September 30, 2011

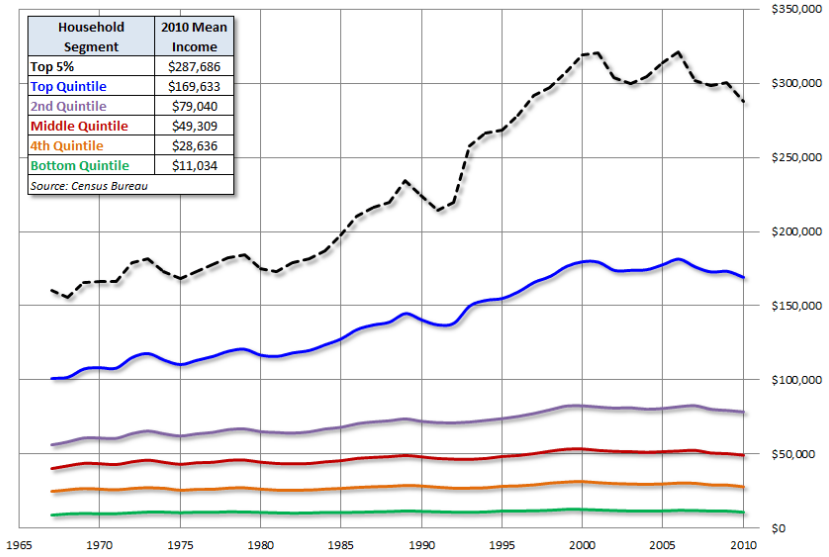
Wealth, Democracy & Tax Policy

The recent protests in New York and other cities around the U.S., regarding the issues of economic inequality, are part of a public awakening to the growing wealth disparity in the United States. Perhaps the most hotly debated and contentious issue of the 2012 Presidential election year will be directly related to the problem of wealth disparity; and the debate regarding the future tax policy of the United States Government. The debate, so far, has centered on the proper level of taxation, especially for those earning over $1 million per year, and individuals worth in excess of $100,000,000.

Doug Short states: "**In real terms, households in the bottom quintile earned less in 2009 than they did in 1989—twenty years earlier."** i.e. the growth in household expenses exceeded the income growth of those households in the lowest quintile. While **"In the top quintile, the annualized income growth increased… 84% during the same period."** "The lack of sustained growth in household incomes is no doubt a major factor in the general decline in consumer confidence over the past decade." [1] (Figure 1)

Figure 1:

Real (Inflation-Adjusted) Mean Household Income by Quintile and Top 5%



Senator Bernie Sanders, (Independent from Vermont), in a Congressional Joint Economic Committee meeting on October 4, 2011, addressed this issue and noted that **the top 1% of Americans earn more income than the bottom 50%, and the wealthiest 400 Americans own more wealth than the next 150 million Americans combined.** *FED Chairman Ben Bernanke, in reply, observed that the wealth disparity has been increasing since the 1970's and that it is a real concern and something that we should address as a society.*

(For more on this subject, please read: **"**Wealth, Income, and Power", by G. William Domhoff[2])

The U.S. has faced the issue of growing wealth disparity throughout its history. Three of our nation's most outstanding leaders addressed this problem in their own times.

---

[1] Short, Doug. "U.S. Household Incomes: A 43-Year Perspective." www.dshort.com 13 Sep. 2011.
Online at : http://advisorperspectives.com/dshort/updates/Household-Income-Distribution.php

[2] Domhoff, William G. "Wealth, Income, and Power." September 2005. Sociology Dept., University of California at Santa Cruz, July 2011.
Online at: http://sociology.ucsc.edu/whorulesamerica/power/wealth.html

Thomas Jefferson, (1743-1826)

> *The property of this country is absolutely concentrated in a very few hands... I am conscious that an equal division of property is impracticable. But the consequences of this enormous inequality producing so much misery to the bulk of mankind, legislators cannot invent too many devices for subdividing property...*[3] (Jefferson 1785)

Theodore Roosevelt, (1858-1919)

> *The absence of effective state, and, especially, national, restraint upon unfair money getting has tended to create a small class of enormously wealthy and economically powerful men, whose chief object is to hold and increase their power...*[4] (Roosevelt 1910)

Dwight Eisenhower, (1890-1969)

> *In the councils of government, we must guard against the acquisition of unwarranted influence... The potential for disastrous rise of misplaced power exists and will persist.*[5] (Eisenhower 1961)

The two solutions championed by these exceptional Republican Presidents were the graduated income tax and the inheritance tax.

> *Another means of silently lessening the inequality of property is to exempt all from taxation below a certain point, and to tax the higher portions of property in geometrical progression as they rise.* (Jefferson 1785)

> *… I believe in a graduated income tax on big fortunes, and in another tax which is far more easily collected and far more effective -- a graduated inheritance tax on big fortunes, properly safeguarded against evasion and increasing rapidly in amount with the size of the estate...*
> *The inheritance tax... is both a far better method of taxation, and far more important for the purpose of having the fortunes of the country bear in proportion to their increase in size a corresponding increase and burden of taxation.* [6] (Roosevelt 1907)

Republican President Theodore Roosevelt, in particular, was concerned that a wealthy **oligarchy** was being perpetrated upon the people of the United States. In order to save the democracy, Roosevelt strongly believed that wealth must be redistributed. If the concentration of wealth were allowed to continue, he believed, the democracy would be lost.

Are these great thinkers incorrect? *Or is it that those less learned and less capable individuals, including a number of current members of Congress (and some Presidential candidates), who argue for flat taxes and low tax rates for all, simply do not comprehend the <u>compounding effect of wealth</u>, and the wealth disparity it creates?*

The issue of wealth disparity was addressed, in the past, by implementing the following:

- 1798 - The Estate and Gift Tax (modernized in 1916)
- 1913 - Income tax[7]

By 1970 the U.S. had one of the least stratified and most prosperous civilizations in history.

Progressive taxation has had more than just social benefits. President Eisenhower <u>defended a highest tax rate of 91%</u> for economic reasons, saying:

---

[3] Jefferson, Thomas. "Thomas Jefferson to James Madison, 28 Oct. 1785." Ed. Julian P. Boyd et al. <u>The Founders' Constitution</u> Vol. 1, Ch. 15, Doc. 32. The University of Chicago Press, 1987. Online at: http://press-pubs.uchicago.edu/founders/documents/v1ch15s32.html

[4] Roosevelt, Theodore *"New Nationalism"* 1910

[5] Eisenhower, Dwight. Farewell Address, 17 Jan. 1961.

[6] Roosevelt, Theodore. Message to Congress, 1907

[7] The 16th Amendment

> *Every dollar spent by the government must be paid for either by taxes or by more borrowing with greater debt. The only way to make more tax cuts now is to have bigger and bigger deficits and to borrow more and more money. Either we or our children will have to bear the burden of this debt. This is one kind of chicken that always comes home to roost. An unwise tax cutter, my fellow citizens, is no real friend of the taxpayer.*[8] (Eisenhower 1954)

During his tenure as President, **Eisenhower successfully utilized the graduated income tax to balance the budget, and did so in a growing and expanding economy.**

Over the last three decades we have seen unprecedented increased government spending and significant tax cuts – especially for the wealthy. The results are massive budget deficits and, due to the compounding effect of wealth, a growing disparity in wealth and declining quality of life for our less fortunate citizens. These results are neither fiscally nor socially sustainable.

Warren Buffett, contemporary investment genius and the "Oracle of Omaha," wrote in an Op-Ed for the New York Times:

> *But for those making more than $1 million — there were 236,883 such households in 2009 — I would raise rates immediately on taxable income in excess of $1 million, including, of course, dividends and capital gains. And for those who make $10 million or more — there were 8,274 in 2009 — I would suggest an additional increase in rate.* ***My friends and I have been coddled long enough by a billionaire-friendly Congress. It's time for our government to get serious about shared sacrifice.***[9]

Note: A hedge fund manager earning $1billion per year has approximately **$832 million** of discretionary savings/spending per year. (Congress passed a special law taxing hedge fund manager's earnings as capital gains at only 15%)

The critical issues before our citizens include: what type of government shall we choose to live under going forward? Will it be a *plutocracy, oligarchy*, or a *democracy?* And what is the most appropriate and fairest way to provide for our revenue needs as a society?

We must ask ourselves if we can afford to ignore the lessons of our nation's history, and the wisdom of our most capable thinkers, past and present. Will we allow future tax policies to continue to facilitate the accumulation of wealth in the hands of the few, or will we choose to devise a more balanced approach that allows for the opportunity of incentive, personal initiative, and wealth accumulation for all?

> ***The man of great wealth owes a peculiar obligation to the State, because he derives special advantages from the mere existence of government.*** *Not only should he recognize this obligation in the way he leads his daily life and in the way he earns and spends his money, but it should also be recognized by the way in which he pays for the protection the State gives him.*
> Teddy Roosevelt: April 14, 1906

- *Roger L. Johnson*

[8] Pres. Eisenhower, Dwight D. "Address on the Tax Program" 15 Mar. 1954

[9] Buffett, Warren. "Stop Coddling the Super-Rich, NY Times 14 Aug. 2011
Online at: http://www.nytimes.com/2011/08/15/opinion/stop-coddling-the-super-rich.html