81-7,12

TAXATION and INEQUALITY

Gabriel Kolko

Gabriel Kolko is on the history faculty at the State University of New York at Buffalo. He is the author of a number of books, including The Triumph of Conservatism and Wealth and Power in America, of which this article is a chapter (published 1962 by Praeger; reprinted by permission).

published by
New England Free Press
791 Tremont St.
Boston, Mass. 02118

10¢

Table I

Percentage of National Personal Income, Before Taxes, Received by Each Income-Tenth*

	Highest Tenth	2nd	3rd	4th	5th	6th	7th	8th	9th	Lowest Tenth
1910	33.9	12.3	10.2	8.8	8.0	7.0	6.0	5.5	4 9	3.4
1918	34.5	12.9	9.6	8.7	7.7	7.2	6.9	5.7	4.4	2.4
1921	38.2	12.8	10.5	8.9	7.4	6.5	5.9	4.6	3.2	2.0
1929	39.0	12.3	9.8	9.0	7.9	6.5	5.5	4.6	3.6	1.8
1934	33.6	13.1	11.0	9.4	8.2	7.3	6.2	5.3	3.8	2.1
1937	34.4	14.1	11.7	10.1	8.5	7.2	6.0	4.4	2.6	1.0
1941	34.0	16.0	12.0	10.0	9.0	7.0	5.0	4.0	2.0	1.0
1945	29.0	16.0	13.0	11.0	9.0	7.0	6.0	5.0	3.0	1.0
1946	32.0	15.0	12.0	10.0	9.0	7.0	6.0	5.0	3.0	1.0
1947	33.5	14.8	11.7	9.9	8.5	7.1	5.8	4.4	3.1	1.2
1948	30.9	14.7	11.9	10.1	8.8	7.5	6.3	5.0	3.3	1.4
1949	29.8	15.5	12.5	10.6	9.1	7.7	6.2	4.7	3.1	0.8
1950	28.7	15.4	12.7	10.8	9.3	7.8	6.3	4.9	3.2	0.9
1951	30.9	15.0	12.3	10.6	8.9	7.6	6.3	4.7	2.9	0.8
1952	29.5	15.3	12.4	10.6	9.1	7.7	6.4	4.9	3.1	1.0
1953	31.4	14.8	11.9	10.3	8.9	7.6	6.2	4.7	3.0	1.2
1954	29.3	15.3	12.4	10.7	9.1	7.7	6.4	4.8	3.1	1.2
1955	29.7	15.7	12.7	10.8	9.1	7.7	6.1	4.5	2.7	1.0
1956	30.6	15.3	12.3	10.5	9.0	7.6	6.1	4.5	2.8	1.3
1957	29.4	15.5	12.7	10.8	9.2	7.7	6.1	4.5	2.9	1.3
1958	27.1	16.3	13.2	11.0	9.4	7.8	6.2	4.6	3.1	1.3
1959	28.9	15.8	12.7	10.7	9.2	7.8	6.3	4.6	2.9	1.1

* In terms of "recipients" for 1910–37 and "spending units" for 1941–59.

Source: Data for 1910–37 are from National Industrial Conference Board, *Studies in Enterprise and Social Progress* (New York: National Industrial Conference Board, 1939), p. 125. Data for 1941–59 were calculated by the Survey Research Center. Figures for 1941–46 are available in rounded form only. Previously unpublished data for 1947–58 are reproduced by permission of the Board of Governors of the Federal Reserve System, and data for 1959 by permission of the Survey Research Center.

The table on this page is from chapter 1 of the book and is referred to on page 33 of this article. But it should be closely studied in itself.

Taxation and Inequality

It is widely believed that, as Ernest van den Haag and Ralph Ross put it, "the effect of progressive income taxes in diminishing the income of the upper brackets is too plain to need rehearsing."[1] But the impact of Federal income taxes on the actual distribution of wealth has been minimal, if not negligible. The desire to avoid the burden of high taxes has given rise to new factors in the distribution of wealth, which have so complicated the picture that a change in form has been mistaken by many for a basic change in content. A careful study of the topic will hardly sustain this illusion.

Contrary to common belief, heavy taxation of upper-income groups did not begin with the advent of the New Deal; it began only with the approach of United States involvement in World War II. Higher income taxation came as a response of the Roosevelt Administration to world events and not as a result of a conscious commitment to a social policy of reducing inequalities in the distribution of wealth.

As a matter of historical record, the New Deal was not seriously interested in taxation as a means of income equalization—despite its frequent assertions that it was. Roosevelt actively supported the Revenue Act of 1934, but his support for the somewhat stronger 1935 Act was equivocal and was finally obtained only because he feared the growing appeal of Huey Long's "Share-the-Wealth Clubs" and attacks by progressives in Congress. Even so, in a number of important areas, the provisions of the two Acts were hardly designed to redistribute wealth effectively or reduce the capital accumulations of the rich. The estate-tax rates, which the 1932 Act set at 2 per cent for each bracket above $70,000, were raised to 3 per cent on amounts above $70,000 and up to $4.5 million, after which the rate dropped to 2 per cent. The corporate income tax was raised from 12 per cent to 15 per cent in 1936, to 19 per cent in 1939; not until 1942 was it raised to 40 per cent.[2]

Before 1941, the New Deal practice on personal-income taxation was, despite its difference in verbiage, essentially a continuation of that of the Hoover Administration. In 1929 and 1940, when the national personal income was almost the same, Federal receipts from personal income taxes were virtually identical—$1.323 billion in 1929 and $1.393 billion in 1940. But in 1941, the Federal personal income tax, increased because of the growing military budget, produced revenue one-half more than in 1940, although personal income increased only 14 per cent. In 1944, personal income was twice the 1940 level, but the tax yield was twelve times as great.[3] While much of this increased burden fell on the upper-income groups—enough to stimulate their search for new ways to avoid the highest tax brackets—the major weight fell on income groups that had never before been subjected to the income tax.

Thus, the ironic fact is that the extension of the income tax to middle- and low-income classes was the only original aspect of the New Deal tax policy.

Taxation: Theory and Practice

The feature of the income-tax structure that purportedly has had a major impact is the extremely steep tax rates (up to 91 per cent) on the very largest incomes. Actually, the resulting varied and ingenious methods of tax avoidance have substantially lessened the importance of these theoretically high rates.

Since 1941, members of the economic elite have attempted to receive their income in nontaxable forms or to postpone receiving it until retirement, when they will be in lower income brackets. There has been a strong downward shift in income-bracket levels, with an increasing proportion in the $25,000–$100,000 bracket, and in some years there has been an absolute drop in the number of returns reporting more than $100,000. More important, however, has been the trend away from the forms of income subject to high tax rates (salaries, wages, and certain types of property income) and toward tax-free interest, capital gains, and many other forms of income taxed at much lower rates or not at all. The proportionate importance of these forms of income to total income rises sharply in every income category over $10,000 a year.

Under Roosevelt, up to 1941, the actual, as opposed to the theoretical, tax rates on very high incomes were not very different from those under Herbert Hoover. Theoretically, the statutory tax is levied on straight income, none of which is derived from capital gains or other sources taxed at lower rates, from which no deductions are made, and no evasion attempted. In 1932, the highest possible tax rate on incomes of $1 million and up was 54 per cent, but only 47 per cent was actually collected. In 1938, the maximum theoretical tax rate had increased to 72 per cent, but only 44 per cent was collected. By 1957, the highest possible tax rate was 91 per cent, but only 52 per cent was collected.[4] As J. Keith Butters, Harvard economist, has written in his major study of taxation and the rich, *Effects of Taxation—Investment by Individuals* (1953), "By far the most striking and significant feature . . . is the large excess of theoretical over actual tax rates on upper bracket individuals when these rates are computed for income inclusive of all net capital gains."[5]

The income of the richest tenth is reduced less than 10 per cent by Federal income taxes. And, of course, the other tenths also show a net reduction in earnings after income taxes. Thus, it should come as no surprise that the distribution of income by tenths after Federal income taxes, shown in Table II, page 34, is practically the same as the distribution before taxes (see Table I, page 14). The slight changes in income-shares effected by the income tax have benefited income-tenths in the upper half almost as frequently as income-tenths in the lower half. These fundamental facts have been ignored by those who interpret the tax system on the basis of their arbitrary preconceptions rather than on the basis of its actual effects.

The Revolution in Taxation

Now we see that progressive taxation of incomes has not been applied to the economic elite sufficiently to change the distribution of income-shares, and that although the economic elite has been subject to heavier Federal income taxation since 1941, the same factor that stimulated a higher tax rate on the rich also produced, for the first time in American history, permanent and significant income taxation of low- and middle-income earners.

In 1939, only 4.0 million families or persons were subject to Federal income taxation; in 1940, 7.5 million; in 1941, 17.6 million; in 1944, 42.4 million; and in 1957, 46.9 million.[6] Similarly, the share of the national personal income subject to Federal income taxes was 10 per cent in 1939, 24 per cent in 1941, and 43 per cent in 1957.[7] The net effect, since there was a fairly stable distribution of income over that period, was to tax lower- and middle-income classes that had never been taxed before. This was done by reducing the minimum tax exemption and extending the tax scale. In 1957, 66 per cent of all reported incomes were taxed at the base rate of

Table II

Percentage of National Personal Income Received by Each Income-Tenth After Federal Income Taxes

	Highest	2nd	3rd	4th	5th	6th	7th	8th	9th	Lowest
1947	31 (−2)*	15	12	10	9	8 (+1)	6	5 (+1)	3	1
1949	28 (−2)	15	13 (+1)	11	9	8	7 (+1)	5	3	1
1950	27 (−2)	15	13	11	10 (+1)	8	7 (+1)	5	3	1
1951	28 (−3)	15	13 (+1)	11 (+1)	9	8	7 (+1)	5	3	1
1952	27 (−3)	15	13 (+1)	11	10 (+1)	8	7 (+1)	5	3	1
1953	28 (−3)	15	12	11 (+1)	9	6	7 (+1)	5	4 (+1)	1
1954	27 (−2)	15	13	11	9	8	7 (+1)	5	4 (+1)	1
1955	27 (−2)	16	13	11	10 (+1)	8	6	5 (+1)	3	1

* Numbers in parentheses indicate change in percentage points from before-tax income.

Source: Bureau of the Census, *Statistical Abstract of the United States—1957* (Washington, D.C.: Government Printing Office, 1957), p. 309. These data, collected by the Survey Research Center, include capital gains but exclude income-in-kind.

20 per cent. For married couples, taxable income began at \$3,500 in 1929, \$2,500 in 1935 and 1936, \$1,500 in 1941, \$1,000 in 1944, and \$1,200 from 1948 on. Inflation sharply increased this trend by reducing the value of both incomes and exemptions, and its influence continues. The percentage of Federal revenue yielded by personal-income taxes increased from a scant 9 per cent in 1916 to 18 per cent in 1941, 41 per cent in 1946, and 53 per cent in 1960. At the same time, the percentage of Federal revenue yielded by corporate-profits taxes grew from 8 per cent in 1916 to 26 per cent in 1941, and 30 per cent in 1946, and fell to 28 per cent in 1960.[8]

In this process of incorporating more and more of the American population into the Federal income tax system, a moderate degree of progressive taxation has been maintained. The income tax is practically the only major tax that is not basically regressive. Nevertheless, the income tax paid by the average family in the lowest income-fifth—in 1957, amounting to 3.3 per cent of their income—constitutes a greater hardship for those living on an emergency budget than does the tax burden of 13.7 per cent paid in the same year by the average family in the richest income-fifth.[9]

The basic tax rate on taxable income (i.e., income after all deductions for dependents, charitable donations, medical expenses, etc.) begins at 20 per cent. A major proportion of legitimate expenses is unclaimed annually, and most of this can, we know, be attributed to low- and middle-income families.[10] Fewer than 10 per cent of those earning less than \$2,000 take credit for deductible expenditures beyond their dependents and the flat 10 per cent allowed on the short form.[11] This failure is due in large part to the complexity of filling out a "long form" for deductions. Deductions, it should be pointed out, must be quite high before they will save a family anything. For example, a family that can claim no deductions for interest, state taxes, donations, casualty losses, or the like must have medical expenses amounting to at least 13 per cent of its total income before it will save anything.

Joint-filing provisions for husbands and wives, intended to lower their tax burden, were of no benefit in 70 per cent of the joint returns filed in 1957, which were from low- and middle-income groups.[12] In the upper-income brackets, however, the joint return can be of enormous benefit. On an income of $35,000, it can realize a peak saving of 40 per cent of the tax bill.[13]

The Combined Impact of All Taxes

Most recent commentators who have credited the Federal income tax with redistributing income have ignored the fact that it is only one of a number of taxes—and the only one that is in some measure progressive. Therefore, any discussion of distribution of income after taxes must consider the consequences of all taxes.

In general, local and states taxes are regressive. More than half—59 per cent in 1958—of all state tax revenues come from sales taxes. About one-half of the expenditures of an average spending unit earning a cash income of less than $1,000 a year are subject to general sales or excise taxes, but only one-third of the expenditures of those earning $10,000-plus are so taxed.[14] In effect, corporations present the public with additional hidden taxes. The corporation income tax is, as the *Wall Street Journal* puts it, "treated by the corporations as merely another cost which they can pass on to their customers."[15] It has been variously estimated that one-third to one-half of this tax is shifted to the consumers. Furthermore, at least two-thirds of American corporations add all payroll-tax costs to their prices.[16]

The Tax Foundation has calculated actual taxes paid as a percentage of income for all income classes in 1958 (see Table III, page 37). Its figures show that state and local taxes are

TABLE III

PERCENTAGE OF 1958 TOTAL INCOME PAID IN FEDERAL, STATE, AND LOCAL TAXES,* BY INCOME CLASS

Income Class (In dollars)	Share of Taxes (In per cent)		
	Federal	State and Local	Total†
0– 2,000	9.6	11.3	21.0
2,000– 4,000	11.0	9.4	20.4
4,000– 6,000	12.1	8.5	20.6
6,000– 8,000	13.9	7.7	21.6
8,000–10,000	13.4	7.2	20.6
10,000–15,000	15.1	6.5	21.6
15,000–plus	28.6	5.9	34.4
Average	16.1	7.5	23.7

* Social-insurance taxes are not included.

† Because of rounding, items do not always add up to totals.

Source: Tax Foundation, *Allocation of the Tax Burden by Income Class* (New York: Tax Foundation, 1960), p. 17.

regressive, and that all Federal taxes combined, although tending to be progressive, fall much more substantially on the low-income classes than is generally realized. Included in its calculations are all local, state, and Federal personal-income taxes; inheritance, estate, and gift taxes; corporate-profit taxes (it assumes that one-half of this is shifted to the public); excise and sales taxes; customs and property taxes. Excluded are the highly regressive social-insurance taxes, which take 7.3 per cent of the total income of those earning $2,000 or less but only 1.5 per cent in the $15,000-plus class.

These Tax Foundation data indicate that the combined American tax system is scarcely "progressive" and hardly in accord with the image of it nourished by most social scientists and students of contemporary America.[17] If, despite innumerable loopholes, the Federal income tax has introduced a moderately progressive but greatly misunderstood and overemphasized taxation, the Federal excise and customs—and most major local and state—taxes have seriously lessened its impact. The income tax paid by the lower-income classes is, for the most part, money that would otherwise go for essential personal and family needs; in this light, the tax burden is substantially heavier for the lower-income classes than for the higher-income classes.

Welfare and Income Inequality

Theoretically, it would be possible for the revenues from regressive taxation to be directed to welfare expenditures for lower-income groups, and for the inequality of income distribution to be reduced thereby to a significant extent. This has actually been achieved, in the eyes of a number of proponents of the income-redistribution thesis. "Through a combination of patchwork revisions of the system—tax laws, minimum wage laws, subsidies and guarantees and regulations of various sorts, plus labor union pressures and new management attitudes—we had repealed the Iron Law of Wages," wrote Frederick Lewis Allen in *The Big Change*. "We had brought about a virtually automatic redistribution of income from the well-to-do to the less well-to-do."[18] The plausibility of this thesis has only been strengthened by the attacks of conservatives on the alleged "welfare state" created by the Roosevelt Administration.

However, this viewpoint is not sustained by a careful examination of the motives for the revisions in the tax structure: The reason for high taxation, at least since 1933, has been not to redistribute income but to pay for extraordinary costs—primarily military from 1940 on—in the most expeditious way. We have not taxed the rich to give to the poor; we have taxed both the rich and the poor and, at least since 1940, contributed only a small fraction of the proceeds to the welfare of the poor.

Consider, for example, 1958. In that year, Federal revenue from personal-income, estate and gift, corporate-profit, and excise and customs taxes, excluding the self-financing social-insurance program, amounted to $69 billion.[19] The families and unattached individuals in the $0–$2,000 class contributed $1.066 billion, those in the $2,000–$4,000 class contributed $4.971 billion. But the Federal government spent only $4.509 billion on what by the most generous definition may be called "welfare." Included were all expenditures for public assistance, public health, education, and "other welfare," and half of the outlay for farm parity prices and income, and public housing. In 1949, Federal expenditures for welfare were $2.037 billion; in 1954, they were $2.451 billion, and in 1955, $4.062 billion. In each of these years, however, the total Federal tax payments of the spending units earning less than $4,000 were greater than these welfare expenditures. If all Federal welfare expenditures went to the $0–$4,000 class—which was certainly not the case—this class more than paid for them.

In brief, welfare spending has not changed the nature of income inequality, nor raised the standard of living of the lowest-income classes above what it would have reached if they had not been subjected to Federal taxation. It might be claimed that these classes must assume some responsibility for the nation's "larger obligations," but this is not an argument advanced by those who assert that we have redistributed income through taxation and welfare measures.

Means of Tax Avoidance

The most effective way of avoiding taxes, of course, is by not declaring one's income. In 1957, 9 per cent of the national personal income—$28 billion—never appeared in tax returns. As indicated in Chapter 1, most of this $28 billion was received by the upper-income class. This problem of undeclared income was negligible before 1941, but, as an Internal Revenue official suggested in 1959, "When the tax rates were low, there wasn't much to be gained." The strictly legal loopholes for tax avoidance are numerous. Still, as one tax accountant put it, "Taxpayers in the 50% bracket or higher start getting a feeling of anger . . . and they start looking for ways to lighten the load. First they take the legal steps of tax avoidance. But many find this doesn't give them enough relief."[20] The wide extent of tax evasion makes it obvious that the risks involved are insufficient to discourage the practice.

Capital gains are the single most important means of avoiding the theoretically high tax on large incomes. The highest tax rate on capital gains—profits from sales of stock, property, etc., that have been held longer than six months—is only 25 per cent. It is significant that in 1942, soon after the income-tax burden on the highest-income groups was increased, Congress reduced this holding period from two years to six months. The effect was to offset the increased tax burden on one form of wealth by reducing it on another. The act was based on the specious assumption that the flow of profits on stocks and sales was "long-term" windfall profit rather than income. In 1957, 20 per cent of the total income of the $100,000-plus class was in capital gains, and this income was, at the most, taxed at a rate only slightly higher than the rate on the taxable income of the lowest-income classes. By way of contrast, only three-tenths of 1 per cent of the total income of those in the $3,500–$4,000 class originated as capital gains that year.[21]

As a result of the preferred tax status of capital gains, the wealthy have attempted to maximize the means for obtaining them, and the concept of executives' compensation in the corporation has been accordingly adjusted. "You can't compete for executive talent today without a gimmick," declared David Sarnoff, Chairman of the Radio Corporation of America, several years ago.[22] These gimmicks take innumerable forms—deferred-compensation plans, profit-sharing trusts, stock options, and the like—but all have two common purposes: to maximize the amount of income going to executives as capital gains and to postpone disbursement of part of their income until retirement, when most will fall into lower-income categories. Before 1940, about 700 companies had such plans in operation; by 1946, 9,000 firms had them.[23]

Under a deferred-compensation plan, the executive receives, after retirement, his own payments to the plan as tax-free income; he pays only a capital-gains tax on the company's contributions. These plans differ in detail but not in essential form. For top executives, special arrangements are often made. Harley J. Earl, a General Motors vice-president who retired in December, 1958, after having earned a peak salary of $130,000 a year, receives $50,000 a year until December, 1963, and $75,000 a year for the ten years thereafter.[24] Although not always so generous, most companies, especially if they are closely owned, sponsor similar plans for top executives.

The stock option, a tax-avoidance factor of tremendous importance to corporate executives, was introduced in the 1950 Revenue Act, and it has become a major means of compensating members of the economic elite. By 1957, 77 per cent of the largest manufacturing corporations had set up option plans. Under the terms of the Act, an option on a company's stock is offered to an executive at no less than 85 per cent (in practice, it is generally 95 per cent) of the current market value. The executive must wait at least eighteen months before he exercises the option—if he chooses to exercise it. If the market price rises, as it almost invariably does in an inflationary economy, the executive buys the stock at its original low price; then, if he waits six months to sell, he pays only the capital-gains tax on the profit. If the stock's price falls 20 per cent or more below the option price, the option price can again be reduced to 95 per cent of the average market price for the twelve months preceding the new change.

"In the past five years," *U.S. News & World Report* observed in 1955, "these options have produced a whole new crop of millionaires." One aircraft company gave thirteen executives an option on 30,000 shares in 1951; in 1955, they realized a 370 per cent profit. A rubber company granted a vice-president an option on 10,000 shares worth $213,800 in 1951; in 1955, they were worth $547,000. In 1957, Frank Pace, Jr., and John J. Hopkins exercised their options to buy General Dynamics stock then valued at $1,125,000 and $1,220,000, respectively; their option price was about one-third the market value at the time of the stock sale. In January, 1956, Donald W. Douglas, Sr., of Douglas Aircraft, exercised an option for 15,000 shares at $16.50 each at a time when the market price had risen to $86—a profit of more than $1 million. During 1956, when executives at Pittsburgh Plate Glass purchased 40,000 company shares at an option price of $41, the market price ranged from $74 to $96. Beginning in 1951, U.S. Steel granted its executives stock options with a face value of $49 million; on August 8, 1957, the stocks were worth $133 million on the market.[25]

Those in the high income-tax bracket find it profitable to receive part of their income in totally tax-exempt interest. In 1957, they received almost $600 million of income in this form. Kuznets, in his study of the top 5 per cent, did not allocate any of this nontaxable income to this income group after 1940. However, we know that the economic elite have been rapidly increasing their tax-exempt holdings since 1929 and that they now own almost all available holdings of this type.[26] We also know that the sales and yield of tax-free state and local securities have risen very sharply since 1939. Thus we can see the rising importance of tax-free income to the wealthy. These securities yield as high as 6 per cent, although the 1959 average yield on high-grade municipal bonds was 4.0 per cent. With a taxable income of $70,000 to $80,000, a tax-free return of 4.0 per cent is equal to a taxable 21.0 per cent return after taxes. In the $150,000–$200,000 bracket, a tax-free 4.0 per cent return is equal to a taxable 40 per cent after taxes, and a tax-free 5.25 per cent is equal to a taxable 52.5 per cent after taxes.

Contrary to common opinion, inherited wealth and large capital accumulations have not been seriously affected by the existing tax laws. Here the legal escape clauses are so numerous that the impact of the high estate tax—theoretically up to 77 per cent on $10 million—is, in actuality, nominal. In 1951, the total net value of estates reported on taxable returns was taxed at only 14 per cent.[27]

A married man can divide his estate so that one-half is taxed at his death and one-half at his wife's death, thereby sharply lowering the tax bracket. In this way alone, the taxes on a $300,000 estate would be reduced from $62,700 to $17,900, and the taxes on $10,060,000 estate from slightly more than $6 million to less than $2.5 million.[28]

However, two major alternatives—gifts and trusts—allows persons with taxable estates of $100,000 and up to avoid the heaviest rates. Gifts made by wealthy individuals during their lifetime are taxed much less than the same gifts made as bequests after their death. The gift-tax rate on $1 million is 27.75 per cent; the inheritance-tax rate is 31.4 per cent. But even this rate is often avoided. A man may split up his estate by giving $6,000 a year to his wife and $3,000 a year—or $6,000, if his wife agrees—to as many other persons as he wishes. Only the donor is taxed on the gift at the gift-tax rate, which begins at 2.25 per cent under $5,000. In addition, a $60,000 basic lifetime exemption is allowed every couple.

By 1951, about 45 per cent of the value of estates worth more than $500,000 had been placed in trusts.[29] The trust guarantees that estate taxes will not be paid by a family on the amount set aside for at least two generations after the death of its founder. It divides the family fortune, for purposes of taxation, into smaller units and can result, under the 1952 tax laws, in tax savings as high as 70 per cent on the income of property placed in trust. By September, 1959, all the states had enacted "custodian laws" to allow members of families to organize and manage trusts in the name of minors, permitting the eventual avoidance of estate taxes, division of income for current tax purposes, and elimination of cumbersome legal procedures for the organization of trusts.

Since the 1952 tax law, a rapidly growing number of special provisions have been created that apply to relatively small groups among the wealthy but add up to a cumulative trend toward legal tax avoidance. The fantastic complexity of the tax law has not succeeded in dimming the sheer genius of tax lawyers, who have aided the economic elite to circumscribe, in a perfectly legal manner, many of the more onerous tax provisions. Their ultimate success, however, can be attributed neither to their ingenuity nor to the intricacy of the tax law; it results from the failure of political administrations over the past four decades to enact tax legislation that seriously challenges the economic power of the wealthy. All recent Administration suggestions for closing these tax loopholes have been coupled with proposals to lower the tax rates on the richest income classes—thereby leaving the wealthy in substantially their present economic position.

Viewing this sharp contrast between the avowed equalitarian sentiments of most politicians and the legal and economic reality of the tax structure, Stanley S. Surrey, of the Harvard Law School, has rightly concluded that "the average congressman does not basically believe in the present rates of income tax in the upper brackets. When he sees them applied to individual cases, he thinks them too high and therefore unfair. . . . Since they are not, however, willing to reduce those rates directly, the natural outcome is indirect reduction through special provisions."[30]

The complexity of the effect of taxation should not be allowed to obscure the basic trends—the growing tax burden on the low- and middle-income classes, and the huge disparity between theoretical and actual tax rates for the wealthy. The conclusion is inescapable: Taxation has not mitigated the fundamentally unequal distribution of income. If anything it has perpetuated inequality by heavily taxing the low- and middle-income groups—those least able to bear its burden.

FOOTNOTES

1. Ralph Ross and Ernest van den Haag, The Fabric of Society: An Introduction to the Social Sciences (N.Y.: Harcourt, Brace, 1957), p. 398.
2. Roy G. & Gladys C. Blakey, The Federal Income Tax (New York: Longmans, Green & Co., 1940), pp. 366-73; and Louis Eisenstein, 'The Rise and Decline of the Estate Tax', Federal Tax Policy for Economic Growth, p. 830ff.
3. Office of Business Economics, National Income, 1954 (Washington, D.C.: Government Printing Office, 1954), p. 171.
4. All calculations from data in Bureau of Internal Revenue, Statistics of Income for 1939, Part I (Washington: G.P.O., 1942), pp. 63-64, and Statistics of Income--Individual Income Tax Returns for 1957 (Washington: G.P.O., 1959), p. 20.
5. J. Keith Butters et al, Effects of Taxation--Investment by Individuals (Boston: Harvard Business School, 1953), p. 85.
6. Daniel Creamer, Personal Income During Business Cycles (Princeton, N.J.: Princeton U Press, 1956), p. 153; Bureau of Internal Revenue, Statistics of Income--Individual Returns for 1957, p. 23.
7. Joseph A. Pechman, 'What Would a Comprehensive Individual Income Tax Yield?' Tax Revision Compendium, I. 258.
8. William Crum et al, Fiscal Planning for Total War (New York: National Bureau of Economic Research, 1942), p. 172, 174; Economic Report of the President--1958, p. 174; Tax Foundation, Reexamining the Federal Corporation Income Tax (New York: Tax Foundation, 1958), p. 22; The Budget of the U.S. Government for the Fiscal Year Ending June 30, 1960 (Washington: G.P.O., 1959), p. M-12.
9. Selma F. Goldsmith, 'Income Distribution by Size--1955-58', Survey of Current Business, April 1959, p. 16.
10. C. Harry Kahn, 'Personal Expense Deductions', 37th Annual Report, National Bureau of Economic Research, 1957, p. 49.
11. Daniel M. Holland and C. Harry Kahn, 'Comparison of Personal Taxable Income', in U.S. Senate, Jt. Committee on the Economic Report, Federal Tax Policy for Economic Growth and Stability, 84th Cong., 1st Sess. (Washington: G.P.O., 1955), 331-32.
12. Bureau of Internal Revenue, Statistics of Income--1957, p. 37; Lawrence H. Seltzer, 'The Individual Income Tax', 39th Annual Report, National Bureau of Economic Research, 1959, p. 74.
13. Holland & Kahn, op. cit., p. 333.
14. Tax Foundation, Federal Excise Taxes (New York: Tax Foundation, 1956), p. 47.
15. Wall Street Journal, 5 May 1958, p. 1.
16. Lewis H. Kimmel, Taxes and Economic Incentives (Washington, Brookings Institution, 1950), p. 182.
17. Even this inadequate progression is an improvement over the

distribution of the total Federal, state, and local tax burden in 1938-39. In that fiscal year, the total Federal tax burden as a percentage of the income of every income class was about equal in every income class up to $10,000 (roughly equal to $20,000 in 1958), when it began to rise steeply. State and local taxes, as a whole, were mildly regressive. See Temporary National Economic Committee, Who Pays the Taxes? (Washington: G.P.O., 1940) Monograph #3, p. 6.

18. Frederick Lewis Allen, The Big Change (New York:Harper & Brothers, 1952), p. 286.

19. Tax Foundation, Allocation of the Tax Burden by Income Class, pp. 14--15; Bureau of the Census, Statistical Abstract--1959, p. 368.

20. All quotations from the Wall St. Journal, 9 April 1959, p. 1.

21. Bureau of Internal Revenue, Statistics of Income--1957, pp. 24-25.

22. Quoted in Arch Patton, 'Executive Compensation: Tax Gimmicks vs. Incentives', Harvard Business Review, Nov/Dec 1953, p. 114. For a general survey of executive tax avoidance, see Robert Schulman, 'Tax Differentials in Executive Compensation', Income Tax Differentials (Princeton, N.J.: Tax Institute, 1958), pp. 67-81.

23. Lawrence H. Seltzer, The Nature and Tax Treatment of Capital Gains and Losses (N.Y.: National Bureau of Economic Research, 1951), pp. 242ff.

24. Proxy Statement, General Motors Corporations, 1958, p. 13.

25. National Industrial Conference Board, Compensation of Top Executives, 'Studies in Personnel Policy', No. 173 (N.Y.: NICB, 1959), p. 12; US News and World Report, 18 March 1955, p. 27; 11 May 1959, pp. 84-85; US Senate Committee on the Judiciary, Study in Administered Prices in the Steel Industry, Report of the Committee, 85th Cong., 2nd Sess. (Washington: G.P.O., 1958), pp. 110-11. Data on General Dynamics, Douglas and Pittsburgh from their 1957 proxy statements.

26. Raymond W. Goldsmith, A Study of Saving in the United States (Princeton, N.J.: Princeton U Press, 1955), III, 374, estimates that in 1944 the estates valued at $100,000 and over owned as much as 98% of the wholly tax--exempt Federal, state, and local bonds. An excellent survey of tax avoidance laws is Stanley S. Surrey, 'The Income Tax Base for Individuals', Income Tax Differentials (Princeton, N.J.: Tax Institute 1958), pp. 34-58.

27. Eisenstein, op. cit., pp. 833-36.

28. Rene A. Wormser, 'How To Save Money by Giving It Away', U.S. News and World Report, 28 December 1956, p. 111.

29. Eisenstein, op. cit., pp. 837ff.

30. Stanley S. Surrey, 'The Congress and the Tax Lobbyist--How Special Tax Provisions Get Enacted', Harvard Law Review, May 1957, p. 1150; see also the pessimistic conclusions of Randolph Paul, Taxation in the United States (Boston: Little, Brown, 1954), pp. 763ff, on the failure of progressive taxation.