

Sixteen for '16 - Number 5: Higher Taxes on Higher Incomes

By [Salvatore Babones](#), [Truthout](#) | Op-Ed

To avoid waste, reduce inequality and maintain some semblance of market efficiency, income taxes should be used to make money as meaningful to a millionaire as it is to you or me.

Back in the olden days of the 1990s, taxpayers with annual incomes over \$500,000 paid federal income taxes at an average effective rate of 30.4 percent.(1) In the 2000s, the equivalent figure is 23.8 percent.(2) Someone has had a very big tax cut in recent years, and the chances are that that someone is not you.

In the 1990s, taxes on high incomes were already low by historical standards. Today, they are even lower. The superrich lower their taxes even more by hiding their income in offshore tax havens. Whatever our statistics say about the tax rates of the superrich, we can be sure they are lower in reality.

At the same time that their tax rates are going down, the annual incomes of highly paid Americans are going through the roof. In the 1990s, the average income of the top 0.1 percent of American taxpayers was around \$3.6 million. In 2012, it was nearly \$6.4 million.(3) And yes, these figures have been adjusted for inflation.

High inequality plus low taxes equals fiscal crisis. The rich are taking more and more money out of the economy, but they are not returning it in the form of taxes. The result is that the US government no longer has the resources it needs to properly govern the country.

High incomes are much higher than ever before, and people with high incomes pay much less tax than they used to.

We need universal preschool, universal healthcare and a massive government-sponsored jobs program. We need complete renewal of our nation's crumbling human and physical infrastructure. We need funds for everything from the cleanup of atomic waste in Hanford, Washington, to improvements at the National Zoo in Washington DC. And we need higher taxes on today's higher incomes to pay for it all.

In 2010, the United States government collected a smaller proportion of the nation's total national income in income taxes than at any time since 1950. Slightly higher taxes on high incomes that came into effect in 2013 reversed this trend, and federal income tax revenues are rising from their 2010 low of 6.1 percent of national income back toward historical average levels.

Under current law, the federal income tax take should rise to 9 percent of national income in 2018. This is an improvement over recent years, but it is still less than in 1998-2001, when the federal government actually had a budget surplus.(4)

The top marginal tax rate on the highest incomes is now 39.6 percent, as it was in the 1990s. This is still a far cry from the 50 percent top tax bracket of the 1970s or the 70 percent top tax bracket of the 1960s, never mind the 91 percent top tax bracket of the 1950s.

A return to the 1990s is a good start, but the next president will have to push much harder because we have since gone a long way down the wrong road. High incomes are much higher than ever before, and people with high incomes pay much less tax than they used to. The result has been an enormous concentration of income among a small, powerful elite.

The concentration of income among a powerful elite may be very good for members of that elite, but it is bad for our society, bad for our democracy and even bad for our economy.

Socially, highly concentrated incomes undermine our national institutions and warp our way of life. For example, people who can afford to send their children to exclusive private schools cease to care for the health of public education, or they erect barriers to separate "their" public schools from everyone else's public schools.

A family with a billion dollar fortune that does absolutely no planning to avoid the 40 percent tax on large estates and no paid work whatsoever can comfortably take out \$15 million a year to live on . . .

Similarly, people who can afford the very best private healthcare care little about ensuring high-quality public healthcare. People who fly private jets care little about congestion at public airports. People who drink imported bottled water care little about the poisoning of rivers and underground aquifers.

Enormous differences in income inevitably create enormous distances between people. America is starting to resemble the fractured societies of Africa and Latin America, where the rich live in gated "communities" with armed guards who enforce the exclusion of the lower classes - except to allow them entry as maids and gardeners.

These nefarious effects of inequality can already be seen in America's sunbelt cities, where there are fine gradations of gated communities: armed guards for the superrich, unarmed guards for the merely well-off, keypad security for the middle class, and on down the line to the unprotected poor. We should be ashamed, one and all.

Politically, highly concentrated incomes threaten the integrity of American democracy by fostering corruption of all kinds. When the income differences between regulators and the industries they regulate are small, we can count on regulators to look after our interests. But when industry executives make two or three (or 10) times as much as regulators, it is almost impossible to prevent corruption.

Even where there is no outright corruption, it is impossible for regulators to retain talented staff. People will take modest income cuts to work in secure public sector employment. They will not take massive income cuts. Those who do are often just doing a few years on the inside so they can better evade regulation when they go back to the private sector.

When doing a few years on the inside includes serving in Congress merely as way to get a high-paying job as a lobbyist, we are in serious trouble.

Along with highly concentrated incomes comes vote-buying and voter suppression. When the stakes are so high, people will play dirty. No one knows how many local boards of one kind or another around the country have been captured by local economic interests, but the number is surely staggering.

Economically, highly concentrated incomes ensconce economic privilege, suppress intergenerational mobility, and can ultimately lead to the total breakdown of the free market as a system for efficiently driving production and consumption decisions.

Privilege is perpetuated by excessive incomes because with enough money, the advantages of wealth overpower any amount of talent and effort on the part of those who are born poor. Nineteenth century English novels were obsessed with inheritance and marriage because in that incredibly unequal society, birth trumped everything else. Twenty-first century America has now reached similar levels of income concentration among a powerful elite.

To make this point graphically clear, a family with a billion dollar fortune that does absolutely no planning to avoid the 40 percent tax on large estates and no paid work whatsoever can comfortably take out \$15 million a year to live on (after taxes, adjusted for inflation) in perpetuity until the end of history - while still growing the estate. That's how mind-bogglingly large a billion dollar fortune is.(5)

When rich people . . . are wasting resources that could be put to much better use by other people . . . this invalidates the foundational principle of modern economics: that the market maximizes the total utility of society.

But probably the least recognized impact of high inequality on our economy is that it severely impairs the efficient operation of the free market itself. Market pricing is at its core a mechanism for rationing. The market directs limited resources to the places where they command the highest prices.

The basic idea of rationing by price is that prices encourage people to carefully weigh their purchases against each other - in other words, to economize.

In an economy where everyone earns roughly the same income, rationing by price works just fine for most goods. People take care of their necessities first. Then they can choose whether to

spend their extra money on eating out, taking vacations, renovating their homes, or saving up to buy something big like a boat.

Because all of these goods are priced in the same currency, people can directly compare their values against each other. And if everyone has roughly the same amount of money to spend, market prices represent roughly the same values for different people. If you and I have the same income, a \$20 restaurant meal means as much to me as it does to you.

Problems set in when incomes are very unequal. For people with extraordinarily high income, prices become meaningless. What does a \$20 restaurant meal mean to someone who makes \$20 million a year? Nothing. The result is incredible waste as the market economy no longer forces people to economize.

When rich people accumulate dozens of cars, maintain yachts they only use once a year, or have servants order fresh-cut flowers every day for houses they rarely visit, they are wasting resources that could be put to much better use by other people.

Waste like this invalidates the foundational principle of modern economics: that the market maximizes the total utility of society. That principle only holds if a dollar has the same meaning for you as it does for me. Highly concentrated incomes undermine the whole idea of the market as an economy - that is, as something that economizes.

And that is the strongest argument for much higher taxes on higher incomes. There are many ways to reduce inequality, but the simplest and most efficient way is through taxation. The goal of income taxes should be to tilt the field so that earning an after-tax dollar means just as much to a CEO as to a fast food worker.

That's why a 90 percent marginal tax on incomes over a million dollars is entirely appropriate. For a poor person who pays no income tax, a \$20 restaurant meal costs \$20. That person must make a real sacrifice to eat out.

For a CEO with a 90 percent marginal tax rate, a \$20 restaurant meal costs \$200 in before-tax income. That may not be a huge sacrifice for someone who makes several million dollars a year, but it does change the equation. A CEO may not hesitate to eat out, but may hesitate to buy a private jet when flying business class will suffice.

To be sure, we need higher taxes on higher incomes to raise money for government. But we also need higher taxes on higher incomes just to make the economy work properly. That's why the economy worked so much better in the high-tax 1950s and 1960s than it has since.

The ultimate goal of income taxes should be to make money as meaningful to a millionaire as it is to you or me. If we can't quite get there in the next few years, we can certainly get closer than we are. One of President Obama's most important accomplishments has been to set us on the

path toward economic sanity by raising taxes on the highest incomes. The next president should build on this legacy - and in a big way.

Notes:

1. Calculations based on [IRS SOI Tax Stats](#) - Individual Statistical Tables by Size of Adjusted Gross Income, Individual Complete Report (Publication 1304), Table 1.1, 1996.
2. Calculations based on IRS SOI Tax Stats - Individual Statistical Tables by Size of Adjusted Gross Income, Individual Complete Report (Publication 1304), Table 1.1, 2011.
3. Calculations based on World Top Incomes Database, variable 6310501.
4. OMB Historical Table 2.3: Receipts by Source as Percentages of GDP: 1934-2019.
5. Author calculations based on a turnover between generations every 30 years and a very conservative 3 percent real return on investment; a 5 percent real return on investment allows the family to withdraw more than \$37 million a year.