All Tax Expenditures*, 129 TAX NOTES 755, 756 (2010) (quoting Deficit Commission Member Rep. Janice D. Schakowsky's D-Ill. statement that "[commission members] certainly can't get rid of the earned income tax credit and the child tax credit"). Erroneous payments under the EITC are estimated at \$11 billion to \$13 billion annually. Nicola M. White, *Treasury, States Seek to Solve EITC Problems*, 130 TAX NOTES 1142, 1142 (2011). Professor Michael Graetz notes that "National Taxpayer Advocate Nina Olson has singled out the EITC as the most troublesome complex provision of the tax code." GRAETZ, UNNECESSARY RETURNS, *supra* note 22, at 91. He also notes that the EITC imposes a large "marriage penalty" on low-income families, since their joint incomes often reduce the amount of the EITC or eliminate it. *Id.* at 174. The EITC supplements the income of the working poor by attempting to offset Social Security taxes. GRAETZ & SCHENK, *supra* note 393, at 427. Since 1997, the EITC spending levels have grown to replace the welfare payments, Aid to Families with Dependent Children, and its successor, Temporary Assistance for Needy Families (TANF). Carasso & Steuerle, *supra* note 393, at 401. The EITC is available indefinitely and cost \$40 billion in 2006, which was greater than the benefits it replaced. See Ralph B. Tower & Kevin M. Hall, *Tax Credits: Their Critical Role in Comprehensive Tax Reform*, 121 TAX NOTES 460, 460 (2008) (observing that by far the most favored groups receiving refundable tax credits are taxpayers with children or dependents under IRC §§ 21, 23, 24, 32). Claims of fraud have long been made against the Earned Income Credit. Robert G. Nassau, *April Madness: We Have a Champion!*, 131 TAX NOTES 93, 93 (2011). The EITC is a refundable credit that is paid even if no tax is withheld. GRAETZ, UNNECESSARY RETURNS, *supra* note 22, at 89. In 1997, Congress introduced the child tax credit, a partially refundable credit, of \$400 per child, which was raised to \$500 per child in 1999, and \$1000 per child in 2001. *Id.* at 90. The Competitive Tax Plan would eliminate the IRS from running what is essentially a social welfare program, and instead,

Calling legislation aid to children, the poor, or to education seems to give it a religious-like aura of sanctity, protecting it against criticism with the result that half the citizens have become exempt from income and much payroll taxation.³⁹⁵

The Roadmap and other plans point out the need to revise the corporate tax.³⁹⁶ However, a proposal to eliminate corporate tax expenditures (e.g. corporate welfare) may face strong resistance.³⁹⁷

The current corporate tax of a combined federal and state rate of 39%, the second highest in the OECD and 8% higher than the OECD average rate, is seen as creating a disadvantage for

the IRS would collect less through income tax withholding and retail purchases. *Id.* at 90-91, 170-81.

395. See Sam Young, *Conversations: Leonard E. Burman*, 124 TAX NOTES 325, 328 (2009). Burman, a former Treasury Department and Congressional Budget Office analyst, comments that close to half of taxpayers don't pay any taxes, and this results in "an unintended consequence of providing more and more of a social safety net through the tax system"; additionally, many that owe some tax get back more than they pay in the form of refundable tax credits. *Id.* at 325, 328. Burman sees it as a problem that our children will pay for current spending (with interest) and that "a majority of taxpayers might think that they can vote for any new program and it won't affect their taxes." *Id.* at 328. Burman advocates introducing a VAT in the context of overall income tax reform and to use it to reduce rates and support health care. *Id.* at 328-29. President Obama's 2012 budget plan is criticized because he largely ignored the National Commission's recommended \$4 trillion in deficit cuts to Medicare, Medicaid, Social Security, and defense, while claiming to make "tough choices and sacrifices." Editorial, *Obama's Budget Plan Sidesteps Tough Issues*, Albuquerque J. (N.M.), February 18, 2011, at A8. The President's plan offsets proposed decreases in safety net programs with increases in education, infrastructure, and research, and the plan freezes spending at levels that cannot be sustained by taxes on the wealthy when nearly half the taxpayers pay no tax. *Id.*

396. See *Moment of Truth*, *supra* note 22, at 32-33; see also Domenici & Rivlin, *supra* note 22, at 3133; Roadmap, *supra* note 142, at 37-39, 59 (recommending elimination of the corporate income tax and replacement with a business consumption tax); GRAETZ, UNNECESSARY RETURNS *supra* note 22, at 108-25. Graetz states,

Increasing taxes on corporations may be as popular with the public now as in 1986, but is far less feasible economically. Absent a fundamental reexamination of U.S. international income tax policies, the combination of sophisticated corporate tax planning and tax competition among nations may cause the taxation of international corporate income to unravel completely. . . . In my view, the most important corporate tax change Congress could enact—both to stimulate our domestic economy and to increase the competitiveness of U.S. companies throughout the world—would be to lower our corporate tax rate substantially. Although a 25 percent rate would put us in line with most OECD nations, it is worth trying to get that rate down to 15 percent—the rate now applicable to dividends and capital gains—or no more than 20 percent.

Id. at 121, 123.

397. See, e.g., Robert Goulder, *AEI Explores Global Lessons on Corporate Tax Reform*, 130 TAX NOTES 1132, 1133 (2011) (noting that while lower rates could be welcomed, "there are big winners under the current rules who stand to gain nothing by seeing the tax base broadened").

American firms operating internationally.³⁹⁸ Likewise, the high corporate tax rate discourages firms from placing facilities in the United States.³⁹⁹ It seems that, after the Tax Reform Act of 1986, the U.S. corporate tax rate was one of the lowest in the OECD.⁴⁰⁰ Now it is one of the highest, even considering the impact of corporate tax expenditures, which lower the effective rate of the tax.⁴⁰¹

Because of the close relationship between personal and corporate income tax rates, it is unlikely that reform could address one area without addressing the other.⁴⁰² Further, the efforts to adopt a VAT have at various times been advanced as a replacement for all or part of the residential school property tax (considered by the Nixon Administration),⁴⁰³ corporate tax,⁴⁰⁴ and income taxes.⁴⁰⁵

The arguments presented today are much the same as those proposed fifteen years ago. Americans are not saving enough, the baby boomers will bankrupt the system, the bulk of Social

398. Roadmap, *supra* note 142, at 60; *see also* Peter R. Merrill, *Competitive Tax Rates for U.S. Companies: How Low to Go?*, 122 TAX NOTES 1009, 1009-10 (2009).

399. *See* Roadmap, *supra* note 142, at 60-61.

400. *See* Michael J. Graetz, *100 Million Unnecessary Returns: A Fresh Start for the U.S. Tax System*, 112 YALE L.J. 261, 285 fig.7 (2002).

401. Amy S. Elliott, *Large U.S. Firms' Tax Rates Surpass OECD Average*, 131 TAX NOTES 244, 244-45 (2011); Merrill, *supra* note 398, at 1009-12 (examining in detail the comparison of corporate tax rates in OECD non-U.S. countries with those of the U.S.). Merrill concludes that, for the combined U.S. corporate tax rate (federal and state) to match the average top statutory rate in the non-U.S. OECD countries, the federal corporate tax rate would need to be reduced to between 21% and 25.5%. *Id.* at 1010, 1013. It has also been suggested that, at its current levels, there is reason to believe that some reduction in the rate would increase revenues. Chris Edwards, *Is the U.S. Corporate Tax in the Laffer Zone?*, 117 TAX NOTES 1073, 1075 (2007); *see also* Calvin H. Johnson, *Taxing GE and Other Masters of the Universe*, 132 TAX NOTES 175, 183-84 (2011) (describing the impact of bonus depreciation on the effective corporate tax rate).

402. Meg Shreve, *Lawmakers Argue Against Reform Effort Centered on Corporate Tax*, 130 TAX NOTES 1125, 1125-26 (2011) (pointing out that considering corporate tax rates apart from individual rates could work to the disadvantage of small businesses using pass-through taxation).

403. Alan Schenk, *The Business Transfer Tax: The Value Added By Subtraction*, 30 TAX NOTES 351, 351-52, 351 n.6 (1986); *see also* Alan Schenk, *Prior U.S. Flirtations With VAT*, in THE VAT READER: WHAT A FEDERAL CONSUMPTION TAX WOULD MEAN FOR AMERICA 52, 53-54 (Tax Analysts, 2010).

404. *See* Domenici & Rivlin, *supra* note 22, *supra* note 142, at 59-62. Using the VAT to replace the corporate tax was suggested by a presidential task force in 1970. *See* Butler, *supra* note 324, at 271 n.35, 301-07 n.213.

405. GRAETZ, UNNECESSARY RETURNS, *supra* note 22, at 200-02. Interestingly, Graetz actually calls his tax a VAT, but notes that other tax proposals are called by names such as the Growth and Investment Tax, which is really a form of VAT. *Id.* at 166. Domenici & Rivlin call their national consumption tax a "Debt Reduction Sales Tax" and the Roadmap calls theirs a Business Consumption Tax ("BCT"). Domenici & Rivlin, *supra* note 22, at 31; Roadmap, *supra* note 142, at 59.

Security goes to affluent families who have a higher wage base and longevity, and the overall system favors the elderly over the young.⁴⁰⁶

One wonders whether Congress can solve this pressing debt crisis. Social Security and Medicare have been looming problems for decades, and long-term funding has not been resolved.⁴⁰⁷ The energy crisis that began in 1973 remains unresolved, and the United States is more dependent on foreign oil now than it was in 1973, while current efforts to expand drilling have been thwarted.⁴⁰⁸ No one believes the United States will be free of its reliance on oil anytime in the foreseeable future.⁴⁰⁹ Yet we subsidize bio-fuels and watch food prices rise because of the use of corn for fuel.⁴¹⁰ Congress' inability to resolve complex problems is also apparent in its inability to find a solution to illegal immigration.⁴¹¹ It is difficult to understand a country dedicated to the rule of law refusing to enforce its immigration laws for over twenty-five years.⁴¹² In 1985, Congress passed an

406. See, e.g., PETERSON, WILL AMERICA GROW UP, *supra* note 20, at 17-25, 31, 75, 143, 162, 199 (providing a comprehensive analysis of the pending crises in Social Security from the vantage point of the mid-1990s).

407. *Id.* at 7.

408. Richard A. Westin, *The Case for a Crude Oil Price Stabilization Tax*, 126 TAX NOTES 481, 481-83, 492 (2010) (describing the problems that have arisen because of the United States' failure to have a coherent energy policy and a brief history of the responses since 1972); Viva Hammer, *Alternative Energy Gets a Second Wind*, 129 TAX NOTES 895, 896-99 (2010) (providing a history of legislation centering on energy production); Diana Furchtgott-Roth, *America Needs More Oil Production, Not Less*, 130 TAX NOTES 1219, 1220 (2011) (identifying the need to continue tax subsidies for oil production to achieve energy independence).

409. BILL PAUL, FUTURE ENERGY: HOW THE NEW OIL INDUSTRY WILL CHANGE PEOPLE, POLITICS, AND PORTFOLIOS 2 (2007) (citing studies predicting that global petroleum consumption will grow from 84 to 85 million barrels a day in 2007 to 118 million barrels a day by 2030).

410. Jeremy Scott, *Is Senate Ethanol Vote a Sign of things To Come?*, 131 TAX NOTES 1209, 1209 (2011) (describing a senate vote to eliminate a \$.45 per gallon ethanol tax credit in the face of rising food prices); Michael M. Gleeson, *Lobbyists Cite Job Impact in Push for Extenders' Renewal*, 132 TAX NOTES 1092, 1092 (2011) (reporting that the Senate-passed amendment to repeal the ethanol tax credit had been blocked); Martin A. Sullivan, *IRS Allows New \$25 Billion Tax Break for Paper Industry*, 125 TAX NOTES 271, 272 (2009) (describing Congress' override of a presidential veto to pass legislation increasing the tax credit to \$1.01 per gallon on cellulosic ethanol as well as its reduction of the ethanol tax credit from a \$.51 per gallon to a \$.45 per gallon subsidy because distilling ethanol from corn was driving prices up).

411. See Hiroshi Motomura, *What Is "Comprehensive Immigration Reform"?* *Taking the Long View*, 63 ARK. L. REV. 225, 233-235 (2010).

412. *Id.* (acknowledging arguments that "legalization" and "amnesty" could be seen as violating the rule of law, but arguing that the history of U.S. immigration policy is more of an "open tolerance" such that prior granting of lawful status, even when they came here outside the law, has left the line between lawful and unlawful status neither clear nor impermeable); HEATHER MAC DONALD, VICTOR DAVIS HANSON, & STEVEN MALANGA, THE IMMIGRATION SOLUTION: A BETTER PLAN THAN TODAY'S, 37 (2007)

amnesty act with the understanding that borders would be secured.⁴¹³ But it never happened, and we are again faced with up to 12 million illegal immigrants.⁴¹⁴ Congress tolerates the creation of a “birth tourism” industry that brings an estimated 300,000 to 400,000 pregnant women to the United States annually to give birth.⁴¹⁵ These children receive automatic citizenship with all the benefits it confers.⁴¹⁶ These issues could and should be resolved in a fair and humane manner so the country can move on to an immigration policy that realistically reflects the vital role immigration will play in America’s future. But Congress languishes in the non-action.⁴¹⁷

M. *Preparation for the Next Emergency*

One hundred years ago in 1911 when Ronald Reagan was born,⁴¹⁸ few could predict the coming Great War, the roaring twenties, the depression, and the Second World War, space travel, or the internet. Whatever the future America needs must be prepared to address significant emergencies that will take hundreds of billions or even trillions of dollars to resolve. Living

(arguing that today’s immigrants, legal and illegal, from countries with poor, ill-educated populations have resulted in a mismatch between the immigrants and today’s economy, unlike immigration a hundred years ago, who brought skills that surpassed those found in the U.S. at the time).

413. Motomura, *supra* note 411, at 225-26. Motomura describes the Immigration Reform and Control Act of 1986 (P.L. 99-603) and the tradeoff between legalization and strengthened border security. *Id.* at 232. He suggests that the current system of ad-hoc legalization has its benefits because enforcement choices are allowed to be discretionary and reflect shifting policies, waiting avoids deciding in advance who will be economic contributors to the U.S., and border enforcement is expensive. *Id.* at 237-38. For these reasons Motomura thinks that screening after entry is responsive to the needs of the U.S. economy. *Id.* at 238. To the same effect, others argue that immigration laws should be structured to attract those immigrants who are best able to benefit our economy and citizens. MAC DONALD ET AL., *supra* note 412, at 170.

414. Motomura, *supra* note 411, at 226-27.

415. Richard D. Lamm, *Immigration: The Ultimate Environmental Issue*, 84 Denv. U. L. Rev. 1006, 1010 (2007). Lamm describes the costs to the U.S. economy of illegal immigration on education, poverty levels, and health care. *Id.* at 1009-15.

416. Marie Weisenberger, *Broken Families: A Call for Consideration of the Family of Illegal Immigrants in U.S. Immigration Enforcement Efforts*, 39 CAP. U. L. REV. 495, 513-15 (2011); Ashley E. Mendoza, *Anchors Aweigh: Redefining Birthright Citizenship in the 21st Century*, 13 J. L. FAM. STUD. 203, 203-04 (2011).

417. Motomura, *supra* note 411, at 227-28 (describing the efforts of Congress in 2007 to again reform immigration which ended in failure and suggesting that the issues raised in 1986 will have to be addressed again because they were never resolved). Overall, Motomura thinks we need to consider carefully the immigration system the next generation of Americans would want us to have and bringing the lawful admissions system into closer alignment with the needs of the U.S. economy. *Id.* at 238-39, 241.

418. PAUL KENGOR, *GOD AND RONALD REAGAN: A SPIRITUAL LIFE* xi (2004) (noting particularly that Reagan’s life and political career coincided with the rise and fall of communism in Russia which began in 1917 and ended in 1991).

on the edge of catastrophe should not be tolerated.⁴¹⁹ In past years Democrats demanded offsets for Republican tax breaks but now see budget proposals with trillion dollar deficits from a Democratic president⁴²⁰ Republicans once thought “deficits do not matter” have members demanding huge spending cuts.⁴²¹ Limiting the flexibility of future generations to make its own economic decisions raises moral questions beyond the scope of this article.

V. THE NEXT TWO YEARS

The current political climate makes it highly unlikely that the looming debt crisis will be addressed in the next two years.⁴²²

419. As this article is being finalized, the world is beginning to respond to a potentially trillion dollar emergency as Japan experienced a 9.0 magnitude earthquake on Friday, March 11, 2011 at 2:46 pm JST followed minutes later by an extremely destructive tsunami caused by the earthquake that hit Japan destroying cities and towns, leaving untold numbers dead, homeless, and without power, food, water, and other supplies, and causing meltdowns at a number of Japans nuclear reactors. Brian Gaynor, Quick decisions needed following quakes, *The New Zealand Herald*, Mar. 19, 2011, at C002 (estimating the damage for the tsunami at \$1.6 billion, making it the most expensive natural disaster with Hurricane Katrina at \$125 billion being the most expensive natural disaster before the tsunami. A world struggling from recession is ill-prepared for another emergency. See Roger Metz, Op-Ed, *Disaster in Japan offers economic lessons*, PENTAGRAPH (Bloomington, IL) Mar. 26, 2011, at A6 (suggesting that the annual U.S. budget deficit of \$1.6 trillion is equivalent to a Japanese tsunami of \$137 billion hitting the shores every month and questioning why the president and Senate leadership will not pull the alarm and warn the people about the looming deficit disaster).

420. See Tax Analysts, *Budget Debate Heats Up on Battle Over Taxes*, 94 TAX NOTES 1557, 1557 (2002) (noting that in 2002, Congressional Democrats were demanding that tax cuts be accompanied by offsets so as not to create prolonged deficits). Democrats also argued that no matter how well justified, deficits do matter when resisting war spending by President Bush. Martin A. Sullivan, *Good Politics, Bad Economics: Five Timely Talking Points*, 99 TAX NOTES 188, 189-90 (2003). Since these earlier Democratic positions, President Obama produces a budget with deficits indefinitely into the future as if deficits do matter. Jeremy Scott, *Obama's fiscal 2012 Budget Disappoints Deficit Hawks*, GOP, 128 TAX NOTES 853, 853 (2002) (reporting that President Obama's 2012 budget projects \$7.4 trillion in federal debt over ten years, including \$1.1 trillion in 2012); Drew Pierson, *OMB Director Rejects Criticisms of Obama Budget Plan*, 128 TAX NOTES 874, 874 (2011) (reporting that members of both parties were critical of the budget's lack of any effort to tackle the country's long-term fiscal problems and that the director of the OMB defended the lack of spending cuts on the basis that to do so during a recession would harm the economy); Michael M. Gleeson, Drew Peirson, & Meg Sheve, *Lawmakers Return to Work on Deficit Supercommittee, Jobs*, 132 TAX NOTES 999, 1000 (2011).

421. Joseph J. Thorndike, *1986, Who Cares?*, 133 TAX NOTES 349, 350 (2011) (noting that the Republicans had abandoned their fiscal responsibility to the extent that Vice President Dick Cheney would declare “deficits don't matter”). Returning to a fiscal conservatism some Republicans are recommending huge spending cuts. *Roadmap*, *supra* note 142, at 7-17 (discussing the effects of unsustainable debt and the impact on the American tradition and character); see *Pledge to America*, *supra* note 374, at 19-23 (pledging to rein in out-of-control spending).

422. Martin A. Sullivan, *A Hitchhiker's Guide to Corporate Tax Reform*, 125 TAX NOTES 1043, 1045 (2009) (predicting that after the 2012 election, increasing concerns

Washington's typical response to a crisis is to expand government through the use of tax expenditures.⁴²³ Such solutions produce action but seldom solve the problem.⁴²⁴ The solution to the present problem is just the opposite. Government needs to shrink, spend less, and raise taxes to balance the budget at

about the federal budget deficit and U.S. competitiveness will bring more attention to tax reform). Meg Shreve, *Tax Reform Takes Nonstop Effort, Former Treasury Officials Say*, 130 TAX NOTES 1123, 1123-24 (2011) (emphasizing the need for presidential leadership for any tax reform to take place). Shreve notes that the 1986 Tax Reform Act took about three years to complete from the first draft to final passage. *Id.* at 1123. Shreve also points out the debate about the need for fiscal and deficit reform to proceed along with tax reform, although Republicans fear that if they proceed together, the result will be a "backdoor" tax increase. *Id.* at 1124-25.

423. Cf. Diane Lim Rogers, *The 'Tastes Great, Less Filling' Approach to Cutting the Deficit*, 131 TAX NOTES 1289, 1290 (2011) ("Tax expenditures amount to approximately \$1 trillion annually — as much as all discretionary spending combined."). Rogers rejects the idea that the budget can be balanced with spending cuts alone and proposes that the savings from a reduction of \$1.0 trillion in tax expenditures should be used to reduce the deficit rather than to lower tax rates as others have proposed. *Id.* Rogers also notes that tax expenditures expand government's influence over the economy by favoring some economic activities over others and that reducing tax expenditures will enhance progressivity. *Id.*; Patrick E. Tolan, Jr., *Questioning Tax Expenditures for Economic Recovery*, 127 TAX NOTES 67, 67, 69 nn.14 & 20 (2010) (stating that expenditures should be used sparingly and as a last resort). Stanley Surrey noted that "[m]ost tax incentives have decidedly adverse effects on equity . . . and are highly irrational." *Id.* at 69 n.14 (quoting Stanley S. Surrey, *Tax Incentives as a Device for Implementing Government Policy: A Comparison With Direct Government Expenditures*, 83 HAR. L. REV. 705, 721 (1970)); Daniel N. Shaviro, *1986-Style Tax Reform: A Good Idea Whose Time Has Passed*, 131 TAX NOTES 817, 824 (2011) (citations omitted) (pointing out that the use of tax expenditures had the effect of making the size of the government look smaller).

424. Theodore P. Seto, *The Problem with Bonus Depreciation*, 126 TAX NOTES 782, 782-83 (2010) (pointing out that enacting bonus depreciation in an effort to end the recession in 2001 had the effect of shifting businesses toward greater use of capital and less use of labor, thereby creating a jobless recovery which was not intended); Paula N. Singer, *Common-Sense Tax Reform*, 122 TAX NOTES 79, 86 (2009) (noting that tax incentives for health savings accounts provide incentives for high-income taxpayers but does little or nothing for low- and middle-income uninsured persons and nothing to solve the vexing problems of the healthcare delivery system).

something less than 20% of GDP.⁴²⁵ Simply relying on growing the economy will not solve the debt crisis.⁴²⁶

Change of the magnitude called for by the studies in Part II requires Presidential leadership to be successful. Like the Bush 43 administration before it, the current administration used its mandate for change to adopt a huge spending bill benefiting its primary political supporters.⁴²⁷ The new administration then spent its political capital on the ACA and a bank reform bill.⁴²⁸ The last two years of the Obama administration will likely be

425. See Diane Lim Rogers, *Evolved Tax Policy*, 132 TAX NOTES 1419, 1419 (2011) (noting that Democrats point to the Clinton years when the budget produced the last surpluses and revenues approached 20% of GDP); Rogers, *supra* note 423, at 1289-90 (noting that elimination of tax expenditures will shrink government); Caroline L. Harris, *Rolling the Deep*, 131 TAX NOTES 733, 733-34 (2011) (noting that the historic average of revenues to GDP is 18% to 19%, that the President's 2012 budget would raise it to 20% by 2021, and that House Budget Committee Chair Paul Ryan, R-Wis., would reduce it to 18.3% by 2021). Harris, after examining proposals, laments that little is likely to happen without any serious presidential leadership. *Id.* at 735; see also *Moment of Truth*, *supra* note 22, at 14 (projecting an objective of capping revenues at 21% of GDP and spending at less than 22% of GDP); Domenici & Rivlin, *supra* note 22, at 16 (recommending that federal spending should be reduced to 23% of GDP and revenues be at 21.4% of GDP by 2020).

426. Sullivan, *Part 2*, *supra* note 39, at 650; see Wesley Elmore, *Entitlement Commission Must Consider Tax Hikes*, *Panelists Say*, 111 TAX NOTES 893, 893 (2011) (reporting comments that neither party will likely initiate entitlement reform but that a commission could provide sufficient "cover" to allow the procedure to commence and comments that the country cannot grow out of its long-term fiscal problem).

427. See American Recovery and Reinvestment Act of 2009, Pub. L. No. 111-5, 123 Stat. 115 (2009). This bill injected \$787.2 billion into the economy, including \$290 billion in tax incentives. Sam Goldfarb & Chuck O'Toole, *Obama Signs "Sweeping" Stimulus Bill with Billions in Tax Relief*, 122 TAX NOTES 946, 946 (2009).

428. See Patient Protection and Affordable Care Act of 2010, Pub. L. No. 111-148, 124 Stat. 119 (2010) (to be codified at 42 U.S.C.A. § 18001); Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, 124 Stat. 1029 (2010) (to be codified at 42 U.S.C.A. § 1305); Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, Pub. L. No. 111-203, 124 Stat. 1376 (2010) (to be codified at 12 U.S.C.A. § 5301); see also Jeremy Scott, *Democrats Push Healthcare Reform Through Congress*, 126 TAX NOTES 1557, 1557 (2010); Lee A. Sheppard, *What's Wrong with the Derivatives Transfer Regulations*, 132 TAX NOTES 465, 465 (2011) (noting Republicans' effort to undermine Dodd-Frank). Daniel N. Shaviro notes the scarcity of political capital in Washington and objects to a 1986 style tax reform:

Just think about it: We are told (and I would agree) that the code is riddled with costly and wasteful special tax benefits, while we face grave, rising, and unsustainable fiscal shortfalls. And the proposed response is to accompany the elimination of those bad rules with significant rate cuts that eliminate most of the budgetary gain from repeal! In other words, massive political capital – a scarce resource in gridlock-prone and interest-group-dominated Washington – should be diverted from deficit reduction, the ostensible goal, and deployed instead to achieve a 1986-style tax reform that to a significant extent is merely revenue neutral. Even if tax rate reduction is unambiguously desirable, one would think more justification was needed for why this particular use of so much of the budgetary gain from repealing costly and wasteful tax preferences should prevail over competing possibilities.

Shaviro, *1986-Style Tax Reform*, *supra* note 423, at 818.

highlighted by controversy between the administration and the Republican House majority.⁴²⁹ President Obama will likely move to the political center, talk about jobs and the spending necessary to put Americans to work and avoid further discussion of Obamacare (e.g. the ACA), the budget-busting, sleeping giant in the room, or of any significant reform to the big unmentionable three programs driving the long-term deficit.⁴³⁰ The likely result is a two year delay in significant action on the deficit.⁴³¹ Further, few believe Congress will allow the benefit cuts necessary for the ACA to meet its deficit reduction goals.⁴³²

429. See Richard J. Cebula & Christopher K. Coombs, *What Happens When You Increase Taxes on the Rich?*, 131 TAX NOTES 299, 299-300 (2011) (arguing that the two year extension of the Bush tax cuts had the effect of avoiding a double-dip recession but not providing incentives for taxpayers to invest in pro-growth investments, which will result in the next two years having slower economic growth). Conflict between Republicans and Democrats developed over the raising of the ceiling on the national debt in August 2011 with the resolution being the raising of the ceiling to sufficient extent so that it will not have to be raised again until after the 2012 elections. Jeremy Scott, *Debt Ceiling Deal Solves Little in the Long Term*, 132 TAX NOTES 565, 565 (2011). The price of the deal was an agreement for an immediate cut of \$900 billion in spending reductions and a second cut of \$1.2 trillion in deficit reduction over ten years to be determined by a Joint Select Committee on Deficit Reduction (the "Supercommittee"). William F. Sweetnam, *Legislative Update – Budget Control Act of 2011: How the Debt Limit and Budget Negotiations Could Impact Health and Retirement Plans*, ST010 ALI-ABA 259, 261 (2011). If the cuts are not passed by November 2011, then automatic cuts will be made—including more than \$500 billion in defense cuts. Scott, *Debt Ceiling Deal Solves Little in the Long Term*, *supra* note 429, at 565. The Supercommittee is made up of 12 members, three from each party of the House and Senate, whose first task may be to interpret whether the new legislation considers the Bush tax cuts and the AMT patch to be extended, the resolution of which may determine whether tax increases can be part of the deficit reduction. Drew Pierson, *Obama Signs Bill to Increase Debt Ceiling*, TAX NOTES TODAY, Aug. 3, 2011, <http://services.taxanalysts.com/taxbase/tnt3.nsf/Number/2011+TNT+149-2?OpenDocument&Login>.

430. See Michael Beller, *Senate Appropriators Approve \$11.7 Billion IRS Budget*, 132 TAX NOTES 1232, 1232-33 (2011) (quoting Senator Lindsey Graham, R-S.C., to the effect that the 2012 election will be a referendum on the Patient Protection and Affordable Care Act (P.L. 111-148)); Paul Starr, *Obama's Fate—and Ours*, *The American Prospect* Sept. 29, 2011, paras. 1-2, www.prospect.org/article/obamas-fate-and-ours (questioning whether President Obama's campaign will be more like that of Presidents Truman or Carter and suggesting that his move to the center will likely demoralize the Democratic base). President Obama is seen, from his jobs speech on September 8, 2011, as making jobs the number one issue for the remainder of his term. See Jeremy Scott, *Obama Jobs Plan Offers Nothing New*, 132 TAX NOTES 1081, 1081 (2011).

431. See Cebula & Coombs, *supra* note 429, at 300 (noting that actions to promote job creation have been postponed until the 2012 elections); see also Amy Elliott, *Rivlin Calls on Obama to Support Bipartisan Budget Reform Plan*, 130 TAX NOTES 891, 891 (2011) (reporting that Alice Rivlin, director of the Office of Management and Budget under President Clinton, expressed disappointment that President Obama's 2012 budget proposal did not propose tax or entitlement reforms).

432. See Sweetnam, *supra* note 429, at 263 ("Any cuts to the Affordable Care Act will be hotly debated by Republicans and Democrats on the Committee."). Several options for handling Medicare have been presented, including the use of health insurance retirement accounts that would receive 4% of the worker's paycheck, which would purchase an

The Democrats professed to use PAYGO and to pay for new spending or tax cuts, but when such payment was inconvenient, the Democrats found a way to waive PAYGO, and legislation was passed without offsets.⁴³³ In setting the rules for the 112th Congress, Republicans adopted Cut-Go budget rules, under which any new spending that would increase the deficit must be offset by spending cuts while tax cuts do not have to be offset.⁴³⁴ In what may be seen as trivializing the matter, a leading Republican has stated: “[w]e don’t have a revenue problem, we have a spending problem.”⁴³⁵

Change may be the subject of the next presidential campaign season, but the political system heavily favors incumbents.⁴³⁶ Once the election is decided in 2012, it is likely that another debt commission will be announced.⁴³⁷ Efforts to find new revenues

annuity at retirement to pay medical costs above a \$2,500 deductible. Diana Furchtgott-Roth, *Cracking the Toughest Entitlement Nut: Medicare*, 131 TAX NOTES 95, 96 (2011).

433. See Drew Pierson, *Republicans Expect to See Tax Reform in Obama’s 2012 Budget*, *supra* note 25, para. 17 (indicating that Republicans will be just as willing to make exceptions to cut-go as Democrats did under PAYGO).

434. Drew Pierson, *House Passes New ‘Cut-Go’ Budget Rules*, 130 TAX NOTES 166, 166 (2011).

435. *Id.*

436. Jerry Shenk, *Break Incumbents’ Protection Rackets*, THE LEBANON DAILY NEWS (PA), July 8, 2011, para. 3, <http://www.patownhall.org/article.php?id=6255> (reporting on Rasmussen Reports survey that 53 percent of Americans believe elections to be rigged in favor of congressional incumbents).

437. Joseph J. Thorndike, *The Myth of Political Cover*, 129 TAX NOTES 869, 869 (2010) (expressing the view that commissions are seen as a way to provide political cover for lawmakers, but in the current climate where everyone is out to save their own skin, the commission is pretty much useless). Thorndike states: “Commissions represent an effort to substitute expertise for leadership. They distract from the real work of deficit reduction: political mobilization and public education. Politicians will begin that work when they’re caught between a rock and a hard place – and not one moment before.” *Id.* Thorndike also points out that major tax increases have a history of occurring only in times of national emergency, such as a war. *Id.* The then-anticipated National Commission report, (later to be called “Moment of Truth”), was being criticized for using the elimination of tax expenditures as a basis to lower rates when the commission’s true task is to “make us take cod liver oil and close the deficit.” Calvin H. Johnson, *The Fiscal Commission Has Forgotten Its Role*, 129 TAX NOTES 921, 921 (2010). Another commentator suggested that the National Commission, by assuming all tax expenditures are equally unjustified tax loopholes, fails to recognize that many tax expenditures are necessary adjustments to the tax base that create fairness and produce economic growth. Bruce Bartlett, *Misunderstanding Tax Expenditures and Tax Rates*, 129 TAX NOTES 931, 931 (2010). Another commentator praised the National Commission for what it did indirectly by making lawmakers and the public understand:

[T]hey may have to swallow not one, but all of the following: a higher gas tax; higher Social Security taxes; cuts in Social Security benefits; limits on Medicare and Medicaid; limits on the mortgage interest deduction; limits on the deduction for charitable contributions; taxes on employer-provided healthcare; cuts in defense spending; and a downsizing of, and pay cut for, the federal civilian workforce.

have been ongoing by advocates in Washington seeking increased federal spending.⁴³⁸ One of the prime suggestions is that the United States should adopt a VAT.⁴³⁹ Indeed, nearly every study seems to conclude that a VAT is the way to go.⁴⁴⁰ Transitional rules have been a problem in the past, as a move away from the income tax could be seen as favoring the wealthy taxpayers, who have built-in gains that may avoid taxation.⁴⁴¹ At the present time, there does not seem to be an effort to institute a

Martin A. Sullivan, *Tax Reform Fantasy*, 129 TAX NOTES 859, 859 (2010). In that no action was taken on the National Commission report, commentators were urging the Supercommittee to take their proposal seriously. Michael Beller, Meg Shreve, & Drew Pierson, *Corporate Tax Reform Alone Isn't Enough, Supercommittee Says*, 132 TAX NOTES 1326, 1328 (2011). David Stockman, Ronald Reagan's Director of the Office of Management and the Budget, urged the Supercommittee to aim for \$10 trillion in deficit reduction over the next decade, while members cautioned that even \$4 trillion in cuts would be difficult. *Id.* at 1328-29.

438. See Butler, *supra* note 324, at 301-04 (giving a brief analysis of potential ways to raise money). But see Rogers, *supra* note 423, at 1420-21 (noting President Obama's reluctance to "go-big" with a revenue heavy strategy to counter the Republican's spending cut exclusive approach for fear of being labeled a "tax raiser"). PETERSON, WILL AMERICA GROW UP, *supra* note 20, at 93-95 (describing the creation of Medicare and Medicaid, the expansion of Social Security when Congress enacted a series of across-the-board hikes that raised Social Security benefits by 72% and calling 1965 the "critical turning point" when the government was protecting the individual against a poverty-ridden old age into an indiscriminate middle-class welfare program). Peterson further notes that from 1965 to 1981, the entitlement revolution entrenched itself into American culture and acquired its own voter constituency. *Id.* at 97. But the acknowledgment of deficits from health care proposals goes back to President Truman's administration, when he proposed a health care program and agricultural subsidies and Republican Senator Taft predicted it would add more than \$16 billion to the deficit. RANDOLPH E. PAUL, TAXATION IN THE UNITED STATES 523 (1954).

439. See *supra* notes 27-28 and accompanying text.

440. See *supra* notes 27-28 and accompanying text. The National Commission considered but determined not to recommend a VAT, giving the impression "that politicians are unwilling to implement a new consumption-based tax even in the face of spiraling projected debt levels." Amy S. Elliott, *Academics Argue for U.S. VAT*, 129 TAX NOTES 960, 960 (2010). It is difficult to determine how much revenue a VAT will generate. Professor Graetz suggests that an additional one percentage point would generate \$70 billion in revenue. *Id.* at 961. However, Martin A. Sullivan seems to suggest that it would take a 10% VAT to close a \$400 billion budget gap. Meg Shreve, *Panelists Question Future of Corporate Tax Reform*, 131 TAX NOTES 19, 20 (2011). The two reasons given for the failure of the National Commission to recommend a VAT are that the Senate had overwhelmingly just voted for a non-binding resolution against creating a VAT, and that the Commission thought the VAT would be a supplement to rather than a replacement of the income tax thereby creating two engines of revenue. Drew Pierson, *Fiscal Commission Looked Closely at VAT, Members Say*, 130 TAX NOTES 1251, 1251 (2011).

441. Diane Lim Rogers, *The Dynamics of Fundamental Tax Reform*, 133 TAX NOTES 221, 223 (2011) (noting that the transitional rules necessary to create change are hard to achieve and historically have effectively benefited the rich by lowering the effective tax rate of the rich); see also Robert Carroll & Alan D. Viard, *Value Added Tax: Basic Concepts and Unresolved Issues*, 126 TAX NOTES 1117, 1122-23 (2010) (illustrating how transitional rules can protect the assets of the wealthy but may still have a negative impact on workers).

consumption tax, at least while the unemployment rate hovers around 10%.⁴⁴² All European countries adopted the VAT, but that has not stopped many of the countries from continuing disastrous social spending programs that have pushed them to the point of bankruptcy.⁴⁴³

There is no shortage of good ideas that have been around for years. But both political consensus and will are noticeably absent. While it is easy to get tax cuts and spending bills, tax increases and spending cuts are nearly impossible.⁴⁴⁴ There is a

442. See Reuven S. Avi-Yonah, *The Political Pathway: When Will the U.S. Adopt a VAT?*, in THE VAT READER: WHAT A FEDERAL CONSUMPTION TAX WOULD MEAN FOR AMERICA 334, 334 (Tax Analysts, 2011) (noting that the apparent overwhelming political opposition to a VAT suggests that it is a live political option and that in other countries' political opposition seems strongest prior to a VAT's adoption). Avi-Yonah sees no way to find sufficient revenue to fund "Medicare, Medicaid, Social Security, interest on the national debt, and defense spending and some discretionary (but politically popular) spending" without an additional source of revenue. *Id.* at 334-35. Recognizing that the current 10% unemployment rate has left many families with no option but to withdraw money from retirement saving for current consumption, one commentator has called on Congress to eliminate the 10% penalty on early withdrawals under IRC § 72(t)(2), and in doing so, suggests the penalty tax is the equivalent of levying a consumption tax on individuals facing financial emergencies. Claire Y. Nash, *It's Time to Amend the Early Distribution Penalty*, 130 TAX NOTES 826, 826-28 (2011).

443. Avi-Yonah, *supra* note 442, at 337. Avi-Yonah concludes his piece on the adoption of a VAT in the U.S. by stating, "[I]t is hard to see how the U.S. can avoid joining the other OECD countries – and almost every other country in the world – in adopting a VAT. The question is no longer whether, but when and how." *Id.* However, it has been pointed out that forty years ago, in the mid- to late-1960s, European countries had governments about the size of the U.S. government, but after they began adopting VATs, their social programs and governments expanded, and their economies underperformed. Charles Gnaedinger, *No U.S. VAT Unless It Replaces Income Tax, Panelists Say*, 126 TAX NOTES 573, 575 (2010). Greece must borrow to pay the interest on its sovereign and is in need of a permanent bailout. See Lee A. Sheppard, *Credit Default Swaps in Bankruptcy Court*, 132 TAX NOTES 323, 323 (2011). While Greece is small, the fear is contagion, or that the problem will spread to Portugal, Ireland, Spain, and Italy. *Id.* All these countries have long-standing VATs. The VAT percentage and date of adoption for each of these countries is as follows: Greece (19%, 1987); Portugal (20%, 1986); Ireland (21.50 %, 1972); Spain (16%, 1986); and Italy (20%, 1973). Leah Durner, Bobby Bui, & Jon Sedon, *Why VAT Around the Globe?*, 125 TAX NOTES 929, 934 (2009). Another commentator concludes: "Unfortunately, Greece's experience indicates that having access to a powerful revenue raiser like the VAT does not insulate a country from financial crisis." Douglas Holtz-Eakin, *The Case Against VAT*, in THE VAT READER: WHAT A FEDERAL CONSUMPTION TAX WOULD MEAN FOR AMERICA 96, 97 (Tax Analysts, 2011).

444. See Michaelsen, *supra* note 387, at 745 (pointing out that politicians get elected by reducing taxes and increasing spending, both of which contribute to the national debt). Michaelsen describes economist Milton Friedman's response to the impossibility of getting spending cuts as refusing to allow any tax increases under a theory described as "starving the beast," where tax cuts would lead to spending cuts. *Id.* at 745. Michaelsen then speaks of the "immorality" of passing debilitating debt on to the next generation and laments the fact that so few people are worried about the debt. *Id.* He further notes that the country is locked into substantial future spending increases. *Id.* at 746. Michaelsen's thoughts can be compared to the reaction of former Speaker of the House of Representatives, Nancy Pelosi (D-CA), to the National Commission's proposed changes to Social Security, that the proposal was "simply unacceptable" and that any proposal must

long history of expanding the safety net.⁴⁴⁵ Reversing the mentality of government domination of the major areas of life planning will not be easy.

VI. THE ONE FUND SOLUTION: IT'S MY MONEY AND I NEED IT NOW!

From the first day a teenager receives a pay check for serving customers at McDonalds, he sees his wages reduced by 7.65%.⁴⁴⁶ Upon inquiry, he learns he has made a contribution to the Social Security and Medicare systems for benefits he will receive nearly fifty years later.⁴⁴⁷ What he does not immediately understand is that his wages have also been reduced by an unseen 7.65% paid by his employer as a matching contribution on his behalf.⁴⁴⁸ Our teenager may not have health insurance and perhaps has heard from his governmental officials that he is not saving enough. Yet, he has paid an effective 15.3% for health care and retirement fifty years away.⁴⁴⁹ If a person does not have

“do what is right for our seniors, who are counting on the bedrock promises of Social Security and Medicare.” William M. VanDenburgh & Nancy B. Nichols, *Fiscal Commission's Report Frames Budgetary Debate*, 130 TAX NOTES 447, 453 (2011).

445. GRAETZ, UNNECESSARY RETURNS, *supra* note 22, at 128-42 (describing the growth and funding for Social Security and Medicare and suggesting solutions for solving the problems of underfunding). Among his suggestions for Social Security is to move the retirement age to age seventy and the early retirement age to sixty-five. *Id.* at 137. He would also consider supplementing Social Security with private accounts. *See id.* at 138-39. For Medicare, high-income persons could be required to purchase their insurance, and low- and middle-income persons could have a high-deductible policy supplemented by the government. *Id.* at 140-42. However, fixing Social Security will be child's play when compared to the problem of fixing Medicare. *Id.* at 140-41.

446. *See* SHAVIRO, MAKING SENSE OF SOCIAL SECURITY REFORM, *supra* note 223, at 10.

447. Social Security benefits consist of a retirement annuity, the amount of which is dependent on average covered wages and the age of full retirement. FAMILY WEALTH MGMT., *supra* note 217, at 580. Recipients can retire early at age sixty-two with a reduced benefit, full retirement at age sixty-five to sixty-seven depending on one's year of birth, or up to age seventy with an enhanced benefit. *Id.* at 581-82. The retirement benefit includes spousal and children's benefits as well as survivor benefits. *Id.* at 579-84. Social Security also provides a disability benefit. *Id.* at 552-53. Medicare provides a hospital insurance benefit for persons who turn sixty-five. *Id.* at 687, 689. The young taxpayer in our example will be paying for an assortment of benefits the majority of which will be available when he retires in his sixties.

448. *See* FAMILY WEALTH MGMT., *supra* note 217, at 579-80, 687.

449. If an individual is making \$100,000 per year his Social Security and Medicare contribution is \$7,650 (7.65%), and his employer will contribute the same amount. *See* SHAVIRO, MAKING SENSE OF SOCIAL SECURITY REFORM, *supra* note 223, at 10. As a technical matter, the employer's contribution is a form of compensation that is not subject to the income tax but, in effect, the individual's wage is \$107,650 (\$100,000 plus \$7,650). *See id.* The employer returns \$15,300 on behalf of the employee having an effective wage of \$107,650. *See id.* Thus, the actual percentage paid is 14.2% and not 16.5%. *Id.* at 10-11, 159 n.2. The entire burden of the tax is generally considered to be borne economically by

healthcare today, why is he paying for health care scheduled to begin in fifty years? It's my money and I need it now!

The One Fund Solution addresses this upside down plan created under the Social Security Act signed into law by President Franklin D. Roosevelt more than seventy-five years ago.⁴⁵⁰ Social Security was designed to address the retirement needs of a population with a life expectancy of sixty-four years and to create an incentive for older people to retire, thereby leaving more work for younger people.⁴⁵¹ It was not until 1965, with the amendments to the Social Security Act creating Medicare and Medicaid, did health care become a priority for the elderly and poor.⁴⁵² For others beginning during World War II, healthcare became attached to employment.⁴⁵³ The political calculations that created this system left the nation with a legacy of an upside down savings plan.⁴⁵⁴ The One Fund Solution reverses this anomaly by funneling health insurance through the One Fund Account in combination with retirement savings.

The One Fund Solution is a system of private accounts administered by the Social Security Administration (the "SSA"). Like other entitlement reform proposals, people fifty-five years and older would not be affected. Persons under age fifty-five

the employee. Deborah A. Geier, *The Payroll Tax Liabilities of Low- and Middle-Income Taxpayers*, 106 TAX NOTES 711, 711 (2005).

450. NANCY J. ALTMAN, *THE BATTLE FOR SOCIAL SECURITY: FROM FDR'S VISION TO BUSH'S GAMBLE* 83 (2005).

451. *Moment of Truth*, *supra* note 22, at 48 (noting that when Social Security was adopted the average life expectancy was sixty-four and the retirement age was sixty-five and that today people live an average of fourteen years longer and can retire three years earlier); *see also* AMITY SHLAES, *THE FORGOTTEN MAN: A NEW HISTORY OF THE DEPRESSION* 255 (2007) ("Roosevelt hoped the program [Social Security] would make older workers comfortable with the idea of retiring earlier, leaving more work for younger people.").

452. PETERSON, *WILL AMERICA GROW UP*, *supra* note 20, at 93-94.

453. Robert B. Helms, *Mission Improbable: No One is going to blow Up Health Insurance*, 111 TAX NOTES 1262, 1262-63 (2011). World War II saw the federal income tax move from a tax on upper income individuals only to a tax on every citizen, that is, it moved from a "class tax to a mass tax." Deborah A. Geier, *Integrating the Federal Tax Burden on Labor Income*, 98 TAX NOTES 563, 567 (2003); *see* Carolyn C. Jones, *Class Tax to Mass Tax: The role of Propaganda in the Expansion of the Income Tax During World War II*, 37 BUFF. L. REV. 685, 719-20, 727-33 (1989).

454. *See* PETERSON, *WILL AMERICA GROW UP*, *supra* note 20, at 94-95. Peterson describes the emphasis on taking care of the seniors and leaving the youth to take care of themselves as follows:

In concept, these entitlements were supposed to "insure" Americans of all ages against economic vicissitudes. In practice, the benefits were funneled almost entirely to the elderly. It was expected that younger Americans would inherit a prosperous future without lifting a finger. They had youth on their side. Only the old needed government assistance to enjoy the harvest of a Promised Land.

Id. at 95.

have made investments in Social Security and Medicare that must be honored. Therefore, the One Fund Solution would cause the SSA to make a present value analysis of the contribution and expected benefits reduced by future contributions for each person in the present system and create an account with an initial deposit into each such person's One Fund Account in an amount based on such analysis. This analysis does not create a new federal liability; it merely recognizes the existing liability and allocates it among those in the system.⁴⁵⁵ Thereafter, FICA taxes would be deposited into the individual account and the account would be credited with a return equal to inflation plus 3%.⁴⁵⁶ Unlike current contributions to Social Security and Medicare, funds in the One Fund Account would be available to purchase healthcare insurance and pay the deductibles and other health care costs.⁴⁵⁷ Health care costs for those under age sixty-five are paid either through employer-provided healthcare plans or through Medicaid.⁴⁵⁸ Employers would have the option of continuing existing plans or making contributions to their employees' One Fund Accounts. Medicaid recipients would have a premium subsidy deposited into their One Fund Accounts. These One Fund contributions would be used to purchase health insurance policies meeting minimal requirements from

455. By recognizing its obligation to each account based on current contributions, the federal government will capitalize the unfunded liability and by recognizing the liability it will take action to eventually discharge that obligation. In October, 2006 the Financial Accounting Standards Board issue Statement No. 158, requiring public and private companies and non-governmental not-for-profit organizations to recognize and report the unfunded or overfunded status of its defined benefit and other post retirement plans. The Fin. Accounting Found., STATEMENT OF FINANCIAL ACCOUNTING STANDARDS NO. 158: EMPLOYERS' ACCOUNTING FOR DEFINED BENEFIT PENSION AND OTHER POST-RETIREMENT PLANS – AN AMENDMENT OF FASB STATEMENTS 87, 88, 106, AND 132(R) 2-3 (Sep. 2006).

456. Butler, *supra* note 1, at 525. The 3% is an average that is somewhat lower than historical GDP growth. See U.S. DEPARTMENT OF COMMERCE, BUREAU OF ECONOMIC ANALYSIS, *Gross Domestic Product – percentage change from preceding period*, <http://www.bea.gov/national/index.htm#gdp> (last visited Feb. 6, 2012).

457. See Butler, *supra* note 1, at 526-27 (stating that additional contributions by employer could be used to fund health care and disability insurance).

458. CONG. BUDGET OFFICE, THE BUDGET AND ECONOMIC OUTLOOK, *supra* note 335, at 62 (describing the coverage of Medicaid and the anticipated growth and increased costs associated therewith); see FAMILY WEALTH MGMT., *supra* note 217, at 721. At age sixty-five, individuals become eligible for Medicare. Since Medicare does not cover all medical expenses, eligible beneficiaries over age sixty-five may still qualify for Medicaid and be considered a "dual eligible" beneficiary. Iris J. Lav & Andrew Brecher, *Passing Down the Deficit: Federal Policies Contribute to the Severity of the State Fiscal Crisis*, 2004 STT 109-4 (2004), http://www.lexisnexis.com/lawschool/research/default.aspx?ORIGINATOR_CODE=00092&signoff=offhttp://www.cbpp.org/5-12-04sfp.pdf. The National Commission proposed putting dual eligibility in Medicaid managed care as a cost saving measure. *Moment of Truth*, *supra* note 22, at 39. Medicaid pays the costs of nursing home care for up to 70% of nursing home residents. GRAETZ, UNNECESSARY RETURNS, *supra* note 22, at 194.

“authorized” private providers. However, the determination of which plan to purchase would be at the option of the One Fund Account owner. If the employer or Medicaid contribution exceeded the cost of the insurance, the excess would remain in the account.⁴⁵⁹

With the gradual elimination of the income tax exclusion of employer-provided health insurance, the employer would be indifferent whether health care costs were used to provide health insurance, paid directly to the employee, or deposited into the employee’s One Fund Account. If paid into the One Fund Account, employees could determine how their funds were used.⁴⁶⁰

A married couple earning \$50,000 annually and covered by a reasonably comprehensive health plan can be said to have an income of \$63,825.⁴⁶¹ This income is the base salary of \$50,000 plus \$10,000 for health insurance and \$3,825 representing the employer’s portion of FICA taxes.⁴⁶² If the employer pays the cost of the health insurance into a fund along with the employee and employer FICA, there would be a contribution of \$17,650 placed in the taxpayer’s account. That money would be used to provide health insurance and related costs and funds for retirement and be subject to limits necessary to assure a long

459. Subject to appropriate disclosure and coverage requirements, health insurance providers would offer policies to individuals through the One Fund Account. Account holders would then elect the level of coverage they desire for themselves and their family. A minimum level of “high deductible” coverage would be required for each individual and their dependents that would be funded through subsidies and real earnings on the One Fund Account. Because it is the individual’s money, the individual can use it in a limited way consistent with maintaining sufficient balances for long-term needs.

460. Major decisions as to the level of insurance, deductible amounts, and health care decisions would be left to the individual, who would, hopefully, have the means to fund a portion of his own care. Because the contributions start at a young age and before life begins to exact its toll for emergency spending, the individual will have a taste of what it means to save. The individual will also see his savings grow without being undermined by inflation or the ultimate burden of taxation when used for life’s important savings events.

461. See *supra* note 73 and accompanying text. Certain employee fringe benefits, such as health insurance, are not included in gross income. I.R.C. §§ 105, 106 (2006). They are not typically included in a discussion of an employee’s income. However, as a technical matter, when discussing effective tax rates or the economic value of an employee’s income, they should be considered since if they were not provided the employee or the government would have to provide them.

462. The cost for healthcare insurance may be low. It has been noted that “[i]n 2008 healthcare benefits contributed 7.1 percent of total compensation cost for workers in private industry (10 percent of average wages).” Peter J. Wiedenbeck, *Taxes and Healthcare*, 124 TAX NOTES 889, 892 (2009). Wiedenbeck further notes that during the four year period 2001 to 2005, median income for persons covered by family health insurance rose only 3% while the national average cost of family health insurance rose 30% from \$8,281 in 2001 to \$10,728 in 2005. *Id.* In 2008, the cost was \$12,680 for family coverage and \$4,704 for employee only coverage. *Id.* at 893.

term-term buildup of funds for retirement.⁴⁶³ Such restrictions balance the government's oversight of individual well-being against the individual's sense of responsibility and freedom of choice, a balance I call "American Paternalism."

Minimum contributions of say 15.3% of payroll to the One Fund Account to cover healthcare and retirement would be required until the fund reached \$1 million and could continue to be made on a voluntary basis until the account value reached \$2 million.⁴⁶⁴ After the account reached \$2 million, no further contributions would be permitted. Monies in the One Fund Account would be invested in government guaranteed bonds,⁴⁶⁵ provided however, once the account reaches a threshold of \$100,000, the account owner could elect to invest in diversified low cost private equity or bond funds. The government's role would be to set standards for withdrawals that would provide the account owner with some level of confidence that he would not run out of funds during retirement.

Contributions to the One Fund Account would include after-tax dollars, but lifetime or death time distributions would be tax-free up to a maximum tax-free distribution of \$2 million. Transfers at death could be to the One Fund Account of the owner's heirs or devisees, thereby building multi-generational wealth in lieu of multi-generational debt. By providing every person the identical opportunity to achieve tax free income, the One Fund Account should be the exclusive vehicle for tax-advantaged savings. Savings arrangements outside the One

463. For example, if the program targets an income for life of \$40,000 to cover retirement healthcare and living, the couple would need to accumulate approximately \$800,000 to purchase a joint-life annuity at sixty-five years of age with a 3% annual increase. After more than forty-five years of working, the couple would need to contribute \$5,000 annually and have it accumulate at a rate of 5%. Inflation would impact both the amount contributed and the amount needed to purchase the annuity.

464. *Moment of Truth*, *supra* note 22, at 53 (recognizing the need to encourage individuals to take responsibility for their own families through a lifetime of work. Employers and employees can create a system of savings that is "open to all, portable, prevent leakage from high fees and early withdrawals and allow for pooled investments that can spread the risk.").

465. The government-guaranteed bonds would bear an interest rate equal to the cost of living plus an additional amount reflecting growth in the economy. Because withdrawals are tax free, the account owner would be protected against erosion from currency inflation and from taxation when withdrawn or at death. President Bush's 2005 proposal for private accounts allowed individuals to invest a portion of their Social Security taxes in private investment accounts, and then reduce their eventual Social Security benefits by an amount equal to the amount diverted to the private account plus interest at a rate of 3% plus the rate of inflation (i.e. a real rate of interest at 3%). PETER A. DIAMOND & PETER R. ORSZAG, *SAVING SOCIAL SECURITY: A BALANCED APPROACH* vii-ix (2005). The inflation adjusted 3% is the projected interest rate on government debt. *Id.* at x.

Fund Account would be taxed on a current basis.⁴⁶⁶ Tax expenditures for healthcare and retirement as well as those for housing and education would be gradually eliminated.⁴⁶⁷

Because it is your money and you may need it now, the One Fund Solution makes it available for current uses—provided such distributions do not interfere with the long-term build up of the fund for retirement. Decisions on the use of the funds will reflect personal choice. For example, an eighty-year-old retiree with funds in his One Fund Account may choose a particularly high deductible health insurance policy or one with a limited annual payout. If that individual later faces a medical condition that requires a significant co-payment, he would choose whether to pay the medical co-payment, keep the funds for other purposes, or pass them on to the next generation at death. In either case, it is the individual's decision.

Some commentators think it inappropriate to force an eighty-year-old retiree to choose between paying for medical care and keeping money for future uses.⁴⁶⁸ In reflecting on means-testing for long-term care under Medicaid, Professor Michael Graetz expressed concern that Medicaid may condemn “many elderly Americans with long-term care need to finish their lives in or near poverty.”⁴⁶⁹ Responsible savings earlier in life would

466. See Calvin H. Johnson, *Repeal Roth Retirement Plans to Increase National Savings*, 124 TAX NOTES 773, 773-74 (2010) (explaining that individuals currently contribute to 401(k) plans on a pre-tax or post-tax basis and to I.R.C. § 529 educational savings plans on a post-tax basis and describing the tax effects of IRAs and 401(k) plans and the repeal of the Roth type plans); Benjamin H. Harris & Rachel M. Johnson, *Automatic Enrollment in IRAs: Costs and Benefits*, 128 TAX NOTES 903, 903 (2009) (describing tax treatment of IRAs and 401(k) plans); James R. Hamill & Craig G. White, *The Interaction of Broad-Based State Scholarship Programs with Federal Education Credits*, 109 TAX NOTES 515, 521-22 (2005) (describing tax effects of IRC § 529 plans). Under the One Fund Solution the individual can continue to make such contributions, but only on a post-tax basis (e.g. in the same manner as is currently being done in the Roth IRAs or educational savings plans). Money can be withdrawn for various uses, such as home ownership, hardship, or education, provided basic levels of funds are maintained in the One Fund Account for health care or retirement security. Because the One Fund is the sole vehicle for tax benefited investment growth, all other tax motivated savings methods should be repealed.

467. See *Moment of Truth*, *supra* note 22, at 29 (suggesting that most tax expenditures should be eliminated). The \$2 lifetime limitation per individual on tax-free withdrawals from the One Fund Account should be sufficient to accommodate the lifetime savings needs of most citizens for education, the down payment on a home, health care, and retirement. To the extent the individual needs additional amounts to support a desired life style, he is free to save on an after tax basis.

468. See *Moment of Truth*, *supra* note 22, at 50 (recognizing the risk that more seniors living into their eighties will run the risk of running out of money and proposing that, twenty years after becoming eligible for Social Security, senior benefits would increase by one percent of the average benefit each year for five years).

469. GRAETZ, UNNECESSARY RETURNS, *supra* note 22, at 194.

permit many elderly to underwrite medical care during retirement through privately purchased insurance, as would further limitations on the ability of seniors to effectively dispose of their assets for the purpose of qualifying for Medicaid when they enter a nursing home.⁴⁷⁰

Indiana Governor Mitch Daniels has suggested that Medicare beneficiaries should share in the cost/benefit decision over medical treatment, rather than simply have the government decide which treatments are cost effective.⁴⁷¹ If someone decides to expend tens of thousands of dollars during their final weeks of life, that person should understand that any inheritance their children would receive would be wiped out, cut in half, or otherwise reduced.⁴⁷²

Because it is your money and you have the opportunity to make contributions beyond the required contributions, you have some flexibility in using the money during your working life. By recognizing that it is your money, you have an incentive to continue saving and spend it wisely. As appropriate levels are reached, investing in certain commercially managed investment funds is available if the owner desires to take some risk in exchange for higher returns. Account balances can be devised or pass subject to laws of descent and distribution at death thereby creating an opportunity to enrich the next generation.⁴⁷³

470. See FAMILY WEALTH MGMT., *supra* note 217, at 721-37 (describing the process and restrictions on qualifying for Medicare); see also Lynda Yamamoto, *Overcrowded Prisons and Filial Responsibility: Will States Utilize "Support of the Indigent" Statutes to Solve the Baby Boomer and Prison Crises?*, 41 RUTGERS L. J. 435, 443-445 (2009) (describing the controversy surrounding Medicaid eligibility in a state's attempt to balance personal responsibility for one's own long-term care with the government's interest to minimize expenditures while providing for those truly in need); see Chadwick Bothe, *The Stigma of Survival: Medicaid Estate Planning*, 51 S. TEX. L. REV. 815, 822-30, 836-37 (2010) (examining in detail the moral controversy surrounding such planning and concluding that the crippling cost of long-term care and the actuarial date on life expectancies among other things make such planning not only necessary but moral).

471. See Mitch Daniels, *An ObamaCare Appeal From the States*, WALL ST. J., Feb. 7, 2011, at A19, available at <http://online.wsj.com/article/SB10001424052748703652104576122172835584158.html>. Indiana Governor Mitch Daniels has instituted a system in Indiana that targets Medicaid ineligible persons and provides modest wealth transfers to enable such persons to obtain health care. See Richard A. Epstein, *Bleak Prospects: How Health Care Reform Has failed in the United States*, 15 TEX. REV. LAW & POL. 1, 36-37 (2010).

472. See David Leonhardt, *Budget Hawk Eyes Deficit*, NEW YORK TIMES, Jan. 4, 2011, at B1, available at <http://www.nytimes.com/2011/01/05/business/economy/05leonhardt.html?pagewanted=all> (quoting Governor Mitch Daniels of Indiana in an interview).

473. Butler, *supra* note 1, at 524-25. Individuals may be reminded of the saying of King Solomon in ancient Israel that "a good man leaves an inheritance to his children's children, but a sinner's wealth is laid up for the righteous." *Proverbs* 13:22. Among the debt reduction proposals, there is little discussion about the cost to the government of

The One Fund Solution does not eliminate governmental programs established to supplement the income of low-income individuals either to provide general revenues or premium support for medical insurance during the person's working years or in retirement. However, such funds should be deposited in the person's One Fund Account with specific authority to use those funds for designated purposes but with authority not to expend them if the recipient so desires. Again, except for medical insurance premiums and the need for accumulating funds for retirement, the individual could either leave the funds in the account to grow with other funds or use them for current expenses.⁴⁷⁴

Transition to the One Fund Solution does not diminish the cash flow to the Treasury. What it does is capitalize the liability, much of which is unfunded, and allocate that liability to individual account holders. Of course the unfunded trust funds established for Social Security and Medicare would be used to support those over fifty-five as needed until those beneficiaries move through the system. To the extent that the One Fund Solution accommodates health insurance for those under age fifty-five, it would involve new disbursements that would be paid for through additional payroll taxes, voluntary contributions, increased taxes, or elimination of tax expenditures.

Institution of the One Fund Solution would be paid for through the elimination of individual tax expenditures, thereby freeing the Internal Revenue Service to concentrate on collecting revenue rather than administering social programs.⁴⁷⁵ Elimination or serious restriction of tax expenditures may be a concept whose time has come.⁴⁷⁶

family breakdown. Pressures undermining long-term monogamous relationships such as no-fault divorce, pre-nuptial agreements, and concepts of separate property permit marriages of convenience which impoverish women and children when they breakdown. Provisions incorporated into One Fund Accounts to encourage long-term relationships may reduce long-term support costs of low income persons.

474. See Butler, *supra* note 1, at 527-28.

475. The case for curbing tax expenditures is succinctly set forth in McMahon, *supra* note 230, at 788-91.

476. See Moment of Truth, *supra* note 22, at 29-30; David Cay Johnston, *Making Tax Simple*, 130 TAX NOTES 347, 347 (2011) (lauding national taxpayer advocate Olson's efforts to promote tax reform and suggesting that the complexity in the code signals that the time is right to reexamine provisions including the mortgage interest deduction); Jeremy Scott, *Mortgage Interest Deduction Might be key to Tax Reform Efforts*, 130 TAX NOTES 361, 361 (2011); Martin A. Sullivan, *Mortgage Deduction Heavily Favors Blue States*, 130 TAX NOTES 364, 365-66 (2011) (evaluating the impact of the mortgage interest deduction on various states, noting that states with the highest per capita benefit from the mortgage interest deduction all voted for President Obama in the 2008 election, and suggesting that Democratic senators might be lukewarm at best about limiting the deduction to less expensive homes than Republicans).

Administration of the check writing function would be the responsibility of the Social Security Administration. As with all proposals, tax expenditures would be phased out over a period of time, but eventually, they would cease to be a part of American tax system.⁴⁷⁷

The One Fund Solution creates a uniform tax-advantaged account for all citizens that would then allow all other income to be subject to a progressive income tax. Every effort would be used to broaden the base, so as to tax all income on a current basis and as appropriate in a coordinated system. Tax revenues increased by the elimination of tax expenditures would be used to fund the continuing obligations to those persons fifty-five and older at the time of implementation. Over time, funds will build up in the One Fund Accounts in excess of distributions for such accounts. At that point, such excess revenues can be used to pay off foreign debt, thereby allowing American citizens to replace fore holders of American debt. Of course, enforcement mechanisms will be necessary to avoid the federal government from using such excess funds on current spending.

By requiring an inflation-adjusted return on investment, the One Fund Solution will place an incentive on the federal government to keep inflation to a minimum and give account owners assurance that their savings will not, to the extent invested in government bonds, be diluted by inflation. The accounts would also be protected against taxes since withdrawals are not taxed. Thus, unless the individual account owner chooses to invest in private investment funds, their retirement income would be predictable. By allowing the funds to be passed at death, many individuals would begin life with a nest egg to be used build a better life for that generation.

Eliminating individual tax expenditures would go a long way toward simplifying the tax code and providing needed revenue to balance the budget.⁴⁷⁸ Base-broadening will permit a reduction in income tax rates as well as funds for discharge of federal

477. Any attempt to eliminate tax expenditures will spark long, heated, and emotional debates, which is why elimination over a period of time would be required. See Eric Kroh, Meg Shreve, Drew Pierson, *Eliminating Tax Expenditures Not AS Simple As It Sounds, Panelists Say*, 130 TAX NOTES 380, 380 (2011).

478. National Taxpayer Advocate Nina Olson sees the key to tax reform is to reduce the top individual tax expenditures and points to the five-year cost (2010-2014) of healthcare (\$659 billion), mortgage interest deduction (\$484 billion) and reduced tax rates for dividends and capital gains (\$403 billion). Amy S. Elliott, *Congress Should Reduce Tax Expenditures, Olson Says*, 130 TAX NOTES 1256, 1256 (2011). Olson points out that it is not the corporate tax expenditures that are causing the loss of revenue but the individual tax expenditures. *Id.*

entitlement and debt obligations.⁴⁷⁹ Broadening the corporate tax base through elimination of tax expenditures and lowering the rates would further simplify the tax code as many have suggested.⁴⁸⁰ Keeping the top personal rate and top corporate rate nearly the same would avoid distorting choice of entity decisions.

By removing tax expenditures from the income tax and keeping it simple by using the One Fund Account as a vehicle to provide support for the less fortunate, the need for an additional tax can be avoided. Could fixing the income tax which has been successful in the United States for almost 100 years would alleviate the need for a VAT?⁴⁸¹ It is important to recognize that a Congress that cannot correct the income tax is unlikely to keep a VAT simple with a broad tax base and lower rate.⁴⁸² Keeping a VAT simple requires the same will power and ability to say “no” to powerful constituencies that is currently lacking in Washington.⁴⁸³ We will merely have two “engines of revenue.”⁴⁸⁴ The VAT has its own unique problems, such as the potential for

479. See *Moment of Truth*, *supra* note 22, at 12.

480. See *id.* at 43.

481. Michael Graetz and others answer that such a reform would be inadequate to address the debt situation and the need for growth. See Michael J. Graetz, *VAT as the Key to Real Tax Reform*, in *THE VAT READER: WHAT A FEDERAL CONSUMPTION TAX WOULD MEAN FOR AMERICA* 112, 115 (Tax Analysts, 2011). It seems that the sheer amount of revenue that is likely to be needed is sufficient to deter consideration of merely reforming the income tax. Victor Thuronyi, *Progressive Corporate Tax Reform*, 130 *TAX NOTES* 1303, 1304 (2011).

482. See Sijbren Cossen, *A VAT Primer for Lawyers, Economists, and Accountants*, 124 *TAX NOTES* 687, 697 (2011) (providing recommendations for the U.S. to follow in keeping the VAT simple). Keeping VAT from stimulating growth of government is a major concern which may require special controls to restrain Congress. Carroll & Viard, *supra* note 441, at 1126. One method is to dedicate the VAT revenue stream to a trust fund of use for a specific purpose such as health care. *Id.* Another method suggested is to have the VAT replace the payroll tax completely with a 17.6% VAT, which would be sufficiently high to deter any increase. *Id.*

483. Ironically, saying “no” might be the reason the U.S. finally adopts a VAT. One commentator thinks that Democrats and Republicans will unite to adopt a VAT because they will have no other choice when the Republicans say “no” to tax increases and the Democrats say “no” to entitlement cuts. Avi-Yonah, *supra* note 442, at 337.

484. See Drew Pierson, *Fiscal Commission Took Serious Look at VAT, Members Say*, *TAX NOTES TODAY*, Mar. 9, 2011, para. 4, [http://services.taxanalysts.com/taxbase/tnt3.nsf/\(Number/2011+TNT+46-5?OpenDocument&Login](http://services.taxanalysts.com/taxbase/tnt3.nsf/(Number/2011+TNT+46-5?OpenDocument&Login) (quoting Erskine Bowles). The National Commission of Fiscal Responsibility and Reform did not recommend a VAT, not because it objected to a consumption tax, but because there was “concern among the commission members that the creation of a VAT would simply end up as a major supplement to, and not a replacement of, the income tax . . .” *Id.* The other reason a VAT was not recommended was that the U.S. Senate had voted overwhelmingly for a nonbinding resolution rejecting a VAT. *Id.* In a contrary statement, National Taxpayer Advocate Nina Olsen reflected on a comment from William Gale that a solution will be found and that it will be something that now is considered impossible, such as a VAT. See Elliott, *supra* note 478, at 1257.

creating a new black market in untaxed goods that is the bane of many European Countries.⁴⁸⁵ America once had an income tax collection ability that was completely voluntary and that was the envy of the world.⁴⁸⁶ Let us try to regain that distinction.

Because the government would guarantee an inflation adjusted, tax-free return on a person's investment in the One Fund Account, it would also be relatively simple for the government to offer to convert amounts in the account to a lifetime annuity when the individual reaches retirement age.⁴⁸⁷ Such a proposal has been suggested for converting I.R.C. § 401(k) plans into a federally guaranteed annuity upon retirement.⁴⁸⁸ In transitioning to the One Fund Solution, participants in other existing tax-benefited plans would have the option to transfer these other plans into their One Fund Account subject to the annual limitations.

The One Fund Solution is a long-term solution. It seeks to build wealth over time that can be passed on to the next generation. Every option presents painful immediate decisions. The One Fund Solution offers long-term choice and perhaps a road to financial freedom: freedom to rent or buy, spend or save, be frugal or extravagant, and financially secure or insecure.

485. See Amity Shlaes, *A VAT Will Make Us Eurotrash*, 126 TAX NOTES 251, 251-52 (2010). Shlaes graphically asserts:

VATs are marvelously intricate and promise plentiful revenue for tax professionals. You'll be hearing the technical arguments for a VAT — VATs are efficient, VATs don't distort the supply chain the way other taxes do, and so on.

But there's one big objection to a VAT. VATs make countries sleazy. In other developed nations, the presence of a VAT is not hard for the visitor's eye to discern. In VAT countries there is a certain scum on the surface of things, an unfriendliness, a sense that life proceeds smoothly and opulently behind closed doors rather than down on the shabby open sidewalk with the rest.

Id. at 251. Shlaes describes how the incentive to evade the VAT has become a national pastime. See *id.* A vendor can avoid paying income tax on a sale and a buyer can avoid paying VAT on a purchase if both are willing to evade the tax system. See *id.* at 252. After describing the efforts in the 1960s and 1970s to get the United States to adopt a VAT had failed, Shlaes recommends that we continue to resist the temptation stating, "[f]ortunately, our leaders rejected the levy. This time, too, let them say: Not VAT again." *Id.* at 252.

486. See Butler, *supra* note 324, at 303.

487. See Lawrence A. Frolik, *Protecting Our Aging Retirees: Converting 401(k) Accounts into Federally Guaranteed Lifetime Annuities*, 47 SAN DIEGO L. REV. 277, 278 (2010). The Social Security benefit described herein is a form of a lifetime annuity. Many insurance companies offer annuity products in exchange for a given lump sum payment. Therefore, it would be a relatively simple matter to include an annuity option on an individual's One Fund Account.

488. See *id.* at 278.

VII. CONCLUSION

America is not only struggling to recover from a deep recession but it also stands on the brink of an economic crisis that could precipitate uncontrollable inflation or a catastrophic economic meltdown.⁴⁸⁹ The economic danger points signaling that the country has entered into economic unknown territory are the deficit exceeding 3% of GDP and the ratio of debt held by the public to GDP exceeding 60%.⁴⁹⁰ There is general agreement that entitlement associated with Medicaid, Medicare, and Social Security coupled with the imminent retirement of the baby boom generation makes the crisis inevitable without prompt action to bring these elements under control.⁴⁹¹

Numerous ideas addressing the current situation present complete, reasonable, well thought out solutions. However, there is little time to implement whatever solution finds political consensus, but, a failure to make a decision is a decision to let the costs fall where they may when the crisis occurs.⁴⁹² Currently, the missing ingredient is political will and an electoral consensus to implement a solution.⁴⁹³ The situation can be summarized as follows: “The only question is whether policymakers address the debt problem now in a deliberative and thoughtful manner, or whether they will be forced to so by a sudden economic crisis.”⁴⁹⁴

This article has set forth the nature of the problem, examined the current proposals to solve the problem, outlined numerous considerations impacted by current government policy and likely to be impacted by any solution, and recognized that no solution is likely before the presidential elections in 2012. Finally, the article presents the One Fund Solution as a preferable long-term solution that has the advantage of creating private accounts for each person in the Social Security system.

Like other proposals, it calls for elimination of the complex and innumerable tax expenditures as a part of the solution that is preferable to the introduction of a VAT. Additionally, it supports a healthcare system providing premium support giving participants some degree of choice while protecting low income individuals with direct grants instead of targeted benefits. The

489. See *Moment of Truth*, *supra* note 22, at 11.

490. See Domenici & Rivlin, *supra* note 22, at 27-28; *Moment of Truth*, *supra* note 22, at 14, 56.

491. See *Moment of Truth*, *supra* note 22, at 11.

492. See *id.*

493. See Domenici & Rivlin, *supra* note 22, at 13.

494. *Id.*

One Fund Solution recognizes that “it’s my money and I need it now.” When people see their savings growing over the years, while being protected from inflation and taxes, they will have an incentive to make rational choices that protect their respective financial security.⁴⁹⁵

Any decision will cause immediate economic pain, but the pain suffered today is far less than the uncontrollable pain that will be suffered at some indefinite time in the future. A further reason to take action now is that it is unpredictable how long the younger generation will stand still seeing their wages transferred to the elder generation.⁴⁹⁶ One commentator sees that a “new reality” is realigning the electorate.⁴⁹⁷ He states: “A shrinking and debt-ridden youth cohort cannot and will not continue to subsidize an expanding and more affluent retired generation. Soon, 65 will be the new 50. We are going to see lots more seniors working well into their 70s.”⁴⁹⁸

495. See Frolik, *supra* note 487, at 329-30.

496. See Victor Davis Hanson, *U.S. Faces New Reality As Old Order Dies*, INVESTORS BUS. DAILY, Jan. 28, 2011, at A13 <http://news.investors.com/ArticlePrint/561146/201101271829/US-Faces-New-Reality-As-Old-Order-Dies.aspx>.

497. *Id.*

498. *Id.*