

## Original Article

# A Critical Study on Defects in American Taxation System

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**Abstract:**

The word tax is derived from Latin word "taxare", which means to access or to predict and this concept has led to the evolution of assessment in taxation as it involves the estimation of amount of money assessee or an individual way to the government and to the respective tax jurisdictions. Tax is the core component of any economy; it is a major source of income which leads to revenue generation and development of the economy but in the recent times the tax is also affected by inflation stagflation an incorrect apportionment of taxes two different classes of the economy. there are 52 States in USA where most of the states have been facing lot of taxation issues. States such as New York, New Jersey, Pennsylvania, California, Colorado, Texas etc. have been facing lot of taxation issues in the recent times. such defects and problems require a proper solution and unique approach to ensure smooth flow of tax implementation in the economy. in this paper we are going to figure out the various defects on the loopholes that are present in the American taxation system how effectively are the taxation laws been enacted and implemented to the US citizens of different income classes.

**Keywords:** Tax codes, tax policies, inflation rates, multifaceted approach, administrative phases.

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**INTRODUCTION:**

A well-structured taxation system is the cornerstone of a nation's economic stability and development. Taxes are compulsory financial charges levied by governments on individuals and businesses to fund public goods and services, including infrastructure, education, healthcare, and defense. The effectiveness and fairness of a taxation system significantly impact a country's social and economic fabric. A robust taxation system is characterized by simplicity, equity, efficiency, and transparency. Simplicity ensures that tax laws are easily understandable and manageable, reducing the compliance burden on taxpayers.

Equity in taxation aims to distribute the tax burden fairly across different income groups, typically through progressive tax structures where higher earners pay a larger percentage of their income. Efficiency relates to the system's ability to collect taxes without causing significant economic distortions or administrative costs. Transparency is vital for maintaining public trust, requiring clear communication of tax rules and the rationale behind tax policies. However, many taxation systems face challenges such as evasion, loopholes, and administrative inefficiencies. These issues can erode public confidence and reduce revenue collection,

undermining the government's ability to provide essential services. Reforms focused on simplifying tax codes, closing loopholes, enhancing enforcement, and leveraging technology for administration can address these defects.

The United States taxation system encompasses a variety of taxes levied at the federal, state, and local levels. These taxes fund government operations and services, including infrastructure, education, healthcare, and national defense. Below is an overview of the main types of taxes in the U.S.

Federal Tax, state taxes, Local taxes, and other taxes. the federal taxes include individual income tax which is the largest source of revenue for the economy it ranges from 10% to 37% based on the income brackets it also include certain deductions and exemptions which help to reduce the taxable income an ultimately give the IT returns to the citizens or the taxpayers. it also includes corporate income tax which is obtained from the organizations and its rate is 21% it also includes certain deductions and exemptions, then there is also payroll taxes and capital gain tax in payroll taxes both the employers and employees contribute towards the taxes it includes social security tax rate which is 6.2 % auto certain limit and Medicare tax rate at 1.45 % but no income limit.

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where is capital gains tax is applied when the sale of any asset, stocks, real estate bonds etc. it also includes short term capital gains tax and long-term capital gains tax the short-term capital gains tax are taxed a minimal rate whereas long term capital gains tax have lower tax rates up to 20% depending on the income. it also includes gift taxes and other excise taxes. the state taxes include state income tax which is levied by most of the states in United States apart from Florida & Texas. it also includes sales tax property tax where are the property tax has many jurisdictions such as city, county & school. the local taxes include property tax sales tax & income tax. The Other types of taxes are inheritance tax sales and use tax luxury taxes and sin taxes (those taxes which are levied on alcohols cigarettes).

#### **OBJECTIVES OF THE STUDY:**

- To study the loopholes in American taxation system.
- To study how effectively the tax laws in US are implemented.

#### **RESEARCH METHODOLOGY:**

##### **Sources of Data:**

The data has been collected from 2 main resources:

- **Primary source:** The primary data is collected from tax officers, tax associates, auditors, financial analyst.
- **Secondary source:** The secondary data has been taken from blogs, internet websites, articles & research journals.

#### **DATA ANALYSIS & INTERPRETATION**

##### **Objective-1:**

To Study The Loopholes In American Taxation System.

##### **1. Taxpayers Perception:**

According to a study made by internal revenue service in the year 2021 reveals that the reports state 94% of the Americans perceive that each and every civilian of the country should pay their share of charges in terms of taxes, whereas majority of the Americans state that IRS differs from age level, tax levy rates etc. and they also believe that the execution of IRS has declined over a period of time. although most of the US citizens recognize the tax framework and the level of tax collection in the

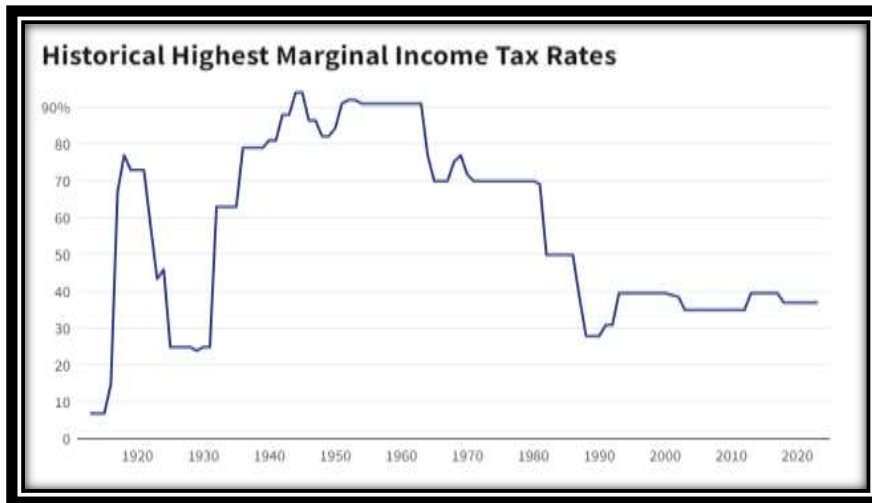
country, they also recognize the tax rate within the system. and the citizens also state that if the rules and regulations of the IRS are executed in a structural manner when the US citizens utilize the tax specifications to the fullest, but in this case US government is playing a back-end game and not executing the rules and regulations of IRS proper manner. ultimately the blend of all these situations has changed the perception of US taxpayers.

##### **2. Joe Biden attempts tax changes:**

When Joe Biden got elected as the president of US the inflation reduction act (IRA) came into existence in the year 2022. according to the IRA act the large Corporates how to pay 15% of taxes on their profit. and the IRA also aimed at reducing the deficit decrease the inflation country, this act made a mandate to all the large corporations to pay taxes where most of the organization's forward the concept of tax avoidance. on the other hand, along with Joe Biden the treasury secretary Janet Yellen instructed that the legislation should not increase the tax rates for families whose income is below \$400,000, but later on as a legislation was passed it was dropped out by the senate parliament in the country. and the IRS act was also tried to be imposed corporations other than the large organization's because the mid-sized organizations were also in the platter of tax avoidance, henceforth the attempt to changes in taxes by the president leaders wasn't successful.

##### **3. Inequity in the distribution of tax burden:**

According to the perception of the US citizens all the taxpayers most of the higher-level income are taxed with higher rates, but in the current scenario the tax burden is not equally distributed among the different income level individuals and various businesses especially the large corporations. according to some latest reports most of the major organizations haven't paid taxes according to their income levels. even the reports reveal that ex-president Donald Trump hasn't paid more taxes for the income that he has earned throughout his tenure. most of the US citizens object that the tax rates are imposed inversely to various income classes i.e., the higher income class pay less taxes and are imposed less taxes, whereas the lower and the middle-income class are imposed higher tax rates simultaneously they pay more taxes when compared to higher income individuals and organizations.



#### 4. Higher benefits for higher tax brackets:

The next defect in American taxation system is that higher benefits are given for the higher tax brackets. as discussed in the earlier points has been in equity in distribution of taxes among various income classes. the ones who fall under the higher tax bracket will have more benefits an advantage when compared to other income class individuals. according to the US tax codes the marginal tax rates are increased on the taxable income henceforth the tax bracket income will increase and will impact the progressive tax system as well as the rates not only because of the marginal tax rate but there are certain other factors where the progressive taxes get impacted by exemptions, lower tax rates & deductions.

#### 5. Corporate Tax Avoidance:

Since 2018, the tax law generally applies a corporate income tax of 21%; however, many U.S. corporations pay far lower effective rates or no tax at all because of substantial business write-offs, carrybacks and carryforwards of losses, aggressive tax planning and, if audited, tenacious and lengthy negotiating. Even as some challenge the existence of any corporate tax regime, others debate the appropriateness and level of corporate tax benefits, particularly those enjoyed by politically influential industries.

#### Objective – 2:

To Study How Effectively The Tax Laws In Us Are Implemented.

In this objective we will get to know and understand how effectively the tax laws are implemented in United States of America. according to the latest reports released by the internal revenue service state that for more than a decade the tax system has fail to meet the Expectations year by year

and has not satisfied the US citizens in terms of tax payments. the satisfaction of the taxpayer will depend on the amount of taxes paid by them about the year even the government has also been utilizing those taxes to frame a structural budget for the economy. In terms of the lower class and the middle-class tax payers they execute E-Filing of taxes which includes the earnings an investments data in the filing forms, and these e-filings are audited thoroughly and strictly throughout the year and when their information provided in forms and returns then the tax structure & returns are levied in a proper manner to the tax paying individuals.

In addition, between 2010 to 2019, the audit rates for tax payers have been declined though the rates for lower income class were less when compared to higher income classes. during the tenure returns which amounted to \$5 million to \$10 million has been decreased to 81% whereas the number of returns filed were 92%. The returns which amounted to more than \$10 million has been declined to 66% where is the number of Returns 84%. from this data we can observe that there has been substantially decline of 11% in \$5 million to \$10 million bracket whereas there has been a huge dip of 18% in excess of \$10 million bracket. according to the study from the experts the Treasury Department revealed that for every \$1 of additional investment in the IRS gives the output of \$11 in tax collections which is significantly higher in terms of ratio. With the growing tax gap the Biden government propose that an additional allocation of \$80 billion IRS this would lead to an increase in IRS funding and will result in generating revenue of \$204 billion till the year 2031. Various reforms, tax complexity and compliance, enforcement of IRS & voluntary compliance has led to effective implementation of tax laws in the United States.



**CONCLUSION:**

The labyrinthine conglomeration of the defects/loopholes of American taxation system put forth both challenges and opportunities. we have seen many reasons for the loopholes of American taxation system and we have also observed how effectively the tax laws have been implemented in the US. there should be a fair correct allocation the various income level classes and there should be a scrupulous audit of the tax that is paid the government by the taxpayers. these loopholes are not about creating more gaps but they can also be engulfed by restructuring the tax system and various laws that needs to be enacted and implemented. the government can also lead to more commitment towards the principles of the taxation and strictly abide to all the mandates and provide a fair tax structure to the citizens of United States of America. This will lead to integrity, trust and compliance which will ramificate to a prosperous society.

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**Conflicts of interest**

There are no conflicts of interest.

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