



Ideas Changing the World

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Tax and Spending Issues

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Higher Taxes Don't Mean More Revenue

The intelligentsia of the Democratic Party is growing increasingly enthusiastic about raising the highest federal income tax rates to 70 percent or more. This is ostensibly with the intent to raise new revenue so federal spending could supposedly remain well above 24 percent of gross domestic product (GDP) rather than be scaled back toward the 19 percent average of 1997-2007, says Alan Reynolds, a senior fellow with the Cato Institute.

All this nostalgia about the good old days of 70 percent tax rates makes it sound as though only the highest incomes would face higher tax rates.

- In reality, there were a dozen tax rates between 48 percent and 70 percent during the 1970s.
- Moreover, the individual income tax actually brought in less revenue when the highest tax rate was 70 percent to 91 percent than it did when the highest tax rate was 28 percent.
- When the highest tax rate ranged from 91 percent to 92 percent (1951-63), even the lowest rate was quite high -- 20 percent or 22 percent.
- However, those super-high tax rates at all income levels brought in revenue of only 7.7 percent of GDP.

Since the era of 70 percent tax rates, the U.S. income tax system has become far more "progressive."

- Congressional Budget Office estimates show that from 1979 to 2007 average income tax rates fell by 110 percent to minus 0.4 percent from 4.1 percent for the second-poorest quintile of taxpayers.
- Average tax rates fell by 56 percent for the middle quintile and 39 percent for the fourth, but only 8 percent at the top.
- Despite these massive tax cuts for the bottom 80 percent, overall federal revenues were the same 18.5 percent share of GDP in 2007 as they were in 1979 and individual tax revenues were nearly the same -- 8.7 percent of GDP in 1979 versus 8.4 percent in 2007.

Source: Alan Reynolds, "Why 70 percent Tax Rates Won't Work," Wall Street Journal, June 16, 2011.

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