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I Like Ike: Bringing Back Eisenhower-Era Progressive Taxation

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Balancing the federal budget has suddenly become so urgent that even food programs for the poor are cut on the grounds that inadequate nutrition now is a lesser evil than the burden of government debt on these same children later. Despite the overblown rhetoric of the balanced-budget stampede, however, budget-slashers have kept one solution off-limits: tax increases for those who can afford them. Yet a return to the level of income tax progressivity of the 1950s, just for corporations and the 0.9 percent of taxpayers with adjusted gross incomes (AGI) of over $200,000, could increase annual federal revenues by as much as $180 billion and make it possible to preserve the safety net intact and to provide the myriad services and types of infrastructure that only a national government can.

The demand that the rich pay their fair share is hardly new. A poll conducted for the Advisory Commission on Intergovernmental Relations during the Reagan administration revealed that half of those questioned picked "make the upper-income taxpayers pay more" as the single most important way of making the tax system fairer.[1] Why, then, does Congress not raise taxes for those who can well-afford Eisenhower-era progressivity? Perhaps because the agenda of the rate-reducers is not so much budget-balancing as protecting the wealth of their economic patrons? Or perhaps because the majority in Congress want to increase the power of corporations by eliminating the countervailing restraints of government?

What can be learned from the golden days of post-World War II Republican normalcy — the period that right-wing congressman and presidential candidate Robert Dornan of California recently referred to as "the happy, innocent Eisenhower years"?[2] In 1954, the Korean War was over and the United States was the undisputed world power. With both houses of Congress under Republican control, President Dwight Eisenhower, seeking to reduce the federal deficit, explained in his budget message that an overhaul of the Internal Revenue Code was needed to "restore normal incentives for sustained production and economic growth."[3] Democrats responded that the Republicans as "the party of the bigshots [with] no sympathy for the laboring man"[4] had drafted a measure "loaded in favor of the wealthy."[5]

So what was the tax relief that the Republicans provided their wealthy constituents in 1954 that prompted Democrats to liken it to the "'trickle-down' theory of taxation of Alexander Hamilton and, more recently, Andrew Mellon"?[6] They rolled back the highest marginal tax rate all the way from 92 to 91 percent and maintained the corporate rate at 52 percent, postponing the reduction to 47 percent that the previous Democratic-controlled Congress had ordered.[7]

In 1954, the 0.3 percent of taxpayers reporting AGI in excess of $40,000 (the equivalent of $200,000 today)[8] accounted for 5 percent of AGI (including 100 percent of net long-term capital gains to make the tax base statistically more comparable to today's),[9] but paid 16 percent of all taxes.[10] In other words, this group's share of total taxes was 3.2 times greater than its share of total AGI. Of this "1954 income tax system" the Reagan administration observed that "most citizens probably thought it was reasonably fair."[11]

By 1993, the 0.9 percent of the taxpayers reporting $200,000 or more in AGI accounted for 13 percent of total AGI, but only 24 percent of all tax payments.[12]

[1]Advisory Commission on Intergovernmental Relations *Changing Public Attitudes on Governments and Taxes*, Tab. 7 at 13 (1983).

[2]Bob Hohler, "Dornan Enters Republican Race," *Boston Globe*, Apr. 14, 1995, at 8 (Lexis).

[3]100 *Cong. Rec.* 569 (1954).

[4]100 *Cong. Rec.* at 15,310 (remark of Rep. Long).

[5]100 *Cong. Rec.* at 12,536 (remark of Sen. Johnson, Col.).

[6]H. Rep. No. 1337, 83d Cong., 2d Sess., reprinted in 1954 *U.S. Code Cong. & Admin. News* 4017, 4595.

[7]Internal Revenue Code of 1954, ch. 736, sections 1(a), 11(b), 68A Stat. at 1, 5, 11.

[8]The consumer price index rose 5.37-fold between 1954 and 1993. Calculated according to U.S. Bureau of the Census, *Statistical Abstract of the United States: 1994*, tab. 746 at 487 (1994).

[9]Only 50 percent of net long-term capital gains were taxable and even included in AGI in 1954. Internal Revenue Code, sections 1201-1202, 68A Stat. at 320. The leading tax scholar of the period considered the preferential treatment of capital gains "probably . . . the main reason for the disparity between theoretical and actual rates of income taxation in the high-income brackets." Randolph Paul, "Erosion of the Tax Base and Rate Structure," in Joint Committee on the Economic Report, *Federal Tax Policy for Economic Growth and Stability*, 84th Cong., 1st Sess. 297, 302 (1955). For calculations of effective tax rates for the early 1950s based on this expanded concept of AGI, see *Federal Tax Policy for Economic Growth and Stability: Hearings Before the Subcommittee on Tax Policy of the Joint Committee on the Economic Report*, 84th Cong., 1st Sess. 253-55 (1955) (testimony of Randolph Paul).

[10]Calculated according to Internal Revenue Service, *Statistics of Income 1954: Individual Income Tax Returns for 1954*, tab. 1 at 33, tab. 12 at 69 (1957). The lowest relevant AGI class in 1954 encompassed incomes from $30,000 to $50,000; in order to include only those returns with at least $40,000 AGI, the figures for this group were halved. Since there were presumably fewer returns reporting between $40,000 and $50,000 AGI than between $30,000 and $40,000, this procedure probably understates the progressivity of the income tax in 1954 and understates the need for additional taxes from the counterpart group in 1993.

[11]1 U.S. Department of the Treasury, *Tax Reform for Fairness, Simplicity, and Economic Growth: The Treasury Department Report to the President* 2 (1984).

[12]Calculated according to 1993 Individual Statistics of Income Advanced Data; furnished by IRS, Individual Statistics Branch (Apr. 19, 1995).

The reduction in progressivity during the last four decades is indicated by the fact that by 1993 the ratio between the group's share of AGI and its share of taxes has been squeezed down to 1.8. If income tax progressivity had remained constant, the rich would have paid 42 percent (or 3.2 times their share of AGI) of all taxes in 1993.

If raising taxes for the rich is such a simple method of balancing the budget, why has it disappeared from public policy discourse?

To increase their share of taxes commensurately with their enhanced share of AGI, the small elite of 980,000 taxpayers with more than $200,000 in AGI should have paid an additional $100 billion in taxes in 1993. For the group as a whole the effective tax rate would have increased only to an average of 49 percent of AGI (with those reporting $200,000 in AGI paying as little as 40 percent instead of the current 25 percent and income-millionaires 60 percent instead of 31 percent).[13]

If the Republican-dominated 104th Congress returned to its 1950s roots and restored the Eisenhower-era corporate tax rate to 52 percent (from its current 35 percent),[14] it could raise an additional $80 billion.[15] Together with the increased individual income tax revenue, the total of $180 billion would suffice to wipe out the projected 1995 deficit of $176 billion (if that object is important), finance the social programs that the new congressional majority asserts the United States is no longer rich enough to afford, or make it possible to provide additional exemptions for lower-income taxpayers and families with children.

Despite the higher rates, not only would the wealthiest taxpayers retain an affluence far above that of the other 99 percent of taxpayers, but the burden would be shared much more democratically than under the repressive squeeze-the-rich Eisenhower Republicans, when only 170,000 taxpayers reported today's equivalent of $200,000 in income and a mere 3,872 were income-millionaire-equivalents — one-sixth and one-seventeenth respectively of today's contingents.

Bringing back Eisenhower-era progressive taxation — which many liberal tax lawyers and economists regarded as a "myth" even in the 1950s[16] — would not only generate the required revenues, but would also fulfill the other traditional purpose of the income tax by reducing the market's increasingly unequal distribution of income through redistribution. During the last 10 years, the share of total income flowing to the poorest 20 percent of households dropped from 4 to 3.6 percent while the richest 5 percent saw their share rise from 17 to 20 percent.[17] As a result, the United States now boasts the most unequal distribution of income and wealth of all industrialized societies.[18]

If raising taxes for the rich is such a simple method of balancing the budget, why has it disappeared from public policy discourse? One reason that self-interested opponents of steeply graduated income taxes and economics textbooks have commonly offered for downplaying its importance is that there simply are not enough rich people to make a difference in such a large and prosperous economy; consequently, soaking the rich serves not to raise significant amounts of revenue, but only the symbolic purpose of vindictively expressing "envy" of the successful.[19] Whatever plausibility that claim may once have had, it no longer holds up — precisely because of the aforementioned polarization of wealth.

Another perennial reason advanced for attacking high effective tax rates is that they tend to dampen the enthusiasm of the rich for work and investment. Yet numerous studies in the 1950s failed to detect a significant weakening of the work ethic or the incentive to invest caused by high tax rates.[20] The withholding of labor and consequent diminution of potential GNP and national economic welfare attributable to high marginal tax rates, exemplified by actor Ronald Reagan's disincentive to appear in more than four films per year after he reached the 90-percent bracket,[21] was atypical.

Rather than confronting the important issues of economic power and inequality, the two congressional parties are outbidding each other in devising methods of regressive revenue extraction to replace the progressive income tax. The two favorites are the flat tax and some variety of sales or consumption tax. Although it might have seemed unimaginable in 1984 that anyone would ever look back with nostalgia on the Reagan administration as a patron of progressive income tax policy, it is worth recalling the Treasury Department's response to President Reagan's call for a fairer tax code.

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[13] These hypothetical effective tax rates are just one of several possible sets for distributing the additional $100 billion in taxes among the affected AGI classes.

[14] 26 U.S.C. section 11.

[15] This figure is a projection from the (latest) data for 1992, when $132 billion in corporation taxes was paid on $402 billion in net income. Advance data furnished by IRS, Corporation Income Branch (Apr. 20, 1995). For data for 1993, *see* U.S. Bureau of the Census, *Statistical Abstract of the United States: 1994*, tab. 873 at 560.

[16] *See, e.g.*, George Lanning, "Some Realities of Tax Reform," in 1 House Committee on Ways and Means, *Tax Revision Compendium: Compendium of Papers on Broadening the Tax Base* 19, 35 (1959).

[17] U.S. Bureau of the Census, *Income, Poverty, and Valuation of Noncash Benefits: 1993*, fig. 1 at xii (Current Population Reports, Ser. P60-188, 1995).

[18] Keith Bradsher, "Gap in Wealth in U.S. Called Widest in West," *N.Y. Times*, Apr. 17, 1995, at A1, col. 5 (nat. ed.).

[19] *Taxes on Incomes, Inheritances, and Gifts: Hearing Before a Subcommittee of the Senate Committee on the Judiciary*, 83d Cong., 2d Sess. 165 (1954) (statement of Prof. Willford King); Henry Hazlitt, "For Whom the Tax Bell Tolls," *Newsweek* 43 (13):72 (Mar. 29, 1954); David Stockman, *The Triumph of Politics: How the Reagan Revolution Failed* 237 (1986).

[20] *See, e.g.*, Thomas Sanders, *Effects of Taxation on Executives* (1951); J. Keith Butters, Lawrence Thompson, & Lynn Bollinger, *Effects of Taxation: Investments by Individuals* (1953).

[21] Stockman, *Triumph of Politics* at 10.

It expressly rejected the flat tax because, even with a liberal exemption for low-income families, it "would involve a substantial shift of the tax burden from those in the highest income brackets to low- or middle-income taxpayers." Similarly, it ruled out a national sales tax on account of "its regressivity" and "distributional inequity."[22]

Although the extraordinarily capacious exemption ($36,800 for a family of four) that, for example, House Majority Leader Dick Armey, R-Texas, would incorporate into his flat tax[23] is in the abstract to be welcomed, it is a Trojan horse. The only reason that his plan or any flat tax can purport to exempt more than half of the population[24] from the payment of income taxes (without raising rates for the rich to levels that they deem "confiscatory")[25] is that proponents intend to reduce revenues radically to defund the federal government.[26] Whether such schemes can buy off opposition to the dismantling of the national safety net by relieving a not insignificant part of the working class of its tax liability remains to be seen. What is already obvious now is the truth-content of Armey's claim that: "Fairness is . . . the flat tax's great virtue. It's based on the idea of fairness we learned in grade school: Everyone should be treated the same."[27] In fact, however, as the *Wall Street Journal* noted, whereas those with incomes between $15,000 and $30,000 would find their taxes cut by $296, taxes on incomes over $300,000 would drop by an average of $108,000 under Armey's plan.[28] Nor is this disparity a surprise. As even Robert Hall and Alvin Rabushka, the intellectual authors of the current flat-tax movement, have conceded, "it is an obvious mathematical law that lower taxes on the successful will have to be made up by higher taxes on average people."[29]

The not-so-hidden agenda of the majority party in Congress is manifestly to roll back social development in the United States not to the period before Franklin Roosevelt, but to that before Theodore Roosevelt and William Howard Taft, both of whom supported progressive income taxation.[30] In the words of Rep. Robert Walker, R-Pa., of the House Budget Committee: "Denying revenue to Washington is . . . a good thing."[31] To the flat-taxers and consumption-taxers, marginal rates, even though they may have been reduced from 91 to 28 percent (at the low point), will, as tax lawyer Louis Eisenstein observed years ago, "always be too high. For in their considered view income taxes are inherently evil. [A]s long as such a tax remains, businessmen are doomed to do less than their best. No matter what the rates are, we will continue to hear: 'Taxes are eating at the foundation of our free-enterprise system . . . and enslaving the American people by depriving them . . . of their right to spend their own money.'"[32] Yet as the chairman of President Nixon's Council of Economic Advisers, Herbert Stein, has reminded the tax-attackers: "There are no self-made men or women in America. Everyone who earns money here earns it in part by virtue of conditions he never made — conditions of society, including the laws that enable him to earn and keep it."[33]

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Although the graduated income tax has been immune to constitutional attack for the last 80 years, simple legislation may nevertheless turn the United States into the world's only capitalist country without one. Ironically, however, as John Kenneth Galbraith observed during the Eisenhower years, it is doubtful whether "any single device has done so much to secure the future of capitalism" as the progressive income tax, which buttresses income inequality because: "The rich man no longer has the embarrassing task of justifying his higher income on grounds of superior morals, ability, diligence or higher natural right. He need only point to the tax he has to pay."[34]

Today's market-knows-besters are no longer embarrassed by economic inequality, which they praise as the greatest engine of prosperity. Because "economic growth is economic justice," their mission, as House Speaker Newt Gingrich recently observed, is to "get government out of the way of the American economy."[35] The new chairman of the House Ways and Means Committee, Rep. Bill Archer, R-Texas, not only is unconcerned that a national sales tax would benefit the rich, but wants the very word expunged from the

[22]1 U.S. Department of the Treasury, *Tax Reform for Fairness, Simplicity, and Economic Growth* at 21, 223, 35.

[23]H.R. 4585, section 101, 103d Cong., 2d Sess. (1994).

[24]The median income of families with two or more children was $36,441 in 1993. U.S. Bureau of the Census, *Income, Poverty, and Valuation of Noncash Benefits*, tab. 4 at 11.

[25]1 U.S. Department of the Treasury, *Tax Reform for Fairness, Simplicity, and Economic Growth* at 2.

[26]*See, e.g.*, William Safire, "The 25% Solution," *N.Y. Times*, Apr. 20, 1995, at A19, col. 1 (nat. ed.).

[27]Dick Armey, "Review Merits of Flat Tax," *Wall Street Journal*, June 16, 1994, at A16.

[28]David Wessel, "Talk of Tax Reform Is Gaining Momentum, But Plans Vary Widely," *Wall Street Journal*, Jan. 31, 1995, at A1, col. 6, at A13, col. 6.

[29]Robert Hall & Alvin Rabushka, *Low Tax, Simple Tax, Flat Tax* 58 (1983).

[30]41 *Cong. Rec.* 27-28 (1906); 44 *Cong. Rec.* 487, 3344 (1909); Theodore Roosevelt, "A Premium on Race Suicide," *Outlook*, 105:163 (Sept. 27, 1913).

[31]"Crossfire," CNN, Apr. 3, 1995, 7:30 p.m. (Lexis).

[32]Louis Eisenstein, *The Ideologies of Taxation* 222 (1961).

[33]Herbert Stein, "The People vs. the People," *Wall Street Journal*, Apr. 20, 1995, at A12, col. 3.

[34]John Kenneth Galbraith, *American Capitalism: The Concept of Countervailing Power* 182 (1956)

[35]Newt Gingrich, "The Contract's Crown Jewel," *Wall Street Journal*, Mar. 21, 1995, at A20.

dictionary and replaced with "'higher income rather than lower income.'"[36] And Bruce Fein, an associate deputy attorney general in the Reagan administration and leading free-enterprise lawyer, finds it so "morally outrageous" that the poorest 50 percent of taxpayers "contribute a paltry 5 percent of income tax revenues" that he proposes lighter taxes on the rich "to reward conduct that most advances the happiness of others."[37]

The new tax- and budget-cutters have set out to refute David Stockman's conclusion that: "The abortive Reagan Revolution proved that the American electorate wants a moderate social democracy to shield it from capitalism's rougher edges."[38] The overreaching embodied in this programmatic return to the jungle of unfettered competition and accumulation may yet trigger a revolt that those who believe that the end of history has arrived would not have thought possible.

[36]David Rosenbaum, "A Zeal for Tax Cuts Now Has Power, Too," *N. Y. Times*, Apr. 4, 1995, at A1, col. 4, at A8, col. 4-5 (nat. ed.).

[37]Bruce Fein, "Morally Right, Fiscally Astute," *Washington Times*, Dec. 13, 1994, at A18 (Lexis).

[38]Stockman, *Triumph of Politics* at 394.