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Our 'Voluntary' Tax Code

By Donald L. Luskin

Should we stop worrying and learn to love the "mother of all tax reform plans" put forward by House Ways and Means Committee Chairman Charles Rangel of New York?

The bill would raise taxes by $3.5 trillion over the coming decade, according to Louisiana Republican Rep. James McCrery, a committee colleague of Mr. Rangel's, making it the largest tax increase in history. There has been so much concern that such a tax increase would hurt financial incentives that drive economic growth that House Speaker Nancy Pelosi distanced herself from Mr. Rangel's plan almost as soon as he announced it.

But fear not. As Mr. Rangel wrote on this page two weeks ago, his bill would "restore a sense of equity and fairness that is critical to the success of our voluntary tax system." That's right, he called our tax system "voluntary." That means we don't have to worry about the incentive effects, since we won't actually have to pay any of that $3.5 trillion -- unless we want to.

So when April 15 comes around, I encourage you to be like Herman Melville's Bartleby and say: "I prefer not to." But wait. By April 15 you'll already have paid, since taxes are involuntarily withheld from your paycheck. Nothing can be done about that, even if you don't volunteer to file a tax return. And if you don't file a return, you'll find yourself involuntarily in jail.

You'll then have to yield to the opinion that Mr. Rangel wasn't being entirely straightforward in writing that our tax system is voluntary. But then, he wasn't being entirely straightforward in writing that his bill, which would further raise taxes on the "rich" who already pay the great majority of federal taxes, has anything to do with equity and fairness.

Perhaps from Mr. Rangel's perspective, our tax system is indeed voluntary. After all, he chooses who pays taxes, how much they pay and how their money gets spent. If he wants to raise our taxes to support a $2 million earmark to create a Charles B. Rangel Center for Public Service at the City College of New York, he can volunteer to do that -- but the rest of us have no such choice.

To be fair, our tax system is indeed voluntary in certain respects. For example, wealthy liberals like Warren Buffett, who call publicly for higher taxes on the rich in the name of fairness, can volunteer to pay more themselves any time they wish to do so. All Mr. Buffett has to do is send a check to Department G -- that's G for "gift" -- at the Bureau of the Public Debt in Parkersburg, W.Va.

Why not try an experiment in which the tax system is made truly voluntary? Already 42 states (as well as the District of Columbia and Puerto Rico) raise revenues with lotteries, through which citizens voluntarily paid $57 billion last year. It's a long and noble tradition. Before the birth of Christ, the Han Dynasty ran lotteries to raise the revenues used to build the Great Wall of China.

Government could be entirely financed by voluntary taxation. Yes, the government would have to be small enough to make do, and citizens would have to be sufficiently public-minded about it. But all 13 original American colonies ran lotteries, and playing them was considered a civic duty. Proceeds from lotteries established Harvard, Yale, Columbia, Dartmouth, Princeton, and William and Mary -- and paid for the cannons that defeated England in the Revolutionary War.

But today, Mr. Rangel might find that the volunteerism in today's tax system is a dangerous thing. His bill would raise the tax rate on capital gains income, but the cap-gains tax is voluntary to the extent that one doesn't have to pay it until one chooses to sell an appreciated asset. That fact is not lost on Mr. Buffett, who believes the rich should pay more taxes, but who has never volunteered to sell even one share of his vast holdings in Berkshire Hathaway -- and thus has never volunteered to pay any cap-gains taxes.

What if every investor did that? It's nice to imagine a nation of long-term investors just like Mr. Buffett. But if stockholders never sold any of their investments, the economy, incomes and job creation would slow to a crawl because a growing economy depends on capital moving freely and continuously to its perceived highest and best use.

Mr. Rangel should also bear in mind that taxes on labor income are voluntary in the sense that one can choose not to pay them by choosing not to earn any labor income -- that is, by not working. All the rich need to do in order to make true Mr. Rangel's characterization of our tax system is to retire to their yachts, rather than continue to contribute to the economy by running hedge funds or doing private equity deals.

When that happens, Mr. Rangel will get a lesson in supply-side economics he'll never forget. Some say that the Laffer Curve is wrong, and that tax cuts don't result in higher tax revenues. But when America's most productive workers stop working -- even a little bit -- in reaction to the incentive effects of the "mother of all tax reform plans," they'll see that the Laffer Curve was right after all, and that it can cut both ways. Involuntary tax hikes result in voluntarily lower tax revenues.

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