



## America's Low Taxes in Comparative Perspective

**Andrea Louise Campbell**, Massachusetts Institute of Technology

The most important debates in U.S. politics concern the size and role of government, as the polarized parties offer contrasting paths forward. Republicans urge holding the line on taxes and limiting domestic expenditures. Democrats aim to preserve government functions and make some new investments – and call for tax increases to support these choices. As citizens and analysts weigh these options, it helps to put U.S. fiscal policy in cross-national perspective. Compared with other developed countries, the United States has very low taxes, does little to fight inequality, and has an extraordinarily complex tax code that undermines faith in the system.

### Low Taxes and Unstable Revenues

Almost no peer nation has taxes as low as the United States:

- In 2009, the United States had the third lowest ratio of taxes to domestic product of the 34 advanced democracies in the Organization for Economic Cooperation and Development.
- Prior to the fiscal crisis, in 2006, total U.S. taxes at all levels of government – federal, state, and local – were 28 percent of gross domestic product, just three-quarters of the percent in Germany and the United Kingdom and about half that of Denmark and Sweden. Among rich democracies, only South Korea had lower taxes than the United States.

America's paltry tax take is attributable to low effective rates, and also to the absence of types of taxes that are important elsewhere. Personal income taxes at all levels of government are slightly higher in the United States. But U.S. corporate taxes and social insurance levies bring in relatively low revenue, and the United States does not have a value-added tax – a type of national sales tax that produces ample, steady revenues in other countries. U.S. taxes are also undependable. During the recent global financial crisis, for example, U.S. tax revenues fell by one-fifth from the 2000 level, compared to a five percent decline across peer nations.

### America Does Little to Promote Equality

U.S. income inequality has grown tremendously in recent decades. The share of income going to the top one percent of earners rose from nine percent in 1970 to nearly 24 percent in 2007, and wealth is even more top-heavy. As plutocrats have prospered, other Americans have faltered. Between 1979 and 2007, before-tax incomes increased by 240 percent for the top one percent, but grew just twenty percent for the middle fifth and ten percent for the bottom.

Do taxes make America more equal? On the surface, U.S. tax policies seem “progressive,” as scholars put it, because the graduated income tax asks a bit more of higher-income earners. But overall, the U.S. government's patterns of taxation and spending do little to mitigate inequalities in market-generated incomes, for several important reasons:

- Although both the individual and corporate tax systems impose higher rates on the top slices of income, the top rates were ratcheted down under President Ronald Reagan and again under President George W. Bush.
- The effective tax bite is reduced by lots of tax breaks built into the system and steadily expanded in recent years. Business and higher-income earners benefit the most.
- Lower income groups face a higher burden from many important U.S. taxes – including the Social Security and Medicare payroll taxes, and the income and sales taxes collected by many states.

When all the taxes are added up, the American tax system is essentially flat – that is, the share of taxes paid by each income group resembles the share of income it receives. In 2011, the lowest fifth of earners received 3.4 percent of total income and paid 2.1 percent of total taxes, the middle fifth received 11.4 percent of income and paid 10.3 percent of taxes, and the top one percent received 21 percent of income and paid 21.6 percent of taxes.

Other advanced nations also take a lot in taxes from low-income households. But European countries also use generous social programs to give extra help to middle and low-income earners. In the United States, this happens only for older citizens on Social Security and Medicare.

### Extraordinary Complexity

The U.S. tax code is also extraordinarily complex, even if we just consider federal taxes alone. Numerous exclusions, deductions and credits add to the length of tax returns and the time needed for completion. Taxing families rather than individuals requires complex calculations, and so does the Alternative Minimum Tax, which forces taxpayers to calculate their tax liability twice, once under the regular income tax and then again under the AMT, and pay whichever is higher.

U.S. survey respondents say that complexity bothers them more than the actual amount they pay. And an opaque, loophole-ridden tax system leads to bitter political conflicts over who pays how much. Many countries make tax compliance easier. Some don't require most to file returns, because individuals rather than families are taxed with withholding from both wages and interest. Credits and deductions may also be equal, not tilted toward the rich as in the United States.

### The Downside of Low Taxes

No one likes to pay taxes, and taxes that are too high can strangle economic growth. But so can taxes that are too low – the threat the United States now faces. U.S. revenues have remained flat, even as the population ages and economic needs grow. Squeezing investments in education, research, and economic infrastructure erodes the bases of future productivity. America spends just 1.7 percent of GDP on transportation infrastructure, for example, compared to 4 percent in Canada, 5 percent in Europe, and 9 percent in China. A recent commission found that U.S. transportation spending is less than half of what is needed to keep systems in good repair and make improvements vital to meet international competition. The story is the same for other economically crucial areas. Low taxes may seem like a good idea – but, over time, they can prove increasingly costly to businesses, families, and the United States as a whole.

**Read more in Andrea Louise Campbell, “[America the Undertaxed: U.S. Fiscal Policy in Perspective](#),” *Foreign Affairs* 91, no. 5 (September/October 2012): 99-112.**