

April 23, 2009

Should the rich pay more?

They already do ...

John LaPlante

The DFL majorities in both chambers of the Minnesota Legislature have proposed adding yet another tax bracket to the state's income tax system, targeting the highest-earning households. That's an unfortunate turn of events, though I'm certainly not surprised—"Soak the rich" must be the unofficial state motto. But for economic, moral, and political reasons, Minnesota and the nation need to end the obsession with income tax "progressivity."

First, some numbers. According to the Tax Foundation, in 2006 the top decile (10 percent) of households by income earned report 47 percent of all AGI (adjusted gross income) in the nation. They paid 71 percent of federal income taxes. In Minnesota, the top decile earned 43 percent of all AGI but paid 66 percent of all the federal income taxes that Minnesota sends to the national government. The Congressional Budget Office, meanwhile, says that nationally, the top decile earned 39 percent of pretax income and paid 71 percent of all income taxes.

You can find a similar pattern in state income taxes. According to the 2009 Minnesota Tax Incidence Study, produced by the Minnesota Department of Revenue, the top decile earned 42 percent of all household income, but paid 57 percent of all income taxes.

The highest-earning taxpayers, in other words, already pay an outsized portion of the income tax.

Rather than making our so-called "progressive" income tax systems even more so, Minnesota and the nation should move towards some form of flat-rate system.

There are a lot of economic arguments against a progressive, or as I call it, graduated tax system, but I'll stick with moral and political ones.

First, at some point, graduated tax rates resemble involuntary servitude. A 100 percent tax would be morally wrong—even if government in turn provided that person with food, housing, clothing, transportation, and every other need in life. Such an arrangement would be a form of slavery.

What percentage of personal income can government take before it gets to that point? I don't know, but the logic behind raising taxes on the wealthy ("we need it, they don't") is troubling.

Placing extraordinary taxes on high-income earners is bad for another reason: That fuels majoritarian impulses that imperil our political system. The majority rules, but our national and political institutions do have checks on majority rule, including the U.S. Bill of Rights. These checks are useful—it's a fact of human existence that small groups of people are vulnerable to rough treatment at the hands of the majority.

Indeed, our political history has been marred by majoritarian excesses, including vigilante justice, lynchings, wartime internment of American citizens and, at our worst, slavery.

By definition, people in the top decile of income earners are a minority vulnerable to being plundered for the benefit of the majority. It is true that a new marginal income tax rate is not as objectionable as mob violence. But it is an attack on the freedom of some people to reap the rewards of their labor.

A graduated tax system invites bad policy. To paraphrase the late economist Milton Friedman, you're going to be a careful shopper if you buy something using your own money—and rather careless if you're spending other people's money.

And our governments spend far too much of other people's money. According to the Tax Policy Center (a joint program of the Urban Institute and the Brookings Institution), 43 percent of the American population (65 million) pays no federal income tax. And, according to the Tax Incidence Study from Minnesota, households in the two lowest deciles here pay no income tax.

Some government programs work well. Others work at cross-purposes with each other, or have long since ceased to be useful. Too few people apply political pressure to fix or scrap dysfunctional programs. If a large portion of the public has little skin in the game, it's not surprising that government doesn't receive the scrutiny that it should.

But, you may ask, what about payroll taxes? The Center on Budget and Policy Priorities says these taxes are a larger burden for most Americans than federal income taxes. That may be true, but they fund two grossly underfunded programs—Social Security and Medicare—that the top decile will eventually be called upon to pay for. And if few people pay that little in federal income taxes, perhaps we've cut federal taxes too much at the lower end of the income scale.

Isn't a flat tax regressive, meaning that lower-income people will pay more as a percentage of their income? Yes. Then again, a Toyota Prius, a Big Mac and a subscription to basic cable also claim a smaller portion of someone's income as they earn more. In short, life itself is regressive.

Even with a flat tax—or even if the state doesn't impose a new income tax bracket—the top decile will still be paying more than the rest of us. They buy more stuff, which means they pay more sales taxes. They buy more expensive houses, and thus pay more in property taxes. When people produce and consume more, they'll pay more. In short, if “soak the rich” is your theme, you don't need a graduated income tax.