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PERSONAL INCOME TAXATION

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THE DEFINITION OF INCOME
AS A PROBLEM OF FISCAL POLICY

By HENRY C. SIMONS

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THE UNIVERSITY OF CHICAGO PRESS
CHICAGO · ILLINOIS

THE UNIVERSITY OF CHICAGO PRESS, CHICAGO & LONDON
The University of Toronto Press, Toronto 5, Canada

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Published 1938. Fourth Impression 1962. Composed and printed
by THE UNIVERSITY OF CHICAGO PRESS, Chicago, Illinois, U.S.A.*

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PREFACE

THIS book perhaps combines strangely the characteristics of an academic treatise and a tract for the times. Attempting to serve both purposes, it may serve neither of them well. In any case, since several sections are addressed mainly to special students, some suggestions may be offered to other readers.

Much can be said for beginning with chapter x, which summarizes the argument and outlines a program for tax reform. Those who must read in haste may consult other chapters on a few topics of their own selection. No one should hesitate to skip parts of chapters i and iii which he finds tedious and unrewarding (pp. 6-15, 63-79, 90-96 esp.); and many readers, with a distaste for academic discussion, may simply omit these chapters.

I am somewhat apprehensive lest readers should find in this book an undue emphasis upon distributional considerations. Taxation is the proper means for mitigating inequality; and, confining attention to this field of economic policy, one naturally places more emphasis upon that objective than would be appropriate in a less restricted discussion. Besides, the reader may wisely make some allowance for the fact that several of these chapters were prepared originally with regard for prevailing opinions which, in both popular and academic circles, have since changed markedly. In spite of endless

revising and re-writing, there are still some passages, notably in the introduction, which would have been more useful as contributions to discussion in the New Era than they will be now. When Republicans were the leading disseminators of economic fallacies, it was proper for the academic person to stress the problem of inequality. Nowadays, however, there is no issue as to the need for lesser concentration of wealth and income. Indeed, we tend now toward relative overemphasis, both in our talk and in our action, upon this particular objective.

On the other hand, there are now momentous issues as to the means by which inequality may properly or actually be mitigated—as to how we may diminish economic inequality without creating a greater inequality or monopoly of political power. A political discussion which has produced keen awareness of a problem has also rendered the community dangerously uncritical and indiscriminating as regards possible solutions. Almost any crank, mercantilist scheme can now be sold as a cure for excessive inequality; and the most naïve and preposterous “purchasing-power” arguments are employed by good people who, like our President, are ordinarily not unsophisticated. Fine sentiments about economic justice are now employed mainly in support of schemes which, in spite of all good intentions, must serve to aggravate inequality, to make poorer a community which at best will be poor enough, and to undermine a political system which we overwhelmingly prefer to the authoritarian alternatives. Thus, I would suggest, as the now significant interpretation of the argu-

ment in chapter i, not merely that progressive taxation is a sound and promising method for mitigating inequality but that it is the only sound and promising method which has seriously been proposed and that other currently popular schemes are unsound technically and incompatible with the kind of total arrangements which we wish to preserve against the recently prevailing world-trend.

Just as the Republican party consolidated its power by dispensing gigantic subsidies in the form of protective-tariff duties, so now the Democrats have been purchasing allegiance by endless restraints upon internal trade. Our politicians, having quietly and passively encouraged the proliferation of monopoly arrangements in many areas, now seek to promote and glorify these arrangements elsewhere. Thus, in the name of justice (fair wages, fair prices, parity prices, and other derivatives of the medieval conception), we are perverting and destroying the free enterprise, free markets, and competitive free trade which are essential to representative government and to orderly political life on a vast national scale. We are deliberately displacing competition within economic groups, which is essentially peaceful, orderly, productive, and mutually advantageous, by organized economic and political action which is inherently exploitative, destructive, and violent. Thus we move toward the politician's millennium where politics has crowded competition entirely out of the picture—toward the economy of organized negotiation which, once achieved, would immediately necessitate the induction of a supreme negotiator who, in turn, would either

liquidate the organizations or utilize them to consolidate his own dictatorial powers. Along the same lines, of course, we are also moving directly away from the conditions which permit of peaceful and orderly relations among the nations of the world.

We need, at the present time, not greater awareness of inequality but greater awareness of the dangers involved in trying to mitigate it by methods which involve restraint of trade. Tax reform, with displacement of sales taxes, customs duties, excise taxes, and payroll levies by progressive personal taxes, would enable us to move gradually but steadily toward better distribution. Such reform can be accomplished within the framework of a democratic, competitive, free-enterprise system. It involves no threat of fundamental change in our institutions; and, instead of restriction of production, it promises increase in employment and in our total national income. In principle, much could be accomplished by more effective governmental spending, especially for education and other welfare services. In fact, however, it is hard to devise new spending schemes that will do more good than harm; and it is easy to impose or retain taxes which more than offset, by their regression and their augmenting of unemployment, any benefits which the expenditures may yield. In a world of large unemployment, it seems hard to mention any new governmental services which are worth the cost of the excise or payroll taxes that might be avoided or repealed if the services in question were withheld. Moreover, if it is hard to avoid bad forms of taxation, it is also hard to get enough taxes of any kind to protect against the in-

flation dangers of new spending schemes. Our economy can be rendered vastly more productive by the restoration of effective price competition; it can be rendered much more stable by movement toward a real monetary system; and, for the significant future, our attack upon inequality may properly be concentrated on changes in the taxes by which present expenditures are financed.

I regret that two recent books, which should be used and cited generously in a study of this kind, became available only after my manuscript was in its final form. The first of these is Roswell Magill's excellent legal study, *Taxable Income* (New York, 1936). This book covers admirably a phase of the subject which is only touched upon in my chapters, and one which, as the reader will discover for himself, I am both indisposed and incompetent to discuss systematically. The other book is a recent Twentieth Century Fund publication, *Facing the Tax Problem* (New York, 1937)—a very useful book which, by virtue of the contributions of Professors Haig and Shoup, is of first-rate importance for its discussion of income-tax problems. My opinions regarding the central points of that discussion have been summarized in a recent review (*Journal of Political Economy*, XLV [August, 1937], 532-35).

The following persons have each made large and generous contributions to the improvement of my manuscript at various stages: Professors Jacob Viner, Frank H. Knight, Simeon E. Leland, and Carl Shoup, and Mr. Aaron Director. I trust that this bare acknowledgment will not obscure my great indebtedness to these men; and I must apologize for not naming the many

graduate students who have markedly influenced my thinking and helped to overcome my inhibitions about publication. (I cannot name them without risking errors of omission which would plague me afterward.) Professor Harry A. Millis has read the manuscript and made several excellent suggestions for change. Both he and Professor Gordon Laing have been helpful and encouraging as regards the arrangements of publication. Miss Gladys Hamilton contributed excellent stenographic services and discovered many errors which might otherwise have survived careful reading of the proof sheets.

For the protection of those who have helped me, be it said that each of them has suggested some changes which I was too indolent or too stubborn to make.

HENRY C. SIMONS

CHICAGO
December 1, 1937

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