

As We See It

The art of taxation consists in so plucking the goose so as to obtain the largest amount of feathers with the least amount of hissing.

- Jean Baptiste Colbert
Finance Minister for Louis XIV

Civilization requires government, and government must be funded. That means taxes. Paying for government was the first—and for thousands of years—the only purpose of taxation. Later the purpose included wealth redistribution.

In the early days of the United States, the government was funded by tariffs—or duties on imported goods—which was a regressive tax as rich and poor alike had to pay the tax in the form of higher prices.

But proceeds from tariffs were not enough. To gain more revenue, Congress passed excise taxes on carriages, distilled spirits, sugar, salt, and other items. Other taxes such as taxes on the value of houses and land eventually followed. The excise taxes and property taxes were considered a decent proxy for taxing wealth.

The system muddled along until the Civil War. Facing a huge revenue crisis in 1861, Union leaders first increased tariff and excise taxes. In a bid to bolster fairness, they also enacted a new federal property tax followed by the nation's first income tax. The act exempted the first \$600 of income, and income between \$600 and \$10,000—a very comfortable sum at the time—was taxed at 3%. Income over \$10,000 was taxed at 5%—raised to 10% in 1864. Congress let the income tax expire in 1872.

In 1894, Congress approved a new income tax, only to have the Supreme Court overturn it as unconstitutional the following year. The subsequent years saw an effort to adopt a constitutional amendment which would allow for an income tax. That amendment, the 16th, was passed in 1913. The tax was designed to affect only the wealthiest 1% of the population, and revenue from it was intended to permit the reduction of crushing protective tariffs and excise taxes that disproportionately burdened the poor and middle class by adding sharply to the prices of food, clothing, and other necessities.

The tax began with a rate of 1% on income over \$3,000 with a surtax of 6% on income over \$500,000. According to the Bureau of Labor Statistics inflation calculator, that \$500,000 would be \$11.5 million now. Today, roughly half of American families pay the personal income tax.

A review of the history of the income tax reveals two important facts. The rate of taxation started low and was focused on the wealthy. However, as government spending grew, the tax rate increased and the taxable base of payers broadened.

Along the way there was always *hissing* as taxes were added or increased, but the *hissing* today is probably the loudest ever. We can only hope that the plucking does not kill the goose.

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