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Will the VAT Lady Sing?

If so, it's over for America.

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A cultural battle is under way in America, a battle between, in columnist Michael Barone's, words, "the culture of dependence and the culture of independence."

The culture of dependence is the belief by American liberalism that government can make better decisions for people than people can make for themselves. The U.S. has now created the largest government spending increases, takeovers, and regulation expansion in the past 65 years, since the end of World War II. It is going to get even worse, as the President's budget plans to spend $45 trillion in the next 10 years, a 70% increase in spending over the last 10. Estimated tax revenues will only be $35 trillion--or maybe even less if the current economic difficulty lasts for a while. The Tax Foundation estimates that we would have to more than double current income tax rates for everyone to balance the 2010 budget, or increase the rates by 50% or more to balance the budgets over the next 10 years.

To put America's new spending policy into perspective, the Heritage Foundation's Brian Riedl reports that federal spending in the 1980s and 1990s remained flat--about $21,000 per household. During George W. Bush's administration, the figure rose to $25,000 per household, and President Obama's budget plans to spend $32,000 per household by 2019. And that number is before all the baby-boomers retire and another $10,000 or so in Social Security, Medicare and Medicaid costs will be spent in addition.

So the new, European America that we have become will need some serious new money to pay for all this spending. Doubling all personal income tax rates would be politically unlikely, and doubling the rates for the top 1% or 2% of taxpayers would not raise anywhere near enough.

So what to do? Reducing federal spending is the most sensible approach, but Congress is unlikely to do it. It is pretty easy to argue that this administration's necessary course will instead be to hike taxes, and not just higher income tax rates will be on the table. We recently saw the White House preference when economic adviser and former Federal Reserve chairman Paul Volker said, "If at the end of the day we need to raise taxes, we should raise taxes," suggesting what we should do is enact a value-added Tax, which he believes is "not as toxic an idea" as it once was.

The VAT is an invisible excise tax added to each phase of a product's production, really a national sales tax, with the cost of the total

VAT ultimately paid by the final purchaser, regardless of his income or wealth. A VAT would likely contain some exemptions--for food, clothing, medicine and housing costs--but it would impose taxes on most other daily purchases, gasoline, televisions, automobiles, computers, airfares, cell phones, refrigerators, newspapers and restaurant foods, for example.

The VAT has been in use in the European countries since the late 1960s, and has had a strong, negative economic influence. Before the European VATs were put into effect, the average EU tax burden was 28% of gross domestic product, compared with the 25% in the U.S. By 2006 with the VATs EU average tax burden was 40% compared with 28% in America.

Average European government spending was about 30% of GDP when the VATs were instituted in the late 1960s. Fast forward to today, and we see European government spending has grown more than 50% and now hits 47% of GDP. And European government debt in 2005 was 50% of GDP, compared with under 40% in America.

Perhaps most important, bigger government spending and higher taxes have radically reduced job growth in Europe. Between 1982 and 2007, Europe created fewer than 10 million new jobs, vs. 45 million in the U.S. Our economic growth was more then one-third faster.

The European Union now requires all member nations to have a minimum VAT of 15%--more or less the equivalent of Congress telling each of our 50 states how high their taxes must be. So has the VAT replaced some of the income tax in Europe? Absolutely not, nor has it reduced the income tax rates. The average VAT rate there is just under 20%, and the EU's top income tax rates average about 46%.

Nor will an American VAT likely replace income taxes here, so it would be a crushing cost addition to the Obama tax increases and on the cost of purchases by non-tax paying lower income people.

So is the VAT coming to America? Probably not before the next presidential election. The Senate voted last week 85-13 to approve a nonbinding resolution stating that the VAT "is a massive tax increase that will cripple families on fixed income and only further push back America's economic recovery." But if President Obama is re-elected, he will almost certainly propose it and press Congress to enact it over popular objections--just as he did with ObamaCare.

The income tax increases in 2011 and 2013 won't come close to paying for our greatly expanded government, so the middle class and lower income people must be taxed as well. Add the VAT to purchased goods, and the government would have money, lots of money, now and forever as the Europeans have shown us. It is estimated that a 1% VAT--with no exemptions--would raise about $1 trillion per decade. America would become European with a 15% or 20% VAT with a few exemptions thrown in.

What the VAT really does, as we have seen in Europe, is to do away with government spending controls. So if enacted by the Congress, higher taxes, bigger government, lower economic growth and fewer jobs will be the result, and all of us will soon be living in a new and much less successful America.