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A In-Depth Analysis of The Federal Tax System

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Benjamin Franklin once said, “In this world, nothing can be said to be certain, except death and taxes.” While death is somewhere off in the future, everyone has to pay taxes in most cases when something of monetary value exchanges hands. It’s a part of everyday life for people, but most people don’t understand why they pay taxes, what taxes are used for, whether the government is doing a good job, and whether they are being taxed fairly. So what are taxes? According to the Oxford Dictionary, a tax is “a compulsory contribution to state revenue, levied by the government on worker’s income and business profits or added to the cost of some goods, services, and transactions” (Oxford University Press). Failure to pay taxes to the government may land individuals and businesses in big trouble with the IRS (Internal Revenue Service), which is the governing body that oversees the proper collection of taxes for the United States. Besides the federal government levying taxes, state and local governments also have the power to levy taxes on its residents. There are a number of different types of taxes that are implemented by local, states, and federal governments, and they generally fall in one of two categories: direct taxes and indirect taxes.

Direct taxes are taxes paid directly to the government by the persons on whom it is imposed. One of the most common types of direct taxes is income taxes, which are basically taxes on income that an individual or business generates. Income taxes are generally what individuals deal with and complain about the most when they think of taxes. Another type of direct tax is property taxes, which is a tax on the appraised value of real property meaning both land and land improvements. People may also be taxed on what they inherit from someone, who dies and leaves them property or items of monetary value and this is called an estate tax. Estate taxes are very complicated, and they have a whole section of the IRC (Internal Revenue Code) devoted to them, which is called Subtitle B—Estate and Gift Taxes. The US also has an expatriation tax for individuals, who have left the US for any reason, over a certain threshold. There is also a wealth tax, which a tax based off of the total value of assets and equity owed by an individual. Raising wealth taxes have been very controversy point of debate in Congress due to the growing need for the government to raise revenue and pay off its growing deficit. Besides individuals getting taxed, businesses that make a profit in the US are taxed based off of any profit that they make.

On the other hand of direct taxes, there are indirect taxes, which are taxes paid by consumers to a third party who then proceeds to pay them to the government. The most common form of indirect taxes that the US sees is the sales tax, which is a percentage tax set by states on certain goods and services. Another form of indirect taxes for individuals are payroll taxes that are deducted from the paycheck and are used towards paying for income taxes, social security contributions, and medicare tax. These deductions from the pay check are also called "pay as you go tax." Employers take these deductions and add their own portion of the payroll tax that they have to pay, and they write a check to the government. Since the business pays the government directly for the payroll tax, it is a direct tax for the business. Taxes do not have to be mutually exclusive. Another example of a tax that is both direct and indirect is a transfer tax, which is a tax on the transfer of any property or document. Gift taxes and estate taxes are both examples of transfer taxes. A tax similar to the sales tax is the VAT (which stands for Value Added Tax). The VAT is calculated by the amount of value added to each stage of production, and the tax that is paid to the seller is paid to the government. However unlike the sales tax, it does not matter if the buyer is the end consumer or a just a producer buying raw materials in order to produce a finished product. The amount of tax that the buyer charges is the value they added less the tax that they paid their seller; and the difference between the two is the amount that the government receives. This process is repeated for every seller or buyer until it is at the end consumer, so the tax burden is spread among the buyers and not just passed off to the end consumer. The US does not have VAT, but it has grown popular in other developed nations in Europe and China. Excise taxes are another big tax that the US implements. Unlike the sales tax and the VAT, they are already built into the price of specific products like gasoline, tobacco, and alcohol; and consumers usually have to pay sales tax and VAT in addition to the excise tax. The excise tax for tobacco, alcohol, and other harmful products are usually called the sin tax. Sometimes imports from other countries or exports going to other countries are taxed when they enter the country or exit the country in order to promote trading within or outside the country. These taxes on imports or exports are called tariffs.

There are many different types of taxes; and besides being taxed directly or indirectly, a tax can be progressive, regressive, or proportional. In order to understand how a tax is progressive, regressive, or proportional, it is necessary to understand what a tax rate is and if it is effective or marginal. A tax rate is the percentage at which a business or individual is taxed; so for example, every dollar that a person spends at a store in Tennessee, they pay a $0.0925 sales tax to the state government. The $0.0925 for every dollar is usually expressed as a 9.25% tax rate. Individuals can have many different tax rates that they pay on their taxable income, and the average of all of their tax rates is the effective (or average) tax rate. The marginal tax rate is the tax rate that applies to the last amount of taxable income. For instance, for an individual with $20,000 of income filing their federal income tax return, the first $8,925 of income is taxed at 10% and the remaining $11,075 of income is taxed at 15%. The 15% tax rate is the marginal tax rate, or the amount paid on every additional dollar of income, but the effective tax rate is 12.77%, which is the weighted average of the two tax rates. A tax is progressive if the effective tax rate increases as the taxable amount increases. The US Federal tax system implements a progressive tax where the tax rate increases with every bracket of additional income that an individual makes. The opposite of a progressive tax is a regressive tax, where the effective tax rate decreases as the taxable amount increases. An example of this would be sales tax since the sales tax would decrease the effective tax rate of a wealthy individual while the same sales tax may have increase the effective tax rate of a low earning income individual. In the middle of progressive and regressive tax, there is the proportional tax, which is a tax rate that is fixed so there is no change when the income increases or decreases.

Now the the major of the different types of taxes have been defined, the basic structure and purpose of the laws can be explain. But the overview given above is in the most basic of terms and forms, so there is still a lot of material about taxes not cover. Because the US tax system is a complicated system with a combination of these different types of taxes. The basis of the US tax system is the IRC, which is called the Internal Revenue Code or Title 26. The IRC covers a number of topics from income taxes, estate and gift taxes, excise taxes, the trust fund code, health plan requirements, etc, but it does not include title 11, which is related to bankruptcy, and title 28, which is related to the judiciary part of taxes. Since it encompasses so many topics and Congress keeps just piling section over sections, it has nearly 10,000 sections and over 300 updates pending to the code. With nearly 10,000 sections, the IRC is very confusing and has a lot of loopholes.

In order to understand the complexities of the IRC, it is necessary to understand who is being taxed. There are a few major business entities: individuals, sole proprietorships, partnerships, s-corporations, corporations, and trusts and estates. An individual is a taxable entity that is taxed on any income made. The IRS divides individuals into four filing statuses: single, head of household, married filing jointly, and married filing separately. An individual files single if they are unmarried and have no dependents. A dependent for the purposes of the IRS is usually a child, who may be a natural born child or adopted child, but maybe any individual, who depends on another individual for housing, food, and financial support and who does not claim their own deduction and personal exemption on their tax return. A person files head of household status if they are single or considered single on the last day of the tax calendar year, paid for more than half of the upkeep for their home, and have one or more qualifying dependents. Couples file married filing jointly if they are married and file their tax return together, or they file married filing separately if they are married but want to file separately. The IRS makes both spouses filing married filing separately use the same type of deduction (standard deduction for both or itemized deduction for both) and other allowances are limited, so they do not get to double-dip and receive extra benefits from tax breaks. With each status, there are different income ranges for the seven different marginal tax rate brackets (see table 1 for example of the breakdown of income ranges and marginal tax rates for individuals filing single). The marginal tax rates are the same for all individual filing statuses, however the taxable income ranges do

Table 1—If Individual's filing status is single, 2013

Taxable Income		
Over	**But Not Over**	**Marginal Tax Rate**
$0	$8,925	10%
$8,925	$36,250	15%
$36,250	$87,850	25%
$87,850	$183,250	28%
$183,250	$398,350	33%
$398,350	$400,000	35%
$400,000	And Over	39.6%

vary due to filing status. This variation in income brackets is a way of creating a fair and progressive tax, so no one is burdened with more taxes than they can afford. Many people get confused on how much in their tax rate actually is. For example, if a person filing as single with $40,000 in taxable income, the first $8,925 will be taxed at 10%, the next $27,325 will be taxed at 15%, and the final $3,750 will be taxed at 25%, which comes out to a total tax liability or the amount you owe of $5,928.75 [($8,925 * 0.10) + ($27,325 * 0.15) + ($3,750 * 0.25)]. That individual's effective tax rate actually turns out to be 15.83%, which is the weighted average of the tax rates, and their marginal tax rate is simply the last tax rate that they applied on their last dollar, which is 25%. Many people get confused and believe that the government is taxing all of their money at the marginal rate. Where an individual falls on the table depends on their taxable income, which is defined as all included items of income earned by that individual less applicable expenses and deductions. Calculating taxable income is where most people get confused since the government has so many rules, exclusions, and stipulations of what qualifies as income, deductible expenses, and eligibility for deductions. For instance, besides having ordinary income, which can be classified generally as salaries, wages, rental income, short-term capital gains, and ordinary dividends, people can also have long-term capital gains or qualified dividends, which are taxed at preferential rates like 0% or 15% depending on what their the marginal tax bracket is. Once an individual has their total income computed, they have to subtract their expenses incurred in the year. Expenses that individuals can subtract from income to get their AGI (or Adjusted Gross Income) include education expenses, business expenses, moving expenses, the deductible portion of self-employment tax, alimony paid, retirement deductions, and education expenses (student loan interest and tuition and fees). Once an individual has their AGI, individuals also have to figure out they should take the standard deduction of $6,100 (for people filing single status in 2013) or if they should itemize their deductions. A brief summary of deductible expenses would include investment losses, charitable contributions, interest expenses (including mortgages), educations expense, family expenses, automotive expenses, medical expenses, casualty and theft losses and a number of other miscellaneous items. 65.6% of individuals use the standard deductions, and many of those who use the itemized deduction are wealthier individuals, who have tax accountants keeping track of and calculating their itemized deductions (IRS).

Once AGI has been calculated and deductions and exemptions have been taken, an individual has their taxable income, where you then use a table like Table 1 on page 5 to calculate the tax owed. A comparison of the tax liability with the AMT (Alternative Minimum Tax), which is an income tax for entities above a certain threshold to pay more taxes, and the regular tax liability is made, and the larger of the two amounts is taken to compute tax owed. Once the tax liability amount is reached, credits, like the foreign tax credit, education credits child tax credit, etc, are subtracted from it. These credits are non-refundable credits that will reduce tax liability but will not reduce it below zero to a negative number (i.e. a refund). However, there are refundable credits like earned income credit (for individuals with children earning below a certain income threshold) and the American Opportunity Credit that reduce tax liability below zero and the government will pay you money (which is called a refund). The other way to get a refund from the government is to overpay tax owed with withholding too much from salaries and wages. This explanation of a federal individual income tax return is a basic explanation, and there are many more facets of an individual return due to the complex nature of the IRC and the multitude of forms based on the monetary activity of each individual.

The next type of business entity is a sole proprietorship, which is where one individual owns an unincorporated business by themselves. A sole proprietorship is a flow-through entity, meaning that all of the losses and gains that the business has are flowed through the entity and on to the proprietor (the owner). So the proprietor is responsible for their own 1040 (the individual income tax return form) as well as a number of forms on the business like a Schedule C (the profit or loss form for the business) and a Schedule SE (the self-employment tax form). The number of forms that the proprietor fills out is based on the complexity and activity of the business; but the complexity of the forms can be quite extensive and usually require a professional on the tax code to prepare. The next kind of business entity is a partnership, which is similar to a sole proprietorship; however unlike the sole proprietorship, there are two or more individuals owning and operating the business. Like the sole proprietorship, the partnership is a flow-through entity, where the earnings and losses flow through the entity to the owners. Although partnerships are flow-through entities, they do have a separate form that the IRS requires the business to fill out, which is the 1065. The 1065 consists of five pages, where the income, expenses, questions about the entity, the partnership distribution of shared items, the analysis of income (or loss), a simplified balances sheet, a books to tax reconciliation, and an analysis of partner's capital. The end form for the partners is a Schedule K-1, which breaks down the partner's share of income, deductions, credits, and other items for the year and what each partner should report on their tax return. Other kinds of partnerships are LLPs (Limited Liability Partnerships), LLCs (Limited Liability Companies), and PLLCs (Professional Limited Liability Company (PLLC), which are mixtures of sole proprietorships, partnerships, and corporations. These limited liability companies are all still flow-through entities; but instead the partners being responsible for all of the losses and damages of the partnership, the partners are only liable for losses up to their portion of the partnership. A lot of accounting firms and law firms are set up as LLCs to mitigate the losses and damages due to malpractice or unethical behavior on the part on one partner or employee. S-Corps are another type of business entity, which is a flow-through entity for tax purposes. S-Corporations have a number of restrictions like only having 100 shareholders, one class of stock (meaning no common and preferred stock), and be incorporated inside the US. For tax purposes, the S-Corps file the form 1120, which is similar the 1065 partnership tax return form except it is for corporations. Schedule K-1s for the 1120s are distributed to the shareholders to account for their share of profits and losses from the tax year.

Unlike sole proprietorships, partnerships, and S-Corps, corporations are not flow-through entities but a separate legal entity. Corporations are taxed from 15% to 35% on their taxable income in the US (see Table 2); however the effective tax rate for US corporations in the 2010

Table 2—For Corporations, 2013

Taxable Income		
Over	**But Not Over**	**Marginal Tax Rate**
$0	$50,000	15%
$50,000	$75,000	25%
$75,000	$100,000	34%
$100,000	$335,000	39%
$335,000	$10,000,000	34%
$10,000,000	$15,000,000	35%
$15,000,000	$18,333,333	38%
$18,333,333	And Over	35%

tax year was 12.6% (O'Toole). Looking at Table 2, it is set up much in the same way that Table 1 on page 5 for the single status individual taxpayer was set up, and it is calculated the same way with each tier applying the marginal tax rate on its tier of additional income, not applying the marginal income on all of the taxable income. Both the federal and state governments can tax corporations, which can top corporate tax rates at 39.2% and corporations are also subject to the AMT like individuals (O'Toole). Many corporations get tax breaks from the various credits and off-shore tax havens and by utilizing tax professionals for financial structuring. Corporations, like S-Corps, file the form 1120 and various other forms that depend on the business of the corporation and the level of financial activity of the corporations. While all of the profits and losses flow through to the owners in the case of the other entities, the corporation is its own entity, so it keeps the majority of its income. However when corporations are making steady profits, they can issue dividends to their stockholders with net income after the corporation has already paid taxes on its income. These dividends are added into the income of the entities that hold them, and then they are taxed again on that entities' tax return. Sometimes, dividend income is taxed three times when a corporation distributes dividends to another corporation, who holds their stock. That receiving corporation is then taxed again on the dividend income that they received, and they may decide to distribute dividends to their shareholders, who are taxed again on their dividend income. There are many intricacies to corporate tax, but that level of detail is not needed for this paper.

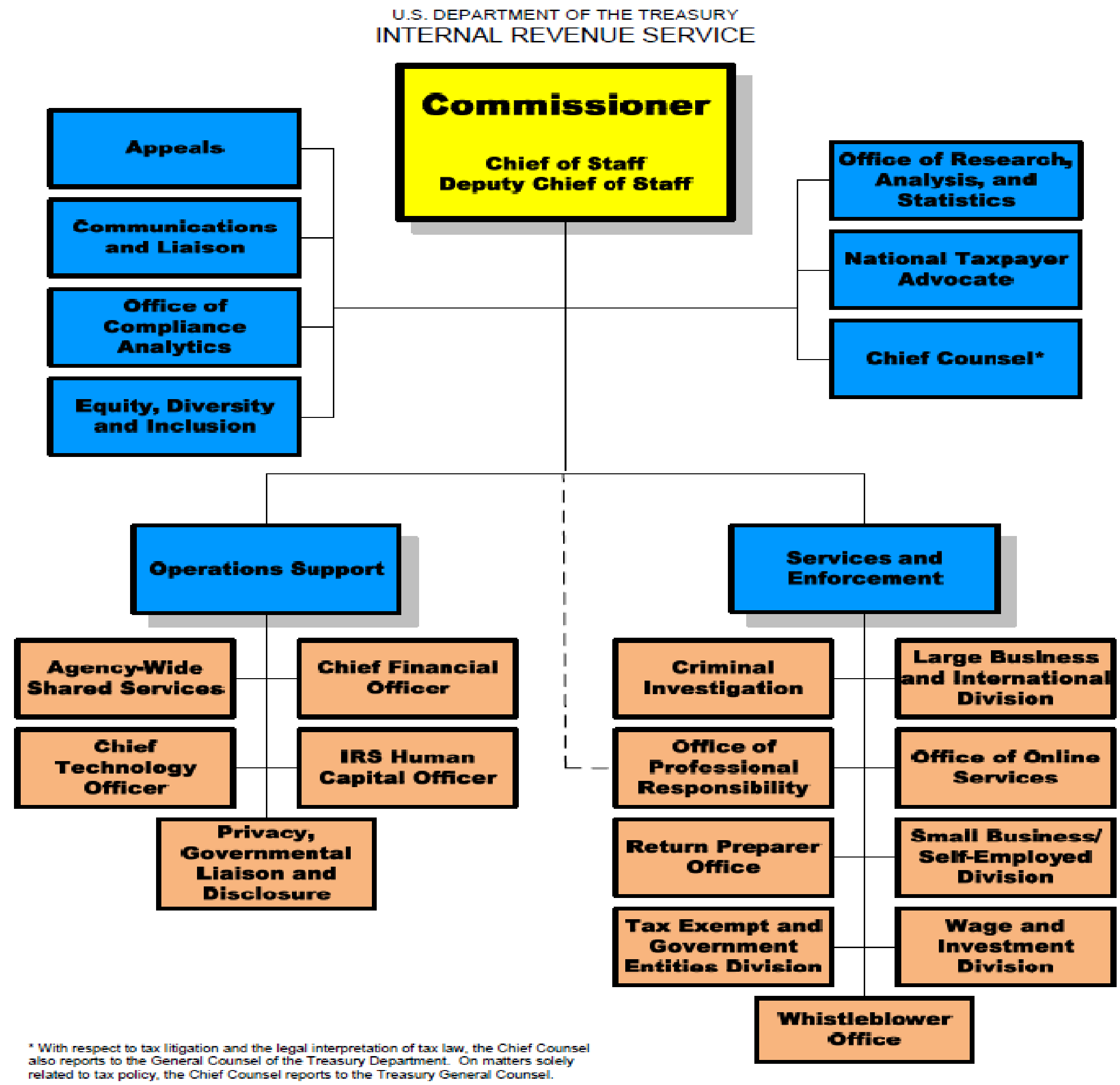
The final general type of taxable entities is trusts and estates, which can be taxed at the entity level or the beneficiary level. An estate is a legal, taxable entity that continues on after the individual dies and earns income like interest, dividends, and capital gains. An example of an estate is Michael Jackson's living estate that continues to earn royalties and other forms of income from any of the decreased musician's work, but not all of Jackson's assets were in the estate so the musician's will was examined to decide what to do with the assets. Every estate has to file a Form 1041, which is the form for estates and trusts, but they only have to pay taxes is the value of the estate is more than $1.5 million. If the value of the estate is more than $1.5 million, then the estate also has to file a Form 706, which is the estate tax form. Notice the term used for taxation purposes is value or assets, and not income, because the estate is not taxed on income but rather the total value of assets of the estate. The other legal, taxable entity, like an estate, is a trust, which is created by an individual to protect their assets and to distribute income to the beneficiaries. Beneficiaries are the individuals, who receive the income of the estate or trust, so in the example above of Michael Jackson's estate, the beneficiaries are his children. The trust, like the estate, reports its income and tax on Form 1041, but since it distributes income, it uses a K-1 form to keep track of the distributions to the beneficiaries. There are many different types of structures of estates and trusts, and they are structured in order to receive the maximal tax benefit.

Now that the generally gist of who is a taxable entity and how income tax is calculated has been explained, there is still the question of why everyone pays taxes? US citizens and other residents earning income in the US pay taxes to the government in order to pay for government expenditures, like infrastructure, national defense, subsidies, Medicare, Social Security, and other government services. If the public did not pay for these services, the standard of living would not be as high as it is now for US residents. For instance, without federal subsidies on corn and other farm products, the cost of produce and other food items would be higher since the subsidies allow farmers to sell produce, like corn, below the cost of production. Government programs, such as Medicare and Social Security, provide financial help for medical expenses and port-retirement living expenses for the poor and elderly, who cannot afford those expenses without help. Part of the reason for those programs and other social welfare acts implemented by the government is to redistribute the wealth from the rich to the poor. Taxation tries to achieve this goal through a progressive tax system, where the effective tax rate is larger for the wealthy than it is for the poor. The idea behind the redistribution of wealth is to create a more financially egalitarian society where everyone has the same opportunities and benefits. Besides paying for social welfare, taxes also help to regulate and restrict certain types of business practices, products, and goods. An example of this restriction is the sin tax on tobacco and alcohol. Another example of taxes being used to restrict or regulate certain types of business is a tariff, which promotes local growth while increasing prices on imports. Raising taxes can also be used to reduce the discretionary spending when individuals have discretionary fund, and therefore control inflation by reducing spending.

So how does the US tax system compare to the ideal concept of taxation and does it achieve their goals? The US tax system is created by Congress, which is made up of politicians without much tax expertise. But first, the IRS needs to evaluate its productivity based on its goals and mission statement. The mission statement of the IRS is, "Provide America's taxpayers top quality service by helping them understand and meet their tax responsibilities and enforce the law with integrity and fairness to all" (IRS). In order to achieve its mission, the IRS has created 3 main departments: the Commissioner, the Deputy Commissioner for Services and Enforcement, and the Deputy Commissioner for Operations Support (see Figure 1 on page 13 for chart). Within those 3 main departments, there are a number of subcommittees and departments that are each in charge of a different task. The Commissioner Department consists of the Chief Counsel; the National Taxpayer Advocate Service; Appeals; Equity, Diversity, & Inclusion; and

Communications & Liaison. The Deputy Commissioner for Services and Enforcement is primarily in charge of the daily operations of the IRS and the enforcement of the IRC. The Deputy Commissioner for Operations Support department "oversees the integrated IRS support functions, facilitating economy of scale efficiencies and better business practices" (IRS.gov). The IRS is a complex organization with numerous layers of bureaucracy and departments.

Figure 1—Diagram of Internal Revenue Service



Working together, the 3 departments of the IRS are supposed to provide a fair and understandable tax system to the US taxpayers. In Table 3 provided by the IRS, the breakdown of the type, number, and the gross amount collected from tax returns filed in the US for 2011.

Table 3—Type, Number, and Gross Amount Collected from Tax Returns Filed, 2011

Type of Return	2011	Gross Amount Collected
Corporations	2,312,909	242,848,000,000
Individual	143,607,800	1,331,160,000,000
Employment Taxes	29,445,812	767,505,000,000
Excise Taxes	522,165	49,338,000,000
Gift Tax	207,858	6,572,000,000
Estate Tax	11,128	2,507,000,000
Total	**176,107,672**	**2,399,930,000,000**

Looking at Table 3 above, the IRS had the most returns from individual income tax returns, which numbered around 143,607,800 tax returns in 2011. Of those 143.6 million individual tax returns filed, over 55% of those returns were filed by using paid preparers (IRS), and nearly 83 million taxpayers requested assistance from the IRS. 83 million out of 143.6 million is 57.8% of taxpayers needing assistances with some part of their tax returns. With over 55% of the population paying tax professionals to do their taxes and 57.8% of taxpayers requesting assistance from the IRS, it doesn't seem like the tax system is very easy to understand from the general publics' point of view. The 57.8% of taxpayers who requested assistance from the IRS are part of an even a bigger percentage since the IRS only answered 68% of its phone calls due to the long wait times that discouraged 32% of its callers to hang up before they talk to an IRS representative (Pergram). The 68% of phone calls answered by the IRS is down from the previous year, which was down from 72% of calls answered (Carrins). Average phone call hold time for IRS assistance was 10 minutes in 2010 and grew to 17 minutes in 2012 (Pegram). The IRS has an even worst success rate with answering written correspondence; a whopping 48% of written correspondences are answered by the IRS in the time frame needed (Pergram). This service provided by IRS in recent years is clearly not living up to the ideal of provided "top quality service."

The idea that the US federal tax system is too complex for the American public is further supported by a survey conducted by the Tax Foundation in 2009, which found that four out of five Americans or 85% of Americans found the tax system to be too complex (Moon). The IRC, as it is known today, come into being with the Internal Revenue Code of 1986, which codified all of the previous statutes Congress had previously issued since the federal income tax become permanent with the 16^{th} Amendment that legalized income taxes. The IRC of 1986 Act was actually just a redesign of the 1954 Code, so most of the terminology and content was the same as it was in 1954. That means that the IRC contains content from 1954, which is almost over 60 years ago. To put the last 60 years in perspective, in 1954, there were only 201 individual income tax returns with AGI over $1 million; whereas in 2010, there were 280,360 returns with AGI over $1 million (IRS). 5,000 changes have been made to the IRC since 2001 that is an average of 1.14 changes per day (Erb). Taking into account all of those changes, the IRC is from start to finish is a total of nearly 4 million words (Erb). While Congress has been making all of those changes to the IRC, a part of Congress (the House Republicans) has also been pushing to reduce the IRS's budget from over $12 billion this year to $9 billion in the next fiscal year (Pergram).

However the reduction in budget may decrease the productivity within the IRS even more since they are already not sufficiently staffed, as indicted by their ability to answer the questions of the taxpayers. In Table 4, the IRS's budgets without the proposed cut are shown by budget activity.

Table 4—A Detailed Breakdown of IRS Budget from 2011 to 2014

Budget Activity	FY 2011	FY 2012	FY 2013	FY 2014--Requested
Taxpayer Services	$2,293,272	$2,239,703	$2,253,510	$2,412,576
Taxpayer Assistance & Education	$678,204	$625,189	$632,514	$660,197
Filing & Account Services	$1,615,068	$1,614,514	$1,620,996	$1,752,379
Enforcement	$5,492,992	$5,299,367	$5,331,000	$5,666,787
Investigations	$644,479	$636,386	$611,233	$661,631
Exam & Collections	$4,689,220	$4,504,885	$4,565,257	$4,842,007
Regulatory	$159,293	$158,096	$154,510	$163,149
Operations Support	$4,056,716	$3,947,416	$3,971,000	$4,480,843
Infrastructure	$926,190	$929,634	$916,269	$939,182
Shared Services & Support	$1,291,568	$1,214,514	$1,239,929	$1,305,701
Information Services	$1,838,958	$1,803,268	$1,814,802	$2,235,960
Business Systems Modernization	$263,369	$330,210	$332,231	$300,827
Health Insurance Tax Credit Administration	$15,481	$0	$0	$0
Subtotal, IRS	$12,121,830	$11,816,696	$11,887,741	$12,861,033
Offsetting Collections – Reimbursements	$141,078	$122,451	$109,193	$110,627
Mandatory Appropriations – User Fees	$285,805	$326,251	$511,425	$277,582
Miscellaneous Items	$0	$246,694	$284,331	$108,765
Total Program Op Level	$12,548,713	$12,512,092	$12,792,690	$13,358,007

All amounts in the table above are in thousands.

In Table 4 on page 16, there has been a slight dip in taxpayer services, which doesn't really make sense. The number of tax returns that are being filed is constantly increasing, so in order to achieve the goal of helping the public to understand and fulfill their tax responsibilities, the IRS would need to increase its support services for taxpayer's in a correlating manner to the number of returns. Enforcement of tax law has also decreased a bit, but that dip may be attributable to the increase in business systems modernization, which an effort by the IRS to modernize all of its systems and improve its business process. With the modernization efforts, the IRS would be more capable of detecting cases of fraud. Even though Enforcement has dipped, it still accounts for about 45% of the IRS's budget in 2011, 44% in 2012, 43% in 2013, and 43% in 2014 (see Pie Chart 1 on page 18). While the taxpayer services has remained pretty constant at 18% to 19% in each of the budgets. The appropriation of funds for the various activities in the IRS seems more focused on the "enforce the law with integrity and fairness to all" portion of their mission statement (IRS). However the case could be made that if the IRS focused equally on the education of America on their tax responsibilities or reducing the complexity of the tax code so most people could understand it, then they would be more likely to pay their taxes instead of trying to find ways to evade their taxes. And this idea of educating the public on their responsibilities goes back to the purpose of taxes, which is to redistribute the wealth of the nation from the rich to the poor for the utilitarian benefit of the whole nation. More people would be willing to pay their "fair" share of taxes if they knew for sure that they were going to a good cause.

Going back to focusing on the budget, the effectiveness and efficiency of the IRS can be gleamed from it and other relevant financial data. The total revenue collected by the IRS in 2011 as shown in Table 3 on page 14 was $2.4 trillion, and the total program operation level expenses in 2011 as shown in Table 4 on page 16 was $12 billion. The profit margin is 99.48%, and the average return on investment in 2011 is $191:$1 (gross amount collected divided by total expenses). Looking at these numbers, anyone would think the IRS is doing a great job with the budget and resources that they have. Looking at the allocations of resources, enforcement is the bulk of the IRS's budget as seen in Pie Chart 1, but looking at Table 5 on page 19, tax evasion from 2001 to 2010 amounted to $3.09 trillion. The IRS collected $2.35 trillion in taxes with a $12.1 billion budget (Journal of Accountancy) in 2010. The average return on investment for the 2010 fiscal year was $194:$1, so for every dollar the IRS spent, they earned the federal government $194. The average return for the entire IRS is good; however let's have a closer look

Pie Chart 1—Percentages of Activities from 2011 to 2014

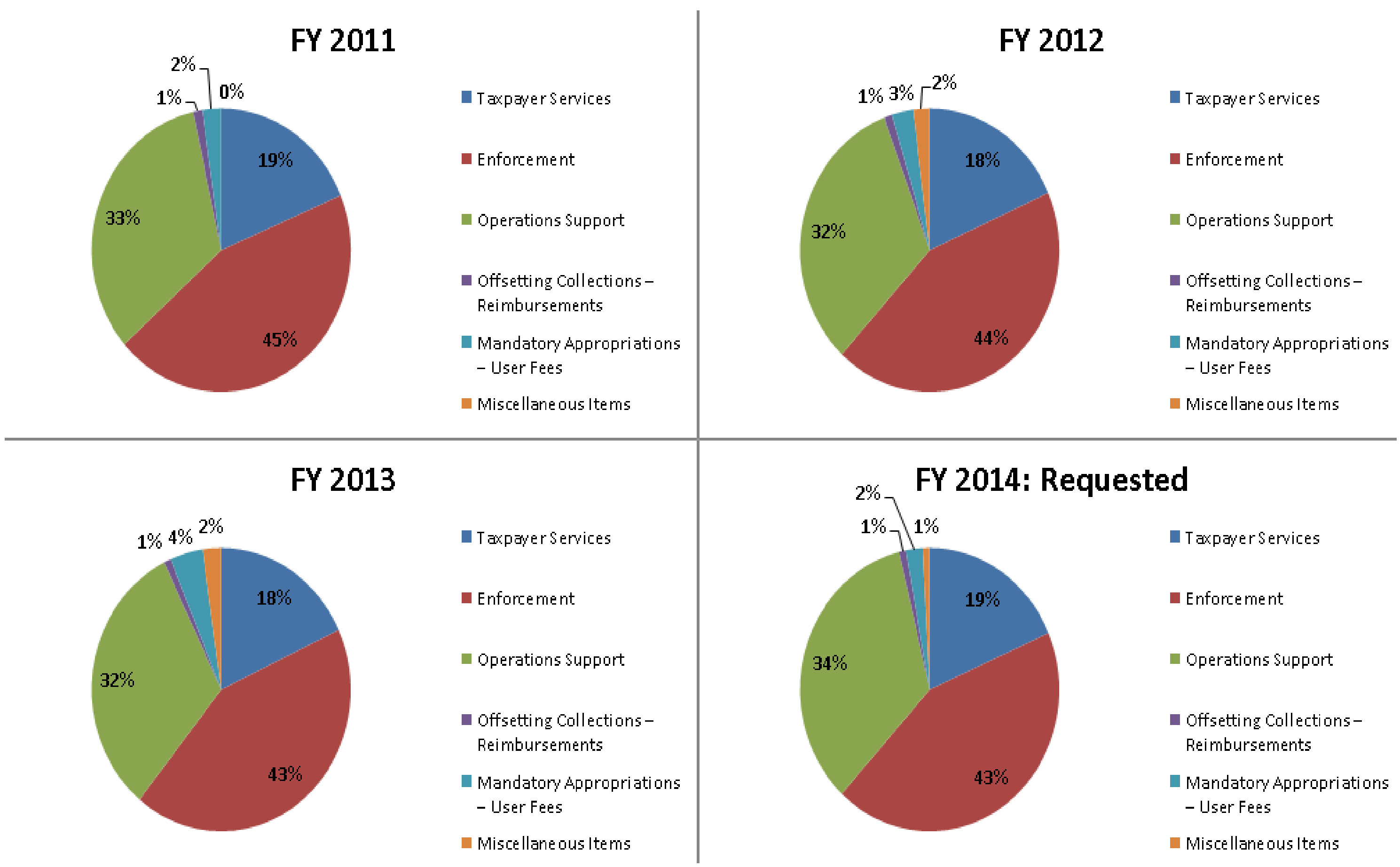


Table 5—Breakdown of Revenue Lost Due to Tax Evasion from 2001-2010

Year	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Revenue Lost	$290	$269	$257	$27t2	$314	$350	$376	$357	$304	$305

All dollars in the table above are in billions.

at the enforcement department budget and return. The revenue potential of the IRS enforcement department is the revenue lost due to tax evasion ($305 billion), the delinquent collections ($29.8 billion), and civil penalties for evasion ($18 billion), which amounts to a total of $352.8 billion (IRS). The enforcement budget for 2010 was $5.5 billion, so the average return on investment for the enforcement department is $64 for every $1 spent (IRS). In comparison with the enforcement budget, the average return on investment for all of the budgeted activities is the gross tax collected less enforcement revenue, which is 2 trillion ($2.35 trillion less $352.8 billion), divided by the expenses excluding enforcement, $6.6 billion (12.1 billion less $5.5 billion). The average return on investment excluding enforcement for 2010 was $303 for every $1 spent. Of the $303 billion lost due to tax evasion, 85% of that lost was due to individuals and the remaining 15% was due to corporations and employers. The majority of individuals, who commit tax fraud, underreport their income and are middle income filers. The effort expended by the IRS on enforcement isn't as profitable for the U.S., so it should focus its efforts on serving the taxpayers about their responsibilities and by simplifying the complexity of the tax code.

Besides the IRS serving individual taxpayers, they also have to serve corporate taxpayers. One look inside the productivity and goal achievement of the IRS in regards to its corporate taxpayers is a look at the enforcement budget of the IRS. Corporate tax takes a large slice of the Enforcement budget, because part of the money goes to paying whistleblowers absurd amounts for providing information to the IRS on companies that are evading their tax liabilities even though as stated earlier corporations and employers only amount to 15% of the money lost due to tax evasion. The IRS paid $125 million to whistleblowers in 2012; and the bulk of the money going to Bradley Birkenfeld, who was awarded $104 million for revealing UBS's program that helped taxpayers hide their assets (O'Toole). In 2006, legislation was passed that allowed the IRS to award "whistleblowers who provide the IRS with evidences of unpaid taxes in excess of $2 million" with up to 30% of the sum recovered (O'Toole). With the $125 million awarded to the whistleblowers, the IRS collected more the $592 million, which is a ROI of $4.74 for every dollar spent on the whistleblowers. Giving whistleblowers up to 30% of the revenue collected seems like a large amount that is unnecessary when a couple million seems sufficient to reveal what they know. Continuing to look at corporate taxes in the US, the IRS collected $242 billion from corporations and businesses in 2011 as seen in Table 3 on page 14, but the effective tax rate of corporations was 12.6% (Schwartz). In Table 2 on page 9, the highest bracket of profits for corporations has a marginal tax rate of 35% and the lowest bracket for corporations has a tax rate of 15%. So how is it possible that corporations are paying less than the lowest profit bracket? The answer is that many corporations take advantage of deductions and legal loopholes in the tax systems. All large corporations have a tax department that takes care of the in-house tax matters; and they also usually have outside CPA firm, like PwC, Ernst & Young, KPMG, or Deloitte, who take care of their tax returns to capture all of the credits, deductions, and other tax savings to reduce its tax liabilities. The Big Four made a total of $44 billion in the US alone, and obviously not all of that income is for tax work but a large chunk of it is. Tax services for each corporations can be anywhere from $100,000 to over $1 million each tax season, which implies that corporations paying for these services are reducing their tax services by a considerable amount. It can also be inferred since most large corporations have both a tax department doing their everyday tax upkeep matters and a large CPA firm actually doing their tax return that the tax system is too complicated on the business side as well as being too complicated on the individual side.

Looking at Table 3 on page 14, 2,312,909 corporate returns were filed, which is 1.3% of all the tax returns filed, and $242 billion was collected from those corporate returns, which is 10.1% of the gross revenue collected. Using those numbers from Table 3 in 2011, that is an average of $104,997 of taxes paid per corporations filing. $104,997 in taxes is equivalent to an individual who has a taxable income of $366,261 would pay in taxes. It's a little ridiculous that large corporations can get away with paying that little to the government when they make hundreds of millions of dollars or even billions of dollars. The structure and laws of the tax system in regards to corporate taxes needs to change, so that corporations bare an equivalent amount of the tax burden. In addition to taking advantage of legal loopholes and deductions, many companies incorporate and headquarter outside of the US, because the US has the highest tax rates among all of the developed countries. In Table 6 below, the top 20 tax regimes for businesses are listed with their corporate income tax rates and their tax revenue to GDP ratio.

Table 6—Corporate Tax Rates in Top 20 Tax Regimes

Country	Corporate Rate	VAT	Tax Revenue as a Percentage of GDP
United Arab Emirates	0.0% except for foreign banks and oil companies	No (considering it)	1.4%
Qatar	10.0%	No	2.2%
Saudi Arabia	20.0%	No	5.3%
Hong Kong, China	16.5%	No	13.0%
Singapore	0.0% - 17.0%	Yes (7.0%)	14.2%
Ireland	25.0%/12.5%/10.0%	Yes (23.0%)	30.8%

Bahrain	0% except for oil companies	No	4.8%
Canada	11.0% to 15.0%	Yes (5.0%)	32.2%
Kiribati	23.4%	No	20.7%
Oman	22.0%	No	2.0%
Kuwait	10.7%	No	1.5%
Mauritius	15.0%	Yes (15.0%)	19.0%
Denmark	25.0%	Yes (25.0%)	49.0%
Luxembourg	29.6%	Yes (15.0%)	36.5%
Malaysia	25.0%	Yes (10.0%)	15.5%
United Kingdom	24.0% - 20.0%	Yes (20.0% or 5.0%)	39%
Kazakhstan	17.5%	Yes (12.0%)	26.8%
Switzerland	23.0% - 13.0%	Yes (8.0%, 3.8%, or 2.5%)	29.4%
Norway	28.0%	Yes (25.0% or 15.0%)	43.6%
Seychelles	25.7%	Yes (15.0%)	32.0%

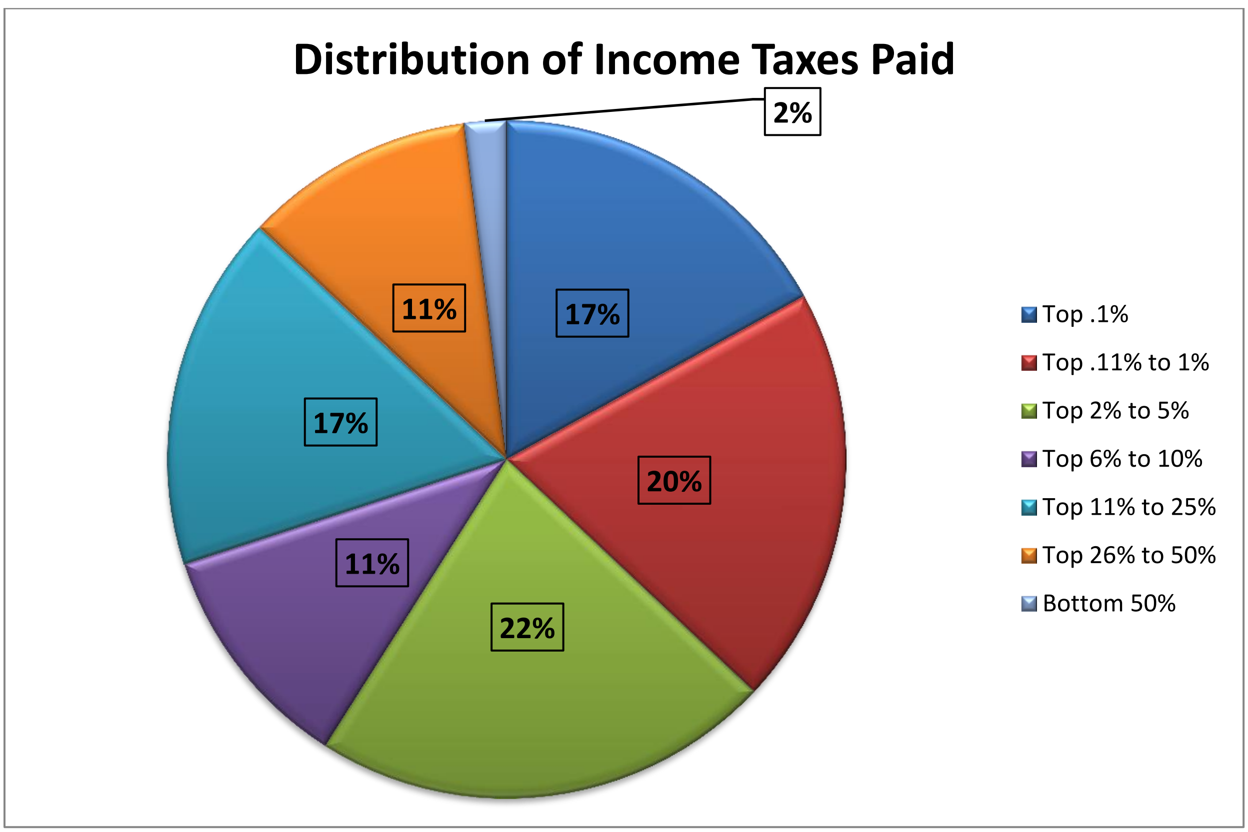
The countries listed above are in order beginning with number 1 and ending with number 20.

The highest corporate tax rate in the chart above is 29.6% in Luxembourg while the US has the highest tax rate in any developed nation; and all of the countries listed above, except for the oil countries, have a VAT, which the US tax system does not have. Many of the countries above are oil producing countries that tax the oil companies, up to 55% of their profits, which makes their tax system very profitable. However it’s not feasible for the US to do that since the US’s primary outputs are services. The tax revenue to GDP ratio is a measure of the growth rate of tax revenue to the country’s growth. The US’s ratio is 25%, which is pretty low among developed nations (Ro). Even though the US has a higher tax rate than everyone else, the US’s revenue isn’t growing as quickly as it is. What does this mean? From the data above, it means that higher tax rates are not the answer to increasing revenue and that the higher tax rates may be scaring away business.

With the resources it has all in all, the IRS seems to be doing pretty well, but what areas can the IRS improve on? Taxpayer education and tax responsibilities. It was mentioned earlier that the majority of Americans do not do their own taxes or understand them, and more importantly, around 57% of Americans do not feel like the current tax system is fair and 59% of those Americans thought that so much is wrong with the current tax system that there should be a total overhaul of it (Pew Research Center). Only 52% of Americans think that they pay the right amount in taxes, but 57% of the populations believes that the wealth do not pay enough in taxes (Pew Research Center). Looking at some of the statistics, 58.3% of tax returns filed are taxable returns, meaning the individual pay money to the government for their tax liability, and out of those individuals who paid taxes, the top 0.10% paid 17% of income taxes, and the top 5% paid 59% of that total income tax paid in 2009 (IRS). The top 25% paid 87% of income tax, and the top 50% paid 96% (IRS). For a more detailed breakdown of the income tax paid in 2009, look at Chart 1 below on page 24. While looking at Chart 1, it seems the amount of tax paid seems very progressive, which is good since that is one of aims of a fair and justice tax system, but the dissatisfaction with tax system is high because most people do not see the statistics but the inefficiencies of the tax system and the high government spending. The high tax brackets do pay the majority of income taxes, but looking closer at the top 1%, the average AGI is around $960,000 and the effective tax rate for that 1% is 24% without taking into account the amounts paid to state and local governments (IRS). The bottom 50% of individuals only paid around 2% of the income taxes paid, and 41.7% of US residents did not pay income taxes in 2009. This percentage of non-income tax payers has increased to 47% as stated by Mitt Romney in 2012

(Ungar). When many people heard that, there was outrage from many people who work every day for their money and pay income taxes, but the statistic itself is misleading and the outrage is an acknowledgement in itself that most people don't understand or like taxes. Because saying 47% of people do not pay taxes is misnomer, because 61% of those individuals are paying taxes through employment taxes that are taken out of their paycheck (Ungar). 17% of those individuals are students, people with disabilities, the long-term unemployed, and other low-income individuals, and the remaining 22% of that 47% are the elderly or retired who have little or no income (Ungar). So the total percentage of individuals who don't pay income taxes is closer to 17% (Marr), which doesn't include illegal aliens who come to the US and work under the table.

Chart 1—Distribution of Income Taxes Paid, 2009

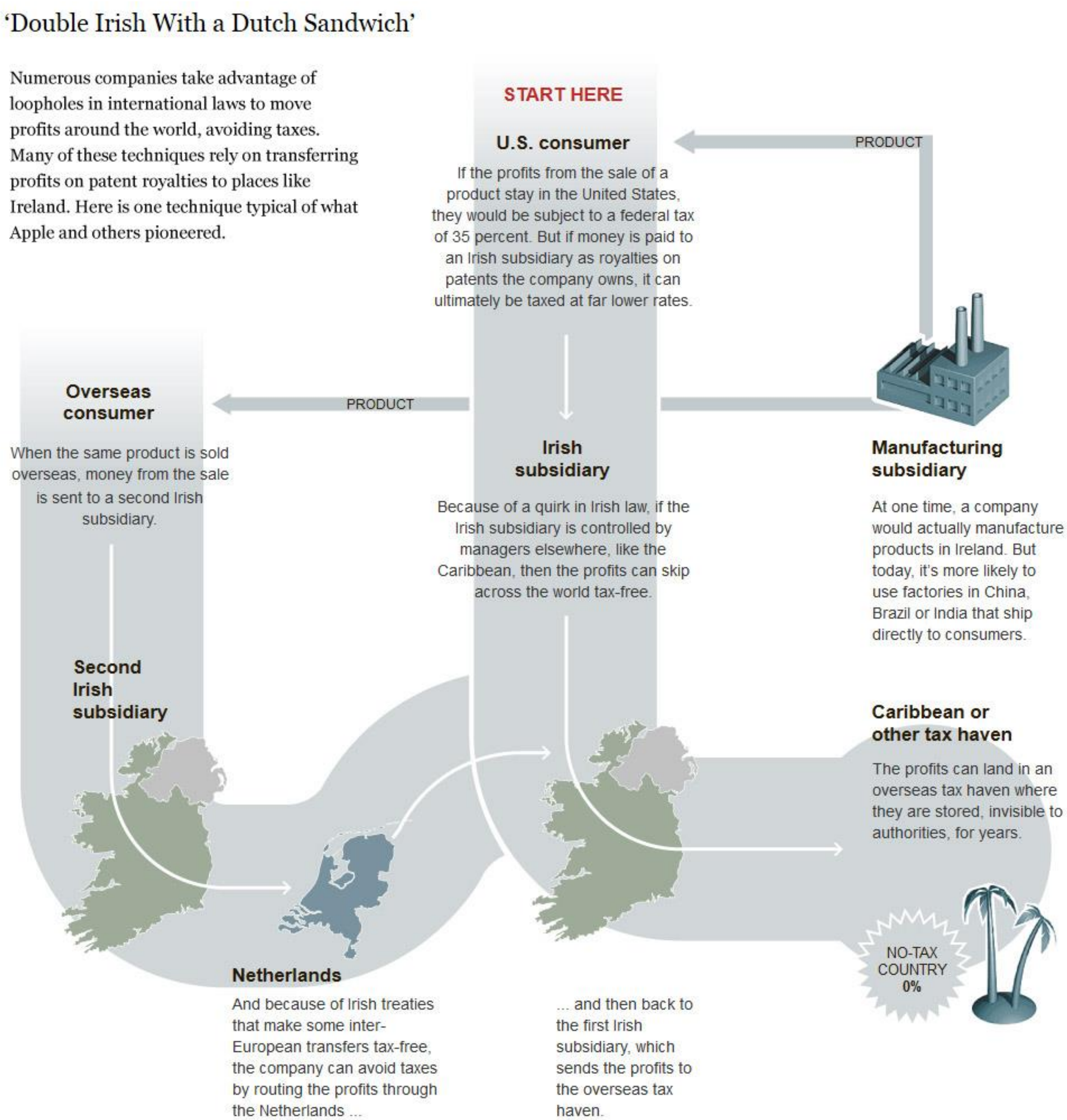


Obviously there is a large amount of discontent with the US income tax system from all sides. The poor and middle class don't believe that the rich pay enough in taxes, while the rich believe that they pay too much in taxes. Many also believe that everyone should pay taxes regardless of income or how small the amount may be. It seems that most people don't know who's paying what, how much they themselves pay, how much others pay, and the tax code in general. This feeling of discontent is magnified by the fact that they don't understand the tax code and they think the part of the code they think they understand is unfair. For instance, many feel that they wealth get too many tax breaks, and they don't believe in the trickle-down economics, which is the idea that if the wealthy are given tax breaks or other economic benefits then they will invest in businesses and other investments that will benefit the lower classes and the economy as a whole. Even though the rich do get a number of tax breaks, they still do make up the majority of the income as see in Chart 1 on page 24. While some of the public is discontent with the rich not paying enough, there are those who think low income individuals and families take advantage of the government. For instance, the Earned Income Tax Credit (EITC), a refundable tax credit, is available to low and medium income individuals and couples with qualifying children. The credit can be as high as $6,044 for filers with 3 or more children, $5,372 with 2 children, $3,250 with 1 child, and $487 with no children for the tax year 2013 (Maag). Refundable credits, like the earned income credit, the child tax credit, and other refundable credits, reduce low income and middle income filers' tax liability below 0 and make the IRS issue a refund to the families. Issuing refunds to families with these credits makes many individuals feel like their hard earned money is going to someone else who has not worked as hard and just went the easy way. However the EITC is an incentive to make individuals work and to get more people to pay into the social security system.

The discontent and dissatisfaction with taxes is clearly evident in the US, because there are constantly headlines of individuals evading taxes. For example, Lil Wayne didn't pay the government a total of $5.5 million in taxes for 2008 and 2009. Wesley Snipes was sentenced to 3 years in prison for failing to file his federal income tax return, which amounted to $7 million in unpaid taxes. And as stated earlier, 85% of tax evasion is perpetrated by individuals. Many more cases of tax evasion are constantly in the news, like the "Real Housewives" star Teresa and Joe Giudice" facing 50 years in prison for evading taxes (Leonard). Obviously the public sees all of these headlines about tax evasion and fraud and about the consequences, but they do not stop doing it. Why don't people stop evading taxes? Well it's never going to totally stop, but the majority of people evade taxes because they do not feel like the amount they have to pay is fair. This goes back to the fact that tax rates in the US are too high, and people are not educated in tax matters and the consequences of evading taxes. This avoidance of paying taxes also suggests that many people don't want to give the government money their hard earned money when they feel like the government is going to waste it.

The discontent with the tax system also extents to corporate taxpayers. Many corporations feel that the tax rate in the US is too high, and to reiterate what was said earlier, the US has the highest tax rate among developed nations. This high tax rate has lead lots of corporations investing in tax shelters to reduce their taxable income and to lighten their tax liability. Many corporations take advantage of the foreign income tax credit, which reduces the tax liability of corporations with foreign source income. One of the most prevalent types of tax avoidance strategies used by corporations, like Apple and Google, is the Double Irish with a Dutch Sandwich, where the company is structured in such a way that it reduces the majority of the companies' tax liabilities. This tax shelter is used most with companies with intellectual property, because the intellectual property is assigned to a subsidiary abroad in Ireland. The company assigns the properties rights to the subsidiary in Ireland, but the company is controlled by managers in a Caribbean country or other tax havens. Using this tactic, any profits made in the US are funneled into the Irish subsidiary, but it is tax free because Irish law only taxes corporation by where they are managed or controlled. So if the company is managed somewhere else, the Ireland does not tax them. Profits made overseas (i.e. not the US) are sent to a SECOND Irish subsidiary, which transfers it to the Netherlands because it is a tax-free transfer within certain European countries. After the company has it in the Netherlands, it is transferred back to the FIRST Irish subsidiary, which transfers it to the overseas tax haven. For a more graphical depiction of the double Irish with a Dutch sandwich, see Picture 1 below on page 28. This tax shelter has saved Apple an estimated "tens of billions of dollars it earned outside the United States in recent years" (Schwartz). Apple is a multinational company valued at over $185 billion paid only a little over $6 billion in taxes last year, even though they should have paid at least $74 billion more than they did from 2009 to 2012 (Schwartz). Apple defends their position of having these offshore subsidiaries by saying "the current system which applies industrial era concepts to a digital economy, actually undermines U.S. competiveness" (Schwartz). Apple may have a point that the US is not competitive in the corporate tax world, especially since many corporations have employed the same tax shelter. Google saved around $3.1 billion in taxes last year with the double Irish tax shelter, and its overseas effective tax rate was 2.4% (Drucker). Other companies that also employ this tax shelter are Microsoft, General Electric, Adobe Systems, Johnson & Johnson, Oracle, Starbucks, Pfizer Inc, etc. All of these companies are worth over billions of dollars and have a larger consumer base in the US, which means that the US is losing billions of dollars in revenue because it is not as competitive in the corporate tax world as other countries. This tax avoidance scheme has angered many in Congress, but only highlights the many loopholes in the corporate tax system.

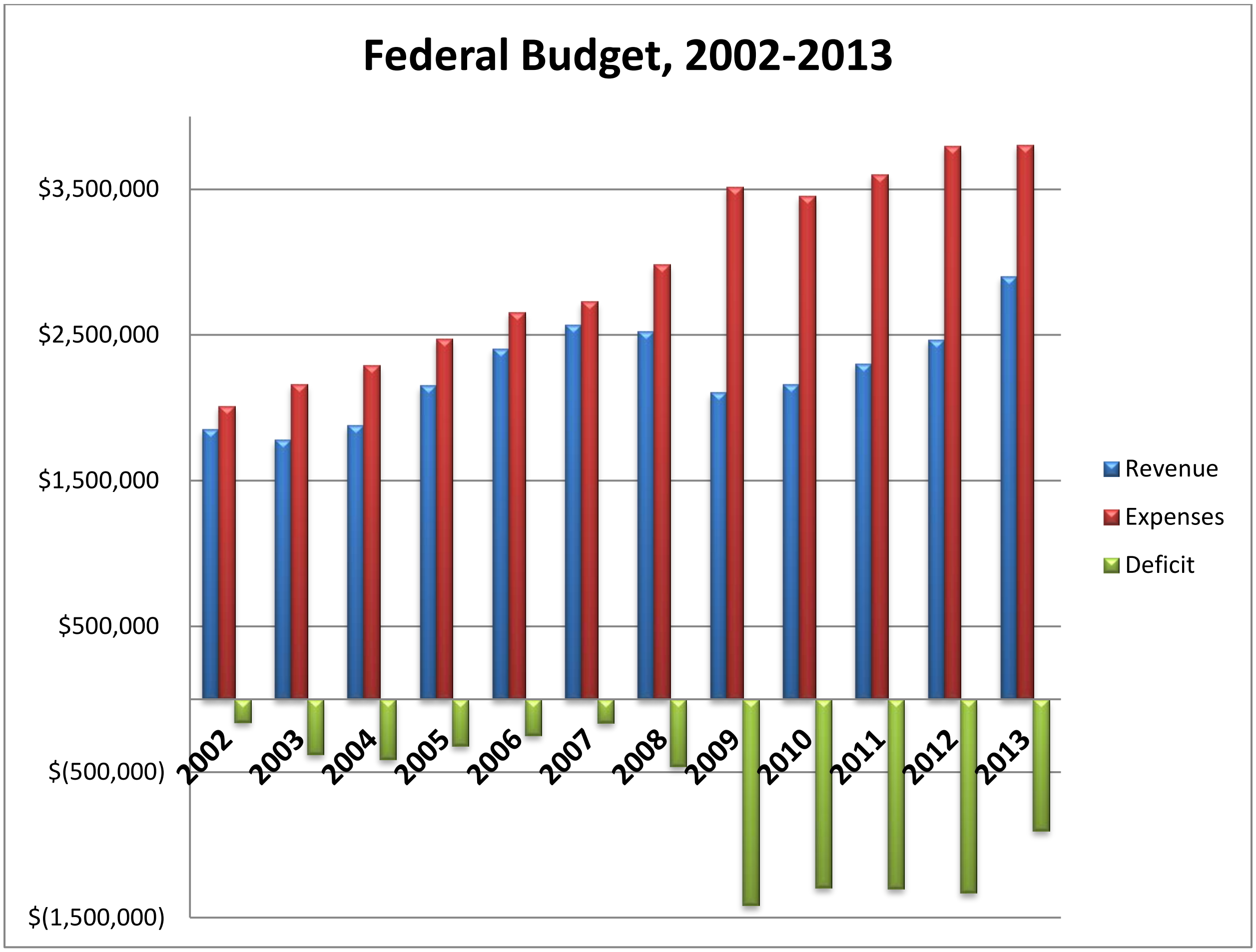
Picture 1—Depiction of Double Irish with a Dutch Sandwich



Besides the vast amounts of dissatisfaction with how people and businesses are being taxed on the federal level, most people are also taxed at the state and local level. California has the highest state income tax rate level with 13.3% (Tax Foundation) while some states like Florida, Tennessee, and Texas do not have state income taxes. Those states with no income taxes usually have higher excise and sales taxes, which are set by each individual state. Michigan is the only state in the US that had a form of the VAT in place called the "Single Business Tax" (or SBT), but it was repealed in 2006. On the corporate side of the state and local taxes, many corporations, like Amazon and eBay, constantly argue with states about paying sales tax for having a shipping facility in the state and not a physical storefront. Tennessee legislatures argued with Amazon about implementing the Tennessee sales tax of 9.25% on all purchases shipped to Tennessee since Amazon wanted to open up a shipping facility in Chattanooga and another one somewhere in middle Tennessee. Although Amazon did fight and threaten to build their facilities in another location, Governor Haslam argued that it would put retailers in Tennessee paying the sales tax at a disadvantage and finally swayed the online retailer. The case in Tennessee is one case of out many where online retailers are fighting to avoid taxes on their products, and Congress and the Supreme Court has yet to decide on the matter either way.

The dissatisfaction and negative view of the government continues to grow up itself. One of the many reasons that taxpayers do not want to pay taxes is because the government is wasting the money that the IRS collects. The IRS collected nearly $2.4 trillion in 2011, but the federal government's deficit is still growing. Since 2002, the federal government has had a deficit that continues to compound on itself with the government borrowing more and more money from other countries. The federal debt is at an all-time high of $16.9 trillion, and Congress had to rush to approve a $400 billion increase the debt ceiling at the end of 2012 so government programs could continue to run in 2013 (USDebtClock.Org). US debt is more than the combined external debt of all the countries in the European Union. In Chart 2 below, there is a comparison the revenues of the federal government, the spending, and the resulting deficit.

Chart 2—Federal Revenue and Spending for 2002 to 2013



All numbers in the chart above are in millions of dollars.

For 2013, most of the federal budget goes to increasing social welfare of the public. Welfare (11% of budget), education (6% of the budget), healthcare (24% of the budget), and pensions (24% of the budget) make up the majority of the government's spending with a total of 62% of the budget (Chantrill). The other big expense is defense, which is 23% of the budget, and the US government uses 6% of the budget on interest from the debt that it already has accrued, which is ridiculous (Chantrill). Even though the federal government knows that it has a huge debt, it continues to increase the budget every year while the receipts from taxes and the various other sorts of income can't compete with the growing budget. A growing part of the budget is the increasing demands of social security. With 76 million baby boomers and the increased longevity of the retired, Social Security faces a larger bill than they have ever seen. The revenue coming from those working and paying for social security cannot match the outflow of social security being paid to the retired, especially since there is an $113,700 cap on the earnings that social security can tax. Another problem of the increasing budget is that health programs, like Medicare and Medicaid, are high-risk programs, meaning that they are very susceptible to fraud, waste, and abuse. Even though these programs are known to be susceptible to these abuses, Congress has not done anything to put in preventative measures. The spending and expenses of the federal government exasperates many of the public, who feel like the government is going to lead the nation into a crisis like Greece and Spain who both are recovering from the excessive expenditures of its government. While one of the aims of a tax system is to increase the social welfare of all its citizens, the question has to be asked if throwing more money at the problem is going to be the solution in the case of Social Security, Medicare, and Medicaid. Obviously the US is not at the brink of disaster at the moment, but the trend of spending billions more than it has needs to stop in order for the US to reduce its debt and recover its economy.

In addition to the public discontent with the spending habits of the national government, the public also is suspicious of the IRS with all of the recent scandals surrounding the governmental entity. One of the recent scandals was the delayed process of approving tax-exempt status for Tea Party groups while the applications of progressive group were being approved in the same time period. Tea Party groups applying for tax-exempt status were asked to disclose a number of contracts and engagements that they wished to engage in the future. During the investigation of the Tea Party –IRS scandal, the IRS admitted that it made mistakes on how it screened conservative candidates and mentioned that liberal groups were on a special lookout list. Amid all of the investigations, acting IRS Commissioner Steven Miller resigned from his post. With all of the extra scrutiny the IRS faces, the abuse of the tax-exempt status at the hands numerous politicians using the foundations they run for their own political purposes and churches crossing political lines have been uncovered. Even though the IRS had uncovered the political tendencies of the churches and foundations operated by politicians, the IRS would not strip them of their tax-exempt status nor could they enforce the regulations on those non-profits. Besides the growing partisanship of the non-profit world, the partisanship at the IRS worries everyone since the IRS is supposed to be a non-partial government entity providing service to all taxpayers regardless of political affiliation. The prejudice in the IRS has the public wary of the entity that is supposed to collect their revenue, and this wariness is extent to the federal government, which is in charge of spending taxpayer's dollars for the good of the nation.

Congress has tried to reform the tax system. One change that they have tried to enact in the past is a patch on the AMT, which an alternative tax used to exclude some of the deductions and exemptions for upper income individuals. The AMT was first enacted in the 1969, and only affected a miniscule portion of the populations. However, the AMT was not indexed for inflations, and it grew to encompass more and more of the population. Since its inception in 1969, Congress has had to pass 19 patches on the AMT, so middle income individuals were not paying more in taxes than they could afford. Part of the problem with the AMT is that the patches are just temporary fixes, and the original amounts are from the 1990s, which is part of the reason why the tax code is so complex and vast. Nothing gets thrown out of the tax code, Congress just continued to add temporary fixes to it until the American Taxpayer Relief Act, which was passed on January 2, 2013.With the new tax act pass, the AMT exemption and threshold is higher and is indexed for inflation. Yay, Congress fixed the AMT from affecting nearly 27 million more taxes than their tax liabilities should be! Wrong. Even though, Congress fixed the AMT exemption and threshold, Congress did not take into account the new Obamacare taxes. The new law imposed a 3.8% tax on investment income for individual filers with income above $200,000 and married filers with income above $250,000 (Williams).This additional 3.8% tax on investment income is not included in the tax liability when calculating whether an individual owes AMT or not. If it was included in the regular tax liability, many high-income taxpayers would be excluded from paying the alternative tax. Another problem for the AMT is that the nation is constantly growing, so 3 or 4 million “middle-class” individuals, most of whom have children (the AMT doesn’t let filers take exemptions for children), will start paying the AMT as their income grows (Williams). “TPC estimates that the number of AMT taxpayers will jump 35% by 2018” (Williams).

Besides Obamacare affecting the AMT, it also has begun to affect the way investors invest. The American Taxpayer Relief Act (or ATRA) increased the top marginal tax rate from 35% to 39.6%, the capital gains rate from 15% to 20% for high income filers (see Table 7 for capital gains rates), and increased the estate tax from 35% to 40% for all amounts over the $5.25 million for single individuals or $10.5 million for couples (Sullivan). Looking at Table 7 below,

Table 7—Capital Gains Tax Rate for 2013

Capital Gains Tax Rate:	**0%**	**15%**	**20%**
Income Bracket:	10% to 15% Bracket	25% to 35% Bracket	39.6% Bracket

the top income bracket is now being charged 20% tax rate for their capital gains, but they also have to pay the 3.8% Obamacare tax on investment income on top of that 20%. So the top tax bracket is will be paying 23.8% on their investment income, and the Obamacare tax on investment income will also affect married filing jointly and head of household filers in the 28% bracket and single filers in the 33% income bracket. So those filers will have a new capital gains tax of 18.8%. Capital gains tax rates are not the only investment income being increased; Obamacare affects all investment income, which includes short-term gains and non-qualified dividends as well. Short-term capital gains are taxed at the regular tax rates, which have increased from 35% go 39.6% + 3.8% for a total of 43.4% on short-term capital gains for the top income bracket. These new higher capital gains tax rates are affecting the way that investors are investing their money and picking their investments for their portfolio. However the increased tax rates should not the focus when looking at investments, because they may not necessarily make a gain on the sale or they may make a large gain that they may not have made otherwise if they had just been thinking about the tax consequences. But because many investors don't want to pay extra taxes, they may be choosing investments like municipal bonds, which have low yield rates ranging from 0.75% to 1.74% (Sullivan). With this low yield bonds, the investor runs the risk of losing principal on the investment. Other investments, like master limited partnerships, pay income to the owner, which is considered a return of principal and not taxed; and these are great investments for older people who need the income but not so much for younger people. Hedge funds are also losing popularity, because most hedge funds require the sale of stocks and other investments that are held for less than a year, which makes it a short-term capital gain taxed at regular income tax rates.

Besides scaring investors with the tax consequences of their investments, the estate tax has increased from 35% to 40% for any amount over $5.25 million for single filers and $10.5 million for married couples. Part of the ATRA also increased the gift tax exemption amount, however many people believe that the exempt amount for both the estate tax and the gift tax would expire since Congress took right up to the expiration date of Bush Era tax cuts to pass the ATRA. Since they believed that both exemptions amounts would expire and not increase, they rushed to beat the system at the end of the year. Although certain exemption amounts were increased, President Obama is now proposing that there be a limit on how much “a person could put into a retirement account on a tax-deferred basis” (Sullivan). The maximum amount that the new proposed budget would allow is an annuity paying $205,000 a year, or a balance of $3.4 million for an individual at age 62. Of course that limit seems high but that puts a huge cap on the amount of money that younger people can save. For example, a 31 year old with $1 million in his or her retirement account with a 4% yield would hit the limit, as well as a 33 year old with $500,000 in his or her retirement accounts with a 6% yield (Sullivan). 11.3% of accounts would be affected if the current interest rate of 4% held truth (Sullivan). Plus if defined-benefit plans are included in this proposal, the number of individuals affected by this proposal would bump up again. If this new limit was passed, it deters investors from saving for retirement, not because $205,000 isn’t enough to live on but because it sends the wrong message about retirement. The government should be encouraging everyone is can to save for retirement, because elderly poverty is at an all-time high. Not to mention the fact that social security is costing more and more to fund, and it may not be able to survive in its current form. The government is also sending the same sign about investments when it increases the both long term and short term capital gains tax rates, because it is deterring people from investing. And investing is good for the economy as a whole, because it gives money to companies that need the financial capital in order for them to grow and produce jobs.

All of these examples of Congress's legislation just show that Congress hasn't fully thought about all of the repercussions from the tax legislations that they pass. Members of Congress obviously do not have backgrounds in taxation, so to ask them to make laws taxing the public seems like an unwise choice on the part of the American public. In addition to the fact that members of Congress are not well-versed in matters of tax, they also are not in the best position to be creating the tax laws and tax systems, because they are in public offices, which come up for re-election every 2 or 6 years depending upon on if they are in the House or the Senate. Another reason why Congress shouldn't be making tax law is because they are the ones who authorize the spending and the budget for the government. In a government based on checks and balances, it doesn't really seem wise for only one branch of the government to be in charge of making the cash and spending it as well, because Congress seems to want to have more money to spend so they'll increase the rate, which is not necessarily the answer to the problem. There needs to be more of a cost benefit analysis report that is passed around in Congress. Because while it's great that they want to improve the social welfare of the poor and elderly, taxing the rich and corporations at higher tax rates is not the solution to the nation's debt problem. That became obvious when many corporations incorporated outside the US to avoid paying US taxes, and the wealthy could just move elsewhere as well. One solution to improve the tax system and the overall US economy in general is for Congress to actually listen to what the IRS and the GAO (Government Accountability Office) have to say in matter regarding tax issues and program efficiency, respectively. If Congress did that, it could improve some of the programs, like Medicare and Medicaid, so the government is not throwing money away to people who do not truly need it. All in all to help the receipts match the expenses, the government should reduce some of its expenses, like not hiring independent contractors when they have employees that can do the same job or not having several different programs do the same thing. There are many ways that the government could reduce the $3.8 trillion that they spend.

Another problem stated in this paper is that the tax code is too complex. 85% of Americans believe this idea that the tax code is too complex. This fact is supported by the fact that Congress can't find a solution to the tangle the tax code has become. The fact that Congress has to pass so much legislation in recent years dealing with issue of taxes means that the current tax system is not working. That leads to the question of what can the US federal government do to improve the current tax system? One of the main things is that the tax system needs to complete overhaul the tax system, because it's a little ridiculous that the IRC goes back to 60 years ago and nothing has been deleted or crossed out from it. The terminology and length of the IRC definitely detracts a lot of individuals from trying to understand taxes and understand their own tax liability. An example of how outdated the tax code is how until recently the AMT would have reverted back to the exemption amounts dated back to the 1990s. So just re-writing the tax code in common terminology today would help a lot with the understanding of taxes. More support for the cleaning up of the tax code is because it would eliminate some of the loopholes in the code itself. As seen earlier in the paper, the IRS has lost $3.09 trillion to tax evasion in the past 10 years. 85% of tax evasion cases are committed by individuals, but only a few individuals are caught and charged with it. In addition to individuals evading tax, large multinational corporations, like Apple, Google, and Microsoft, are avoiding paying billions of dollars in taxes for profits made in the US by using these loopholes. If the tax code were to be cleaned up, there would be less room for error, evasion, and less work for the IRS to do. By cleaning up the tax code, the IRS and other tax experts should not eliminate deductions and other credits completely but scrutinize each item closely. By analyzing each tax item in the IRC, the IRS and other tax officials could do a cost-benefit analysis of the cost of the tax item and the respecting benefits of the tax item. An example of this could be the way the US decides to tax based on citizenship and not on residency like most other nations. The US taxes citizens on the world wide income, meaning income made from all over the world, even if the citizen is not in the US. Of course the citizen isn't quite paying double taxes, because the US does give a foreign tax credit, which reduces the amount of worldwide income they tax. However, it seems silly for US citizens to pay the US government for income that is already being taxed by the country, which they are living in, because they are not receiving any of the benefits that the federal government performs for residents.

In addition to simplifying the code, the corporate tax portion of the IRC should be made more competitive. The market is a global market that is getting more and more interconnected every single day, and multinational companies, like Google, Microsoft, and Apple are taking advantage of that fact. If the US lowered tax rates so they were more on par with other developed nations, then more corporations would probably incorporate in the US. Another reason why the US should lower tax rates and reduce the number of loopholes that corporations have is because it would broaden the tax base of US corporations paying taxes. Corporations should bear a bigger tax burden than the 10.1% that it did in 2011, because they do make so much money. Like stated earlier for individuals, the US should also tax corporations based on residency, or something like nexus (which is what state and local governments use to determine if companies are taxed in their states or cities), not based on where the company is incorporated in. It should also simplify the sourcing rules, because they are very complicated and usually allow the company to understate the amount of income that they have in the US. That way more income earned and spent in the US stays in the US to help the citizens.

Some more specific tax ideals that the US government should enact may be a model like Hong Kong's tax system. In Hong Kong, the individual filer chooses either to use a complicated tax system like the US's tax system or pay a simple flat tax. However Hong Kong does have the multitude of deductions and credits, like the US does, but it does have deductions for charitable contributions, mortgage interest expense, etc. This choice between the two options streamlines the process for Hong Kong's tax department, and it is further simplified by the fact employees take care of all taxes on the salary while business take care of all taxes on business profits. That aspect of Hong Kong's tax system is much different than America's since part of employee wages are withheld from the paycheck by the employers and sent to the government. It also has a flat tax of 16.5% on corporation profits, which is much lower than the 35% that the US has. Most corporations in Hong Kong pay this low flat tax and are attracted to Hong Kong, because the simplistic nature of the tax system and the freedom from government interference allows for growth and investment by the companies. More growth is stimulated by the fact companies pay a profit taxes before distributing dividends, and individuals are not taxed again on capital gains. Another tax system similar to Hong Kong's is Singapore's, which has a flat tax for corporations as well. It also has a progressive income tax system for individuals with rates starting at 2% and topping out at 20%. Also like Hong Kong, Singapore does not tax on an individual's capital gains. Both Hong Kong and Singapore have has success with their tax system, and both systems are relatively easy to implement in the US if the government wanted to implement them.

Besides looking at other countries, the government should also be looking at other forms of taxes as a solution to boost revenues. For instances, many European nations have implemented the VAT (Value-Added Tax), in hopes of generating revenues like the corporate income tax and the personal income tax. The VAT is more effective than sales tax, because it gives the sellers a direct financial stake in collected the tax from the buyer and eliminates the decision of whether the buyer is the end consumer or not. And since the tax is spread out from the beginning producer to the end buyer, the buyer does not have as much of an urge to shop on the internet to evade the tax, because their portion of the tax is not big at all. Whereas if sales tax was implemented on the good or service, then the sales tax, which can be as high as 10%, is the sole burden of the taxpayer and it is felt more heavily by them. Some examples of countries using the VAT are Bangladesh, China, and the European Union. Since Bangladesh begin using the VAT instead of the sales tax and excise duties, it has become the government's largest source of income at over 50% of the government's income. China's VAT encompasses 33.9% of China's total tax revenue. The VAT seems like a good idea for the government to begin using; however there are a few problems that could possibly arise. One problem that will arise is that states are currently in charge of administrating the sales tax for each individual state and receiving that income. So the problem is who implements the VAT and who receives the revenues? The US obviously cannot have both a sales tax and a VAT; so if the sales tax was to go, where would the states get their main source of funding? Or could they split the revenue? The federal government could implement a nationwide VAT rate, and states could take the original percentage of sales tax that they implemented and give the federal government the remainder of the tax. An example of this would be the IRS implementing a 15% VAT everywhere, and in Tennessee, where the sales tax was originally 9.25%, Tennessee would take 9.25% of the VAT and the government would receive 5.75% remainder. Receiving income from the VAT would definitely boost revenues for the federal government, since they do not receive income from the sales taxes in the states. Many other factors play a role in the decision of whether the US should implement a VAT or not, but it is a viable option of raising revenue for the government.

The tax system in the US is a pretty productive system that generates a fair amount of revenue from the resources and people it has. However it seems that the tax revenue potential of the US has been passed due to too much complexity in the system, high tax rates for both businesses and people, and a public aversion for paying into a costly bureaucracy. In order for the IRS to achieve maximum returns, it should increase the assistance and education provided to the public to enlighten them of the purpose of taxes and their tax responsibilities. Congress should simplify the tax code, so that more people understand it and less people can find loopholes in it. Together both the IRS and Congress should aim to find a tax system that is more progressive and fair the public, because no one is happy with it right now. They should endeavor to lower tax rates for both businesses and people, because the tax base of the government will increase and less people will try to evade taxes. More companies will also come back to the US since the tax rate isn't so high and there is room for growth. Another idea to stimulate growth is to reduce the capital gain tax rate, so more people invest in the market. If the government could take a few of these suggestions and implement them for the government, then the US would be in a better fiscal position. Regardless of whether they take similar measures to the ones laid out in the paper, the federal government really does need to reduce its expenditures in order to reduce its debt and do something about the tax system. The current system will continue to take more and more work to fix, because the environment is constantly changing and the tax code needs to be update to reflect that in order to capture the maximum revenue possible for the good of society.

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