THE FREEMAN

The Progressive Income Tax

Backed by the envious, used by the greedy

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By Doug Bandow

Most Americans dislike the income tax, now more than a century old. The rates are too high. The provisions are unfair. The recordkeeping is onerous. The revenues are wasted.

Other than that, Mrs. Lincoln, how was the play?

But there are fans. The politicians, certainly, of both parties. What good would it do to serve in Congress if you didn’t have any money to spend? There are other sources of public money, to be sure, but none so effective at plucking the geese while minimizing the hissing. Withholding means many Americans look forward to receiving a refund even though that means they have provided an interest-free loan to the very officials conscripting people’s money for dubious purposes.

The beneficiaries of the politicians’ largesse also share in the income-tax lovefest. Uncle Sam needs money to write checks. He can borrow, but there’s a limit to investors' credulity. Borrow too much and they might doubt Washington’s ability to repay. Moreover, robust tax collections are necessary to repay debts. So creditors, too, benefit from the income tax, even if they don’t enjoy paying on the other end.

Don’t forget about the armies of tax preparers and IRS agents who, at the end of the day, end up with much of the deadweight loss.

Then there are the fans of expensive and expansive government. Jonathan Cohn of the *New Republic* argued that the money collected has gone for building infrastructure, cleaning the environment, and keeping us safe from foreign threats. Alas, a lot of federal building is politically driven, conservation measures spend huge amounts inefficiently to control minimal problems, and military outlays go to defend scores of foreign societies rather than our own. In all these cases, less would be more.

More dangerous may be the social engineers. For instance, Yale economics professor Robert J. Shiller suggested using the income tax to mitigate “some of the worst consequences of income inequality.” He proposed indexing taxes to income inequality.

It’s a genuinely nutty idea: Inequality measures are sensitive to data distortion based on dates chosen, units measured, and more. Moreover, they incorporate no judgments about how the inequality arose. Were opportunities obstructed, systems manipulated, wealth extracted, people defrauded? Or did a generally free society operate naturally and deliver ever-changing income and wealth patterns? If the latter, what is the government trying to "correct"? And if the former, is the government correcting the right things?

Worse, though, is the weird presumption that seizing private wealth from mostly productive taxpayers and giving it to political operators noted for their electoral skills rather than economic judgment would somehow remedy financial disparities. There is no evidence that increasing Washington's resources would yield greater social or economic justice, improve economic efficiency or growth, or make people wealthier or freer.

To the contrary, experience demonstrates that the majority—most people outside of those who make their living from the federal trough—are likely to end up worse off. Extensive bureaucracies soak up a lot of money before it leaves government hands. Cash gets tossed at influential interest groups, such as businesses, non-profits, contractors, and unions. Benefits for the poor are dwarfed by middle class welfare, such as Social Security and Medicare. Federal largesse gets bestowed on foreigners through misnamed foreign aid, which long meant taking money from poor people in rich countries and giving it to rich people in poor countries. America's defense budget is another form of foreign aid, subsidizing some of the wealthiest countries on the planet.

Providing more money to expand these and other programs is supposed to close the income and wealth gaps? The social engineers just assume that the benevolent dictator model, in which angels enact direct transfers that make people healthier and happier, can actually exist.

Unfortunately, the income tax creates additional harms. By taxing work, the levy discourages work. The higher the rate, the greater the incentive to choose leisure and invest in consumption and tax shelters. Moreover, credits and deductions give legislators the opportunity to play social engineers, providing subsidies and manipulating behavior *sub rosa*.

The greater the resulting complexity, the more wealth is wasted in compliance activities rather than invested in productive endeavors. Indeed, the system most benefits tax professionals who profit from the system's failings. Today the tax code and IRS rules run nearly 75,000 pages. And there never is any certainty; my Cato Institute colleague Chris Edwards noted nearly 5,000 tax changes over the last decade. Ever-confused taxpayers are a captive audience for tax preparers and litigators.

Income taxes impose a number of other burdens. There is no financial privacy, since Uncle Sam is empowered to rummage through everyone's personal affairs. And taxpayers are expected to maintain potentially extensive records for possible inspection for years. For instance, use a home office and you'd better keep your utility bills, home repair charges, and gasoline receipts!

Moreover, as Edwards pointed out, the entire enforcement process is built around a denial of due process. From start to finish the burden of proof falls on the taxpayer, not the government. The Fifth Amendment right against self-incrimination is out the window. Fourth Amendment protections against unreasonable searches and seizures don’t apply. Sixth and Seventh Amendment guarantees of a jury trial don’t cover the U.S. Tax Court.

Contrast this with the sales tax. You pay it when you purchase something and you are done with it. You don't have to keep personal records. You don't have to file a return. There is no government rummaging around through your bank records for enforcement.

Even social engineering usually is at a minimum. Consumption levies typically include little variations of rates among goods, with at most occasional exemptions of “necessities” and surcharges for “luxuries.” There seldom is much attempt to manipulate rates to achieve objectives other than raising revenue. Even politicians don’t claim that they can use the sales tax to solve the “problem” of income inequality.

The first income tax in U.S. history was proposed in 1814 to fund the ill-fated War of 1812. Happily, the conflict ended before Congress could demonstrate the dire consequences even of taxation with representation. In 1861, a desperate national government turned to the income tax to fund its war to conquer the Southern states seeking to separate. Americans sacrificed both independence and liberty in that conflict.

A search for revenue to replace declining tariff collections led to another income tax in 1894, but the Supreme Court declared the levy unconstitutional. Legislators probably could have met the jurists’ objections by scaling back the tax. Instead, 15 years later Congress proposed a constitutional amendment, which was approved on February 2, 1913, during the heyday of the Progressive Era. From modest beginnings it has grown into a monster.

There is a necessary role for government, but it is far more limited than today’s Leviathan in Washington. Government must be funded, but it should be by something other than today’s income tax, which has made it far too easy for politicians to mulct the public. There are many reasons for Americans’ steady and serious loss of liberty, but the income tax ranks high among them.

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