



ELEANOR MILL

WELFARE REFORM FOR THE RICH

BY HARRY JOHNSON

"First there was the War on Poverty. Then there was the war on the poor."

~Chuck Wilder

As Gingrich and Clinton try to outdo each other in blaming the poor for the decline of America, they set about "reforming" the system of supports for poor children built up since LBJ's War on Poverty, by punishing the poor. Even the most liberal of reform measures continue to blame poor individuals for not 'making it'. No one questions the economic system which, without checks, eliminates jobs, benefits, security and well-being for American workers. Even fewer questions are raised about the system of direct benefits and tax breaks which constitute welfare for the rich.

Newt Gingrich's home district is Cobb County, Georgia, a wealthy Atlanta suburb which is notoriously inhospitable to blacks. Noam Chomsky notes that Cobb County receives more federal subsidies than any other suburban county in the U.S., except for Arlington, Virginia, which is effectively part of the federal government, and Brevard County, Florida, home of the Kennedy Space Center. "Cobb County's largest employer is Lockheed Aeronautical Systems, which is designing the F-22 advance tactical fighter and other military aircraft. Seventy-two percent of the (Cobb County) workforce are in white collar jobs in expanding areas of the economy like insurance, electronics, computers and trade -- all carefully tended by the 'nanny state'. It is remarkably easy for conservative entrepreneurial values to flourish while one is feeding happily at the public trough."

If economics is "the dismal science", tax policy seems to be the most bleak of its elements. It is, however, imperative that we understand some of its elements if we are to reform welfare for the rich. A recent book by Ralph Estes, resident fellow of the Institute for Policy Studies, called *Who Pays? Who Profits?: The Truth About the American Tax System*, is helpful.

First, a couple of definitions:

~**Progressive Tax:** One that is fair and is proportionate to ability to pay. People in lower income brackets pay lower rates and those in higher brackets pay higher rates. Those who can pay more should pay more. The pain of the tax bite should be felt equally.

~**Regressive Tax:** "...takes a higher percentage of a taxpayer's income at lower income levels. Sales taxes, for example, are generally regressive. People with low incomes have to spend most or all of their income on living expenses, so they pay sales taxes on nearly everything they spend (unless exemptions for food or medicine are allowed)." (Estes)

Example -- A family with income of \$15,000, all of which is spent on living expenses subject to 6% sales tax. They pay \$900, or 6% of their income in sales tax.

-- A family with income of \$500,000, which spends \$100,000 on living expenses (and are living pretty high on the hog). They pay \$6,000 in sales tax, 1.2% of their income.

The rate (percentage) goes up as the income goes down; that's regressive taxation.

Income Tax on Individuals

The federal income tax used to be more fair, more progressive. Through the 1950s to 1964, the highest income bracket was taxed at 91%. In 1964 it was dropped to 77%, and stayed around 70% until 1981. In 1986 the top rate was still 50%. The *Tax Reform Act of 1986* (spearheaded by Oregon Senator Bob Packwood) cut the top rate to only 28%, for all income above \$50,000. In 1995 the top rate is up to 39% for income above \$250,000.

So, the first step in welfare reform for the rich is to restore some progressivity to the income tax. *Raise income taxes on the wealthy.*

Income Tax on Corporations

Another thing we need to realize is that tax breaks to one group increase the burden on the rest of us. When corporations get a tax break, that money must be made up by middle and low income taxpayers.

Corporations are heavy users of public services. Estes lists estimates of the costs to the public of corporate activity:

1. Injuries, accidents, illness, harassment, discrimination...
2. Price fixing, monopolies, deceptive advertising, product injuries and illness -- cancer...
3. Air pollution -- acid rain, damage, health costs...
4. Water pollution -- damage to fishing, recreation, health...

5. Hazardous waste -- disposal, cleanup...
6. Defense contract overcharges...
7. Income tax fraud...

8. Violations of federal regulations...
9. Bribery, extortion, kickbacks, other crimes...

Estes' estimate of the total cost to the public of private corporate activity is \$2.5 trillion per year. This doesn't include the billions we are spending bailing out failed savings & loans and banks. These costs are borne by workers, consumers, communities and taxpayers.

In spite of these increasing costs to individual citizens, the burden of taxes has been shifting from corporations to individuals. In 1950 corporations paid 39% of U.S. income taxes and individuals paid 61%. This year corporations will pay about 10% and individuals 90%. Many corporations are able, with clever accounting, to avoid paying income tax at all, even though they control billions of dollars of assets and pay their executives millions of dollars in compensation.

Step 2: Raise the income tax on corporations. We should raise these individual and corporate income tax rates back to where they were before the 1980s, when the income tax was more fair to everyone and did not noticeably inhibit incentive and business was overall more healthy.

Wealth Tax

An annual tax of individuals and corporations on the value of their assets -- real estate, securities and business assets above liabilities. Eight of the industrial countries have a wealth tax. Japan and Switzerland raise the largest part of their tax revenue from wealth taxes. With an exemption of \$500,000 per person to allow for home equity, savings for kids' education and a fair amount for a rainy day, a 4% wealth tax would, according to Estes, raise about \$225 billion per year (about one-half of income tax revenues). This would make it more difficult for individuals and corporations to pay no taxes in a given year, as some continue to do.

Inheritance Tax

Most of the wealthy got that way by luck or by inheriting money, not by harder work or superior talent. Inheriting large sums of money can be worse for the character than being raised by a single mother on ADC. Studies show that people who inherit money are generally less productive than those who earn it.

We should increase taxes on inheritance substantially after allowing a reasonably generous exemption of, say, \$500,000.

Capital Gains Tax

Almost all capital gains come from the sale of stocks and nonresidential real estate. 93% of the people don't have any capital gains. 72% of capital gains go to the wealthiest 1% of the population.

Capital gains taxes, taxes on profits from investments, are drastically different from taxes on wages. If you are employed, taxes are withheld before you ever see the money you earned. A person with capital gains can control when they will be taxed by deciding if and when to sell stocks and property. This is a decided advantage for earnings on investments over earnings from wages.

In the 1960s, when the income tax rate for the top bracket was 91%, capital gains were taxed at only 25%. In 1981 the capital gains tax went down to 20%, while the top income tax rate went down to 50%. The capital gains tax rate was raised to the level of ordinary income in 1986. In 1995 the capital gains rate remains at 28%, while the top income tax bracket is 39%. I burden you with this brief history because it gives us a real life laboratory for evaluating the effects of raising and lowering the capital gains tax.

Gingrich, Dole & Co., as well as Bill Clinton, want to cut the capital gains tax rate. They claim that a cut would stimulate investment, create jobs, encourage savings and revive the economy. Some even argue that a cut would actually raise revenue as investors are encouraged to sell assets with accrued capital gains.

Would a capital gains tax cut stimulate investment and job creation? The Congressional Research Service reports that, "the effect (of the proposed capital gains tax cut) on the rate of return to new investments would be extremely small and the effect on output in the economy would be negligible." *Business Week* magazine, citing a study by the chief economist of the House Budget Committee, reports that "investment in business equipment rose after capital gains tax increases and fell after capital gains tax decreases."

During the two years after the 1981 capital gains cut to 20%, "the annual growth rate (of the economy) was only 1% -- 2.5 percentage points below prior growth... (and) unemployment ballooned from 7.3% to 9.3%.... In fact, improved economic growth has typically followed hikes -- not cuts -- in the capital gains tax." (*Business Week*)

How about encouraging savings and investment? Professor Alan Blinder, writing in *Business Week*: "Tax incentives for saving and investment proliferated in the 1980s, and almost all failed.... There was no substantial rise in the share of gross domestic product saved or invested, and there was no burst of productivity growth."

Estes again, in an Institute for Policy Studies briefing paper (October 1992):

"The capital gains tax is largely irrelevant to a business decision to invest in new equipment, since business rarely realizes gains on disposal of such assets.

"Business will not invest in productive facilities if demand does not exist for its products, no matter what the level of capital gains taxes."

If a capital gains tax cut would not lead to more jobs, more investment, stimulate the economy or increase savings significantly, what would it do?

Estes:

"A capital gains tax cut would increase the inequality of income distribution in the U.S. that has seen the rich getting richer and the poor getting poorer, and now places our nation 20th out of 21 industrialized nations in rankings of income equality.

"...would mean taxing the fruits of labor (even) more heavily than the fruits of wealth.

"...would send a message that investments in capital should be encouraged over investments in people."

A capital gains tax cut is simply an increase in welfare for the very rich. This income should be taxed just like any other income; special treatment for the rich is unjustifiable.

Corporate Foreign Tax Credit

This jewel in the welfare crown works as follows:

A corporation based in San Diego pays taxes to the state of California. These taxes are considered deductions on the tax form just like other costs of doing business. A deduction is a subtraction from the amount of income on which the tax bill is calculated.

Now if this corporation moves across the border to Tijuana and pays taxes to Mexico, these taxes have turned into tax credits which are deducted from the bill itself. Corporations are thus encouraged by foreign tax credits to move out of the country. This should be stopped.

Some other jewels in the crown:

Earnings ceiling on Social Security withholding:

This ceiling of \$60,000 ruthlessly increases the regressivity of our tax system. For 1994, 6.2% of your income is withheld for Social Security taxes. (Your employer also pays 6.2% for you. Self-employed people must pay the whole 12.4%.) This tax is withheld on earnings up to \$60,000. Anything earned above that amount is not taxed for Social Security at all. All income should be taxed for Social Security.

Social Security and Medicare are paid to all retirees, regardless of their other income. Many retirees feel that they "have it coming," that they are only receiving what they put into the system over their working years. The truth is that retirees get back everything they paid in, plus interest, in seven years. After that they are on welfare. Social Security and Medicare benefits should be means-tested. The rich don't need them.

Deductions for mortgage interest:

This also is sharply regressive. Buyers of expensive homes, including second and third homes, receive much more of a benefit than buyers of less expensive homes, working people. Renters get no benefit at all. This deduction should be eliminated.

Deductions for business meals and entertainment:

Allowing business people to deduct 50% of the cost of business meals at expensive restaurants, while eliminating school lunches for poor children and milk and formula for poor infants, seems to exemplify the Republican agenda. This deduction should be eliminated.

These changes in the tax system to make it more progressive and in line with the rest of the industrialized world, are the necessary first steps in reforming welfare for the rich.

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