by Bruce Bartlett

The Case for Ending the Capital Gains Tax

The Treasury Department's recent tax proposals call for taxing capital gains at ordinary rates (although indexing such gains for inflation). Those who oppose preferential treatment for capital gains have traditionally based their arguments on grounds of equity. Preferential treatment, they argue, allows wealthy individuals to escape paying their fair share of taxes.

But taxing capital gains to investors, even at a low rate, while also taxing the return on capital, represents double taxation. Inasmuch as an increase in share price, for example, reflects the anticipation of higher future dividends, the increase in capital is not distinct from the increase in income. Taxing capital gains means taxing capital, and this discourages the formation and mobility of capital, thereby reducing the standard of living of all Americans.

Consider the economic consequences of the 1978 and 1981 reductions *in capital gains tax rates. New issues of corporate common stock increased threefold between 1978 and 1982. New commitments to venture capital funds increased from just $39 million in 1977 to $11.5* billion *by the end of 1983. The inflation-adjusted market value of corporate equities, which had fallen 24 per cent in the five years prior to 1978, rose 46 per cent in the five years following.*

The real question is, why not eliminate capital gains taxation altogether?

THE TAXATION OF capital gains is among the most controversial issues in the field of public finance. It is likely to become even more controversial as a result of the Treasury Department's recent tax reform proposal, which would have capital gains taxed at ordinary income rates. The maximum marginal tax rate on long-term capital gains would rise from the current 20 per cent to 35 per cent but, because of indexing, the tax would apply only to that portion of the gain which exceeds the inflation rate.[1]

There is a strong case to be made for capital gains tax reform; the question is, however, whether this is the kind of reform needed. Why not abolish the capital gains tax altogether?

1. Footnotes appear at end of article.

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Reduction in Rates

The Tax Reform Act of 1969 sharply increased the maximum tax rate on capital gains, in response to reformers who argued that preferential treatment for capital gains allowed many wealthy individuals to escape paying their "fair share" of taxes. During the 1976 presidential campaign, Jimmy Carter repeatedly asserted that he believed capital gains should be treated no differently from ordinary income.[2] The Treasury Department subsequently proposed a plan that would abolish special treatment of capital gains.

The hearings on the Carter tax reform proposal ended up persuading Congress that what was really needed was more preferential treatment for capital gains, not less. Key testimony was offered by Ed Zschau, representing the American Electronics Association. Zschau (who later became a member of Congress from the Silicon Valley area of California) presented compelling evidence that the increase in the capital gains tax in 1969 had severely hurt high-tech companies.[3] Congress also became convinced that the capital gains tax rate was so high that it was actually reducing government revenue below the level a lower tax rate would have yielded.

In 1978 Congress cut the maximum capital gains tax from about 49 per cent to 28 per cent. The maximum federal income tax rate on ordinary income at the time was 70 per cent. When that maximum was cut to 50 per cent by the 1981 tax bill, the rate on capital gains declined to 20 per cent. The evidence strongly suggests that this cut in the capital gains tax did indeed have all the positive effects its proponents had predicted.

Economics of Capital Gains Taxes

The Carter administration strongly opposed the reduction in capital gains tax rates in 1978.[4] Criticism focused on the fact that most capital gains are realized by high-income individuals and households. In 1982, for example, 54 per cent of all long-term capital gains (in excess of short-term capital losses) accrued to taxpayers with incomes over $100,000.[5] A cut in the capital gains tax rate was viewed as a give-away to the rich.

Wealthy individuals do benefit from a lower tax rate on capital gains. Brookings Institution scholar Joseph Pechman has estimated that, if capital gains were taxed at ordinary rates, individuals with incomes above $1 million would pay 16.4 per cent more in federal income tax in 1985.[6] This assumes, of course, that these investors would choose to take their capital gains and pay the higher tax rate. They could simply hold on to their assets, rather than selling them. Raising capital gains taxes, rather than increasing federal tax revenues, may reduce them.

Mobility of Capital

This important characteristic of capital gains taxes is known as the "lock-in" effect. Capital gains are taxed only when realized. No taxable income results if the asset is never sold, even if it has increased substantially in value. A higher tax rate on capital gains thus encourages investors to hold on to assets that have appreciated in value. The higher the tax rate on capital gains, the more pronounced this effect will be.[7]

The lock-in effect has important implications for the economy, as well as for federal revenues. Capital needs to be mobile to be effective. If capital is locked into particular investments because of the capital gains tax, the whole economy suffers. Plants are not built; jobs are not created; goods are not produced. Economist Roy Webb made this point in a recent article:

> "Investment is facilitated by financial intermediation, through which people with productive uses for capital indirectly acquire funds from others who have the desire and the ability to substitute future for current consumption. . . . An efficient system of financial capital intermediation directs funds to the most productive investments. Thus, the more efficient the system of intermediation, the more benefit accrues directly to savers and capital users, and indirectly to workers (whose marginal product is raised) and consumers (who see an increased supply of commodities).[8]

The 1970s witnessed a dramatic reduction in the mobility of capital. By 1978, 39 per cent of all household wealth was tied up in tangible assets, compared with 29 per cent in the mid-1960s. At the same time, holdings of financial assets, especially corporate equities, declined. According to the Federal Reserve, corporate equities as a share of household financial assets fell from 35.3 per cent in 1968 to just 15.6 per cent in 1978.[9]

Inflation is commonly viewed as the primary cause of this development. But inflation must be viewed within the context of its impact on the capital gains tax. According to a 1979 study by Harvard economists Martin Feldstein and Joel Slemrod, individuals paid $500 million in excess federal tax in 1973 because paper capital gains were not adjusted for inflation. Their research shows that, in that year, individuals realized, and paid taxes on, some $4.5 billion in nominal capital gains on corporate stock. When adjusted for inflation, this $4.5 billion "gain" became a $1 billion capital loss.[10]

If investors know that much, if not all, of any capital gain they might report is the result solely of inflation, not any real gain, they are going to be less willing to buy or sell corporate stock.[11] They will prefer to invest in assets, such as paintings and real estate, which produce a tax-free "psychic" income, thus locking their income into illiquid, nonfinancial and nonproductive assets.

Feldstein has carefully analyzed the effect of capital gains taxation on the sale of common stock. He concluded that the capital gains tax at pre-1978 rates was high enough to discourage significant amounts of stock selling and predicted that a reduction in the capital gains tax rate would increase federal revenue.[12]

Impact on Federal Revenue

Congress said explicitly in 1978 that it expected the capital gains tax cut to increase federal revenue.[13] The available evidence suggests that Congress was right, although the Treasury Department never produced its study of the tax cut required by section 555 of the Revenue Act of 1978.[14] The Treasury Department's consultant on the issue, Professor Gerald Auten of Bowling Green State University, has concluded that by 1981 the tax cut had resulted in $2.5 billion in capital gains tax revenue that would not have been received under the pre-1978 tax rate.[15] Available data from the Internal Revenue Service (IRS), presented in Table I, indicate that realizations of capital gains have increased substantially since 1978, especially among the wealthy. The latest Treasury Department estimates, presented in Table II, indicate that capital gains tax revenues increased over 59 per cent between 1978 and 1982. Preliminary data for 1983 show that capital gains from the sale of capital assets (net of capital losses) increased to $45.4 billion, a rise of 32 per cent over tax year 1982.[16]

Even if the tax cut does not result in increased capital gains tax revenues, total tax revenues should rise as the tax cut stimulates investment, creating higher profits and larger payrolls. Remember, however, that increasing tax revenues was not the original justification for the tax cut. The tax cut was meant to stimulate investment, especially risk investment.[17]

On this score, the tax cut would appear to be a huge success, regardless of its revenue effects. According to George Gilder, the capital gains tax cut led to substantial new commitments to venture capital funds, which increased from just $39 million in 1977 to $11.5 billion by the end of 1983. Venture capital has, of course, provided the principal fuel for the entrepreneurial advances that have occurred since 1978 in computers, biotechnology and many other high-tech industries.[18]

Effect on Business Formation

The capital gains tax cuts of 1978 and 1981 improved the ability of firms to raise funds through equity offerings. The average daily volume of transactions on the New York Stock Exchange, for example, increased from 28.6 million shares in 1978 to over 85 million shares in 1983; according to Professor Slemrod, much of this increase is directly attributable to the capital gains tax cut.[19] In addition, as Figure A shows, new issues of corporate common stock have increased threefold since the 1978 tax cut (with significant spurts occurring directly after both the 1978 and 1981 tax reductions).

The increase in new issues and volume, together with the increase in potential after-tax returns to investors, has contributed to a sharp

Table I Long-Term Gains Net of Long-Term Losses (billions of dollars)

Adjusted Gross Income Class	*1978*	*1982*	*Percentage Change*
0–$25,000	9.7	10.2	5.2
$25,000–$50,000	9.0	8.5	−5.5
$50,000–$100,000	6.6	10.2	54.5
$100,000–$500,000	8.6	21.3	147.7
Over $500,000	3.7	24.5	562.2
Total	37.7	74.7	98.1

Source: Internal Revenue Service, *Statistics of Income, Individual Income Tax Returns*, 1978 and 1981.

Table II Taxes paid on Capital Gains Income (billions of dollars)

1982	$12.9
1981	12.7
1980	12.5
1979	11.7
1978	9.3
1977	8.1

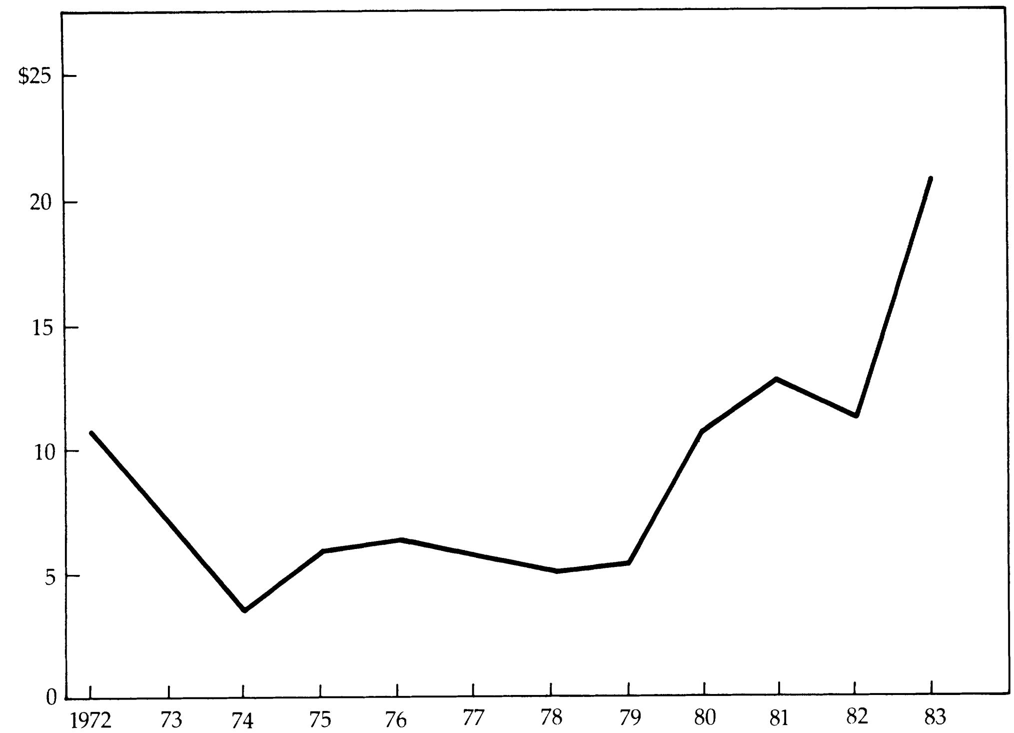
Source: Department of the Treasury, Office of Tax Analysis, March 5, 1985.

Table III Market Value of Corporate Equities (billions of dollars)

Year	*Current Dollars*	*1972 Dollars*
1983	2,151.5	999.1
1982	1,810.5	873.0
1981	1,568.5	801.9
1980	1,635.6	916.7
1979	1,230.7	753.1
1978	1,028.3	683.6
1977	995.4	710.7
1976	1,051.9	794.8
1975	892.5	709.5
1974	676.9	588.2
1973	948.1	896.6
	Percentage Change	
1973–78	+8.5%	−24.0%
1978–83	+109.0%	+46.0%

Source: Federal Reserve, Flow of Funds Accounts.

Figure A New Issues of Corporate Common Stock (billions of 1972 dollars)



Source: *Economic Report of the President, 1984,* p. 322.

rise in the market value of corporate equities. As Table III shows, the market value of corporate equities, in inflation-adjusted dollars, fell 24 per cent in the five years prior to the capital gains tax cut and rose 46 per cent in the five years following.

Since 1979, proprietors' equity in noncorporate business—generally small businesses—has increased 185 per cent, compared to a decline of 16.7 per cent between 1975 and 1979 (see Table IV). This suggests that many more small businesses have been formed, and succeeded, as a result of the tax cut. And according to studies by Professor David Birch at MIT, small newly established firms create the vast majority of new jobs in the U.S.[20]

Table IV Proprietors' Equity in Noncorporate Business (billions of dollars)

Year	*Current Dollars*	*1972 Dollars*
1984	53.3	23.8
1983	44.0	20.4
1982	16.1	7.8
1981	18.9	9.7
1980	28.0	15.7
1979	15.5	9.5
1978	16.4	10.9
1977	19.2	13.7
1976	17.2	13.0
1975	14.4	11.4
	Percentage Change	
1975–79	+7.9%	−16.7%
1979–84	+243.9%	+150.5%

Source: Federal Reserve, Flow of Funds Accounts.

Equity and Tax Neutrality

Many policymakers seem to ignore the economic benefits resulting from capital gains tax reductions; they argue that capital gains should, in the interest of fairness, be taxed the same as ordinary income.[21] Some recent tax proposals, such as the Bradley-Gephardt bill, call for the elimination of special treatment for capital gains in the context of overall tax reform. Because these proposals also advocate a reduction in marginal tax rates, some proponents of lower taxes have mistakenly come to believe that the impact on the economy of eliminating preferential tax treatment for capital gains would be negligible—a small price to pay for reducing marginal income tax rates. But if the benefits of the 1978 and 1981 capital gains tax cuts were to be reversed, the effect could be disastrous, for both capital investment and jobs.

The equity argument is, moreover, spurious. Taxing capital gains to investors, even at a low rate, while also taxing return on capital represents a double taxation of capital. It is indefensible in terms of fairness and seriously detrimental to the economy.

The equity issue is a long-standing one. H. C. Simons strongly opposed the preferential treatment for capital gains initiated by the Revenue Act of 1921. (Prior to 1913, of course, there was no income tax, and from 1913 to 1921, capital gains were taxed as ordinary income.[22]) Simons rested his entire case for full taxation of capital gains on grounds of equity: "The main and decisive case for inclusion of capital gains" in income, he wrote in 1938, "rests on the fact that equity among individuals is impossible under an income tax which disregards such items."[23]

There are, of course, other generally accepted principles of taxation aside from equity, such as efficiency and simplicity, and different forms of equity, such as "horizontal" equity between those with equal incomes derived from different sources and "vertical" equity between those with different incomes. Although full taxation of capital gains may satisfy one tax principle or one notion of equity, it may seriously violate others.

Furthermore, tax theorists have different definitions of income, hence different ideas about a properly designed tax policy. In Great Britain and many European countries, for example, income has long been defined as a regular and more or less predictable flow; windfalls and one-time payments have not been considered income elements. As the distinguished British economist Sir John Hicks put it in *Value and Capital:*

> "If a person expects no change in economic conditions, and expects to receive a constant flow of receipts, the same amount in every future week as he receives this week, it is reasonable to say that that amount is his income. But suppose he expects to receive a smaller amount in future weeks than this week (this week's receipts may include wages for several week's work, or perhaps a bonus on shares), then we should not regard the whole of his current receipts as income; some part would be reckoned to capital account."[24]

The British long held that capital gains were not income (except for professional traders), hence were not subject to taxation. They now use a system similar to that in the U.S., whereby capital gains are taxed at lower rates than ordinary income.[25] Many other countries, however, including Belgium, Italy, Japan, the Netherlands, West Germany and Australia, do not effectively tax long-term capital gains.[26]

Capital Gains and Income from Capital

It seems to be commonly accepted, in the U.S. at least, that capital gains are income; the only question is at what rate they should be taxed.[27] In earlier years, however, the income status of capital gains was hotly debated, and it remains the key question that must be resolved before anyone can even begin to determine the proper tax rate for capital gains.

Irving Fisher held that capital gains are not income. In his model, capital and income are interchangeable. Capital, by definition, produces a flow of income, and flows of income must necessarily be associated with a stock of capital. For example, if one were to issue a piece of paper promising the holder $100 per year in perpetuity, and if the prevailing interest rate were 5 per cent, then that piece of paper would have a capital value of $2,000. One might say that, at a 5 per cent interest rate, $100 in income per year is exactly the same as a $2,000 stock of capital. Similarly, wages may be viewed as a return to human capital.[28]

In this context, a tax on capital gains, when imposed in addition to a tax on the returns to capital—interest, dividends, or even wages—constitutes double taxation. Since human capital is never taxed, the problem arises only in the case of financial or tangible capital. The result is that the total tax on capital, hence its cost to entrepreneurs, can reach very high levels.[29]

Consider a share of ownership in some asset such as a corporation. The value of that share is generally the present value of the dividends associated with it. If the corporation were to become more profitable, its share price would rise—but the increase merely reflects the anticipation of higher dividends in the future. The increase in capital, in other words, is not distinct from the increase in income. To tax both the dividends *and* the increase in share price is to tax capital gain as well as income.[30]

Lawrence Seltzer of Wayne State University summarizes the position as follows:

> "To tax capital gains as income, it is argued, puts a double tax on the recipient: first, on the capital value of future incomes; then, on the incomes themselves as they are received. A man who reinvests a capital gain of $50,000 will be subject to income tax on the future incomes he obtains from the gain; and these incomes constitute his real gain. To tax him also on the principal value of the gain itself is to tax him twice."[31]

In the interest of tax neutrality, either the capital or the return to capital should be taxed, not both.

Time to Eliminate the Tax

To put the matter simply: Gains from the sale of long-term assets do not come from current production and are not current income. They merely represent the conversion of an asset from one form into another. Congress already recognizes this principle with regard to the sales of homes, as Hoover Institution economist Roger Freeman notes. Under current law, any capital gain arising from the sale of a primary residence, provided it is reinvested in another primary residence of equal or greater value within 24 months, is free of tax. "It can be argued," Freeman says, "that there is no reason to treat a 'rollover' in other types of investment differently—except the political reason that millions sell their houses for more than they paid for them (or plan or hope to) but only one taxpayer in 14 enjoys other types of capital gains."[32]

Martin Feldstein has revived the Fisherian model and argued, accordingly, that income from capital should be free of taxation. Existing taxes on capital, he points out, violate the principle of horizontal equity, which holds that individuals who would be equally well off in the absence of a tax should be equally well off if a tax exists. Indeed, he favors abolishing the income tax entirely and substituting a progressive consumption tax. Such a tax system, by definition, would not tax capital gains until such gains were consumed:

> "The accumulated wealth will be taxed whenever it is used to finance personal consumption. Moreover, if it is given or bequeathed to others, it will be subject to the gift and estate taxes and then, when it is spent, to a further tax on consumption. I find it difficult to understand why the critics are worried more about the accumulation of new wealth within individual lifetimes under a consumption tax than about the untaxed consumption supported by inherited wealth under the current income tax."[33]

Feldstein, like Fisher, essentially equates income with consumption. Income is not really income in an economic sense unless it is consumed. Wealth and capital should not be taxed in the process of accumulation because, so long as they are not converted into consumption goods, they are not income. In their model, a consumption tax is an income tax, whereas what we call an income tax today is, to a large extent, a tax on capital.

In short, although capital gains—realized or not—clearly represent added wealth, they do not represent income. Taxing capital gains means taxing capital, and this discourages the formation and mobility of capital, thereby reducing the standard of living of all Americans. If the concern is the possibility of increasing inequality in the distribution of wealth, then a consumption tax provides a more egalitarian answer than a capital gains tax.

Conclusion

The case against the capital gains tax appears strong on both economic and equity grounds. There are legitimate reasons for going further than just advocating a lower rate or indexing capital gains, as the Treasury Department has proposed, and strong reasons for opposing its recommendation that the partial exclusion of long-term capital gains be ended. Capital gains should be entirely free of tax.

The vast bulk of capital gains are already entirely free of capital gains tax. Capital gains on the sale of homes by individuals are almost never taxed, and most capital gains on corporate equities are realized by financial institutions trading on behalf of pension funds, which again are not subject to the capital gains tax. Also, because capital gains are harder for the IRS to locate than other sources of income, capital gains taxes are often evaded. For these and other reasons, some economists have suggested that the capital gains tax is virtually a voluntary tax.[34]

Rather than the tinkering proposed by the Treasury Department, it is time for the administration to adopt a bold approach and take a significant step toward tax neutrality by eliminating the capital gains tax. ■

Footnotes

1. U.S., Department of the Treasury, Office of the Secretary, *Tax Reform for Fairness, Simplicity, and Economic Growth* (Washington, D.C.: Department of the Treasury, November 1984), vol. 1, pp. 100–105.
2. On numerous occasions Carter said that one of his principal goals was to treat all income the same for tax purposes. See U.S., Congress, House, Committee on House Administration, *The Presidential Campaign 1976* (Washington: Government Printing Office, 1978), pp. 152, 158.
3. U.S., Congress, House, Committee on Ways and Means, *The President's 1978 Tax Reduction and Reform Proposals,* 95th Congress, 2nd session (Washington, D.C.: Government Printing Office, 1978), part 3, pp. 1307–1338. See also Robert J. Samuelson, "Making Life Difficult for Congress," *National Journal*, March 18, 1978, p. 437.
4. See Robert J. Samuelson, "Pounding the Carter Tax Proposal From All Sides," *National Journal*, May 13, 1978, pp. 757–759, and Editorial, "How to Unsoak the Rich," *New York Times*, May 19, 1978.
5. Internal Revenue Service, *Statistics of Income—1982, Individual Income Tax Returns* (Washington, D.C.: Government Printing Office, 1984), p. 46.
6. Joseph A. Pechman, *Federal Tax Policy*, 4th ed. (Washington, D.C.: The Brookings Institution, 1983), p. 360.
7. For a theoretical discussion, see Charles C. Holt and John P. Shelton, "The Lock-In Effect of the Capital Gains Tax," *National Tax Journal*, December 1962, pp. 337–352; and Jonathan A. Brown, "The Locked-in Problem," in U.S., Congress, Joint Economic Committee, *Federal Tax Policy for Economic Growth and Stability*, 84th Congress, 1st session (Washington, D.C.: Government Printing Office, 1955), pp. 367–381. For some empirical data, see Martin Feldstein and Joel Slemrod, "The Lock-in Effect of the Capital Gains Tax: Some Time-Series Evidence," *Tax Notes*, August 7, 1978, pp. 134–135; and Shlomo Yitzhaki, "An Empirical Test of the Lock-in Effect of the Capital Gains Tax," *Review of Economics and Statistics*, November 1979, pp. 626–629.
8. Roy H. Webb, "Taxing Capital Gains," Federal Reserve Bank of Richmond *Economic Review*, November/December 1980, p. 15.
9. *Balance Sheets for the U.S. Economy, 1945–83* (Washington, D.C.: Federal Reserve Board, Division of Research and Statistics, Flow of Funds Section, April 1984), series 702.
10. Martin Feldstein and Joel Slemrod, "Inflation and the Excess Taxation of Capital Gains on Corporate Stock," *National Tax Journal*, June 1979, pp. 107–118.
11. For data on the impact of inflation on financial and tangible assets, see Jack Hibbert, *Measuring the Effects of Inflation on Income, Saving and Wealth* (Paris: Organization for Economic Cooperation and Development, 1983).
12. See Martin Feldstein and Shlomo Yitzhaki, "The Effects of the Capital Gains Tax on the Selling and Switching of Common Stock," *Journal of Public Economics*, February 1978, pp. 17–36; and Martin Feldstein, Joel Slemrod and Shlomo Yitzhaki, "The Effects of Taxation on the Selling of Corporate Stock and the Realization of Capital Gains," *Quarterly Journal of Economics*, June 1980, pp. 777–791. See also Joseph Minarik, "The Effects of Taxation on the Selling of Corporate Stock and the Realization of Capital Gains: Comment," *Quarterly Journal of Economics*, February 1984, pp. 93–110; and Martin Feldstein, Joel Slemrod and Shlomo Yitzhaki, "The Effects of Taxation on the Selling of Corporate Stock and the Realization of Capital Gains: Reply," *Quarterly Journal of Economics,* February 1984, pp. 111–120.
13. U.S., Congress, Joint Committee on Taxation, *General Explanation of the Revenue Act of 1978* (Washington, D.C.: U.S. Government Printing Office, 1979), p. 252.
14. *Ibid.*, p. 320.
15. Gerald E. Auten, "Capital Gains: An Evaluation of the 1978 and 1981 Tax Cuts," in Charls [sic] E. Walker and Mark A. Bloomfield, eds., *New Directions in Federal Tax Policy for the 1980s* (Cambridge, Massachusetts: Ballinger, 1983), p. 136.
16. Susan Hostetter and Dan Holik, "Preliminary Income and Tax Statistics for 1983 Individual Income Tax Returns," *The Statistics of Income Bulletin*, Winter 1984–85, p. 19.
17. The capital gains tax has long been known to have particular impact on entrepreneurial activity. See Thomas H. Sanders, *Effects of Taxation on Executives* (Boston: Division of Research, Graduate School of Business Administration, Harvard University, 1951), pp. 210–214.
18. George Gilder, *The Spirit of Enterprise* (New York: Simon & Schuster, 1984), p. 44.
19. *New York Stock Exchange Fact Book 1984*, p. 73; Joel Slemrod, "Stock Transactions Volume and the 1978 Capital Gains Tax Reduction," *Public Finance Quarterly*, January 1982, pp. 3–16. See also Michael K. Evans, *The Truth About Supply-Side Economics* (New York: Basic Books, 1983), pp. 163–185.
20. David L. Birch, "Who Creates Jobs?" *The Public Interest*, Fall 1981, pp. 3–14.
21. See, for example, Alan S. Blinder, "Capital Gains: Tax Them Like Income," *Washington Post*, July 22, 1982.
22. Anita Wells, "Legislative History of Treatment of Capital Gains Under the Federal Income Tax, 1913–1948," *National Tax Journal*, March 1949, pp.

12–32.
23. H. C. Simons, *Personal Income Taxation* (Chicago: University of Chicago Press, 1938), pp. 148–169.
24. J. R. Hicks, *Value and Capital,* 2nd ed. (New York: Oxford University Press, 1946), p. 172. See also Carl C. Plehn, "The Concept of Income, As Recurrent, Consumable Receipts," *American Economic Review,* March 1924, pp. 1–12.
25. J. A. Kay and M. A. King, *The British Tax System,* 2nd ed. (New York: Oxford University Press, 1980), p. 81.
26. *Comparison of Individual Taxation of Long and Short Term Capital Gains on Portfolio Stock Investments in Ten Countries* (New York: Securities Industry Association and Arthur Anderson & Co., 1980).
27. See Richard A. Musgrave and Peggy B. Musgrave, *Public Finance in Theory and Practice,* 2nd ed. (New York: McGraw-Hill, 1976), pp. 244–248; and Richard Goode, *The Individual Income Tax* (Washington: Brookings Institution, 1976), pp. 176–211.
28. See Irving Fisher, *The Theory of Interest* (New York: Macmillan, 1930), pp. 25–29; and Fisher, "Income in Theory and Income Taxation in Practice," *Econometrica,* January 1937, pp. 1–55.
29. See George N. Hatsopoulas, *High Cost of Capital: Handicap of American Industry* (Washington, D.C.: American Business Conference, 1983).
30. For further elaboration, see Richard E. Wagner, *Public Finance* (Boston: Little, Brown & Co., 1983), pp. 177–180; Norman B. Ture and Kenneth Sanden, *The Effects of Tax Policy on Capital Formation* (New York: Financial Executives Research Foundation, 1977), pp. 64–66; and Robert E. Hall and Alvin Rabushka, *Low Tax, Simple Tax, Flat Tax* (New York: McGraw-Hill, 1983), pp. 48–49.
31. Lawrence H. Seltzer, "Capital Gains and the Income Tax," *American Economic Review,* May 1950, p. 372.
32. Roger A. Freeman, *Tax Loopholes* (Washington, D.C.: American Enterprise Institute, 1973), p. 43.
33. Martin S. Feldstein, "Taxing Consumption," *The New Republic,* February 28, 1976, p. 17. Feldstein is referring to the fact that, under current tax law, all capital gains are "stepped-up" at death and, therefore, escape capital gains taxation (although they are still subject to the estate tax). Interestingly, the data suggest that taxes of all kinds have done little to change the distribution of wealth in the U.S. See Mervyn A. King, "How Effective have Fiscal Policies been in Changing the Distribution of Income and Wealth?" *American Economic Review,* May 1980, pp. 72–76.

    See also Martin Feldstein, "On the Theory of Tax Reform," *Journal of Public Economics,* 1976, pp. 77–104; Feldstein, "The Welfare Cost of Capital Income Taxation," *Journal of Political Economy,* April 1978, part 2, pp. S29–S51; and Michael A. Schuyler, *Consumption Taxes: Promises & Problems* (Washington, D.C.: Institute for Research on the Economics of Taxation, 1984),p. 28.
34. See Eugene Steuerle, "Is Income From Capital Subject to Individual Income Taxation?" *Public Finance Quarterly,* July 1982, pp. 282–303. It should be remembered that under current law even if the capital gains tax were abolished wealthy individuals with capital gains would still be subject to the minimum tax.