Tax Foundation's

Tax Review

MAY, 1970
Vol. XXXI, No. 5

The Tax Reform Act of 1969

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The Tax Reform (and *relief)* Act of 1969 stands out as one of the major laws of American tax history. Originating out of the desire to remove inequities, pressures for other changes, especially tax relief, gained force.* This paper explains the significance of some provisions and their probable effects. Such evaluations include judgements which are at least partially uncertain. Taxpayer responses, for example, remain to be disclosed by actions.

Only a few of the specific aspects of the law are even mentioned below. Each of two dozen or so might well receive pages of commentary. Major industries face new conditions. Almost every business faces higher taxes—leaving stockholders with less return on their investment, forcing consumers to pay higher prices, and altering managerial decisions. New burdens will fall on some individuals who have paid little or no tax; but for most persons income tax will be reduced somewhat.

Revenue Results

The temporary 10 percent surcharge on income tax (enacted in 1968 to help curb inflation and originally scheduled to expire in mid-1969) was continued to December 31, 1969. It was then replaced by a 5 percent surcharge for half of 1970. In one sense, the Act imposes an additional tax of 2.5 percent in 1970; in comparison with 1969, however, the surcharge is reduced. The extension of the auto and gasoline excise taxes may also be viewed in different ways. Does the new law continue "temporary" taxes, or does it add burdens otherwise scheduled to disappear?

Looking beyond, we find (Table 1) revenue results which are unquestionably much greater than any flowing from "tax reforms" as conceived early in 1969. The revenue estimates are based upon 1969 levels of income. The yield changes in the future will, of course, be greater.

(1) By eliminating the Investment Tax Credit, the law *adds* permanent burdens on business—around \$3.3 billion a year more tax. (2) Various changes classed as "tax reform" will bring \$1.2 billion *more revenue* in 1970 and \$3.3 billion a year more when permanently effective. Some will come from individuals directly. But much will, in the first instance, come from businesses. All of these burdens must eventually fall upon people—the customers, owners, or employees and suppliers of business firms. (3) *Revenue-reducing features* give individuals income *tax relief* of \$1.4 billion in 1970 and \$9.1 billion a year when fully effective. But because

This Issue in Brief

Some of the far-reaching implications of the 1969 Federal tax changes are analyzed by Dr. Harriss, including the relative amount of tax reform versus tax reduction.

Despite the greatly reduced taxes on lower income families, he notes that general rate reduction continues to be a major goal of proper tax reform.

Similarly, the elimination of the investment tax credit and other changes in business taxation will actually handicap rather than promote economic expansion, suggesting the unmet need for constructive reform in this area.

**A Tax Foundation report summarizes the legislative history and describes the many provisions of the final versions. That report does not attempt to explain the significance or evaluate the bill as a whole or its many features.*

this large relief becomes effective in stages the full significance is not yet widely appreciated.

(4) Social Security *outlays* are increased by $4.4 billion. This law, unlike prior ones which expanded retirement benefits, does not specify any tax increases. Yet, the 15 percent benefit expansion must be financed. Since the ways of doing so have not been indicated, the full tax effects of the 1969 law cannot be analyzed now. If the tax increases take the form of raising the wage base (from $7,800 to perhaps $12,000 as under the Senate version of the bill), the tax relief for millions of middle-bracket taxpayers will be largely or entirely offset by higher payroll taxes, especially when the employer's portion is taken into account.

Table I
Tax Reform and Tax Relief, and Increased Social Security Benefits
at 1969 Levels of Income, Calendar Years
(Millions of dollars)

	1970	1972	Long Run
Tax Reform	+1,150	+1,660	+3,320
Repeal of investment credit	+2,500	+2,990	+3,300
Tax reform and repeal of investment credit	+3,650	+4,650	+6,620
Income tax relief:			
Low-income allowance	— 625	—2,057	—2,057
Increase in standard deduction		—1,355	—1,642
Increase in exemption	— 816	—3,267	—4,845
Maximum 50-percent rate on earned income		— 170	— 170
Tax treatment of single persons		— 420	— 420
Total tax relief under conference bill	—1,441	—7,269	—9,134
Balance between reform (+) and relief (—) under conference bill	+2,209	—2,619	—2,514
Extension of surcharge and excises	+4,270	+ 800	
Total	+6,479	—1,819	—2,514
Social Security Benefits	+4,400 first year		

Source: Joint Committee on Internal Revenue Taxation.

Distribution of Changes in Tax Burden

Table 2 shows by income class the estimated distribution of burdens of individual income tax changes. These estimates make no allowance for the $5.2 billion increase in taxes on corporations; yet somehow, consumers, stockholders, and others will have to bear these burdens on corporations. Table 3 estimates the distribution of the corporate increases by 5 income classes on the assumption that half of the total is borne by the stockholder and half by consumers.

Within all income brackets, and especially those over $20,000, the law will have widely different effects on various individuals. Some features affect only a small fraction of taxpayers in a group.

In general, reductions in the low brackets are relatively large. For about 7.6 million returns of individuals and families, the relief is great enough to eliminate tax entirely. For humanitarian reasons, and for economy in administration, removal of millions from the tax rolls may seem wise. But citizen responsibility in supporting economy in the growth of spending may weaken. Presumably the great bulk of the increase in disposable income will be used for consumption and rather little for saving.

The $2.1 billion of new low-income relief will benefit those with relatively little income but still above the exemption level. The phase-out (i.e., the reduction of relief) prevents the allowance from granting much relief to those with somewhat higher incomes ($7,000 or more). The law goes far toward meeting goals which have considerable appeal on humane grounds—and on what some people would call equity grounds.

From $10,000 to $15,000 net relief averaging 12.6 percent of tax is above average (ignoring probable increases in Social Security taxes), but in the higher ranges net tax relief is small, in part, but only in part, because there the "reform" increases are greatest and affect some persons rather heavily.

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How Much Reform?

In addition to benefits designated as "tax relief" but which may also deserve to be classed as "reforms," how much "reform" will this law really accomplish? Differences of view will depend upon concepts of "reform". For many years critics of Federal taxation have urged both reduction in the extreme rates of tax and also structural revisions—changes in inclusions, exclusions, deductions. But there has been little agreement on priorities or on the relative importance of changes with appreciably different revenue, burden, and economic effects. Nevertheless, the Act of 1969 does deal with most of the avoidance elements which elicited most criticism.

As a result, the group of individuals with incomes over $100,000 will actually pay more in tax—estimated to be 7.2 percent. Tax shelters offer less protection. Opportunities for converting other forms of income into capital gain have been reduced, and the rates on capital gains have been increased in some cases.

Disagreement about the merits of almost every change, and the proposals which were rejected, con-

Table 2
Tax Relief Provisions Affecting Individuals, When Fully Effective,
By Adjusted Gross Income Class, 1969 Levels
(Dollar amounts in millions)

Adjusted gross income class[1]	Reform provisions	Relief provisions: Low income allowance	$750 exemption	15-percent $2,000 standard deduction	Maximum tax on earned income	Tax treatment of single persons	Total relief provisions	Total all provisions	Percentage change from tax under prior law[2]
0 to $3,000	+ $6	— $682	— $140	—	—	—	— $822	— $816	—69.8
$3,000 to $5,000	— 6	— 719	— 366	— $10	—	—	—1,095	—1,101	—33.2
$5,000 to $7,000	— 4	— 458	— 612	— 31	—	— $7	—1,108	—1,112	—19.9
$7,000 to $10,000	— 5	— 198	—1,244	— 366	—	— 45	—1,853	—1,858	—15.8
$10,000 to $15,000	+ 6	—	—1,407	— 858	—	— 68	—2,333	—2,327	—12.6
$15,000 to $20,000	— 7	—	— 480	— 242	—	— 62	— 784	— 791	— 8.6
$20,000 to $50,000	+ 56	—	— 462	— 125	— $5	—179	— 771	— 715	— 5.1
$50,000 to $100,000	+ 54	—	— 104	— 8	— 30	— 40	— 182	— 128	— 1.9
$100,000 and over	+740	—	— 30	— 1	—135	— 17	— 183	+ 557	+ 7.2
Total	+840	—2,057	—4,845	—1,642	—170	—420	—9,134	—8,294	—10.6

1. Does not include data shown in Table 3.
2. Exclusive of tax surcharge.
Note: Details do not necessarily add to totals because of rounding.
Source: Same as Table 1.

tinues. One man's "loophole" seems to someone else a justified protection against excessive burdens. Or a much criticized feature is defended as a meritorious means of providing incentive for actions in the public interest.

Analysis of each of the features classed as "reforms" encounters difficulties, partly because special interests, being biased, will present less than complete evidence and partly because of complexity. Every element of the income tax relates to several others—and to individual and business behavior—and often in more ways than casual observation can reveal. A balanced view about the desirability of a "reform" must include more than the effects upon the distribution of tax burdens. Also relevant are effects upon the economy—investment in new construction—and upon society more generally—greater incentives for the young to work. When these varied results have been identified in the future, evaluating them will require judgments based in part upon intangibles about which views will differ. What are the relative merits of activities aided by tax encouragement of state-local borrowing or percentage depletion in excess of cost?

One outstanding element—the new 10 percent minimum tax—will directly affect only a relative handful of persons and corporations. But it does reach types of receipts heretofore largely or entirely exempt. How much "preference" income will still be taxed lightly, or not at all? Amounts cannot be estimated accurately. (Social Security benefits remain fully exempt.) The tax rate, though perhaps seemingly low, will reduce the relative attractiveness of some types of investment and activity. The responses of taxpayers, and the economic effects, remain to be seen.

One of the most basic "reforms" would be reduction of tax rates. Such action would attack problems of every diverse kind. Exclusions and inclusions, discriminations and preferences, all features, lose some of their practical importance as applicable tax rates go down. Such features gain significance, of course, the *higher the rates* of tax and the greater the *differences* of rates at various income levels, or as among groups (married or single individuals), or as affecting types of economic activity (manufacturing, finance, or natural resource industries).

For single individuals, heads of households, and high-bracket earned income, the Tax Reform Act of 1969 does reduce rates. Otherwise, it achieves no moderation of rates. Moreover, in one major respect (elimination of the investment tax credit) the law in effect raises rates.

Another rate increase results from the raising in some cases of rates on long-term capital gains—of individuals in highest brackets and of corporations. In narrowing the gap between ordinary income and capital gains, this

Table 3
Corporate Tax Increases: Estimated Distribution by Adjusted Gross Income Class

Adjusted Gross Income	Assuming half borne by shareholders and half by consumers: Percentage of tax	Percentage of AGI
0-$5,000	16.2	1.4
$5,000 to $10,000	22.6	.6
$10,000 to $15,000	15.4	.5
$15,000 to $20,000	7.6	.6
$20,000 and over	38.2	1.6

Source: Same as Table 1.

change reduces the incentives to alter affairs to convert various sources of income into capital gains. Over many years, the lower capital gains rate has been defended as an "escape valve," a device freeing society from some of the bad effects of very high tax rates. This advantage has now been reduced, not so much by moderating other rates (except on some earned income) as by raising the burden on certain capital gains.

Although most students of Federal taxation could probably make a list of several items of "unfinished business" in tax reform, the sense of urgency would be only a modest fraction of that early in 1969. The many forces of Congressional and Executive Branch action have produced compromises which, like so many, will fully satisfy no one and yet receive widespread commendation.

Exemption Increase Instead of Rate Reduction

The House bill provided for reduction in personal tax rates through the entire income scale. As finally passed, however, the Act provides little in rate cuts. Instead, it grants approximately the same total revenue reduction by raising the personal exemption. But the distribution by income class of about the same amount of tax relief is markedly different under the two approaches. The exemption increases provide more relief than would the House rate reduction in the ranges below $15,000 and markedly less above.

The approach chosen, along with other provisions, favors taxpayers with smaller incomes, and especially large families.

Choice of the exemption method has another result—an absence of moderation in the *marginal influences* of personal income tax rates. For most taxpayers, the incentive effects of tax rates will generally continue at the highest amounts applicable over recent years. Both work efforts and investment choices will be subject to the same pressures as in the recent past—except that from year to year the marginal influences will actually gain increasing force as incomes go up (part of the rise being due to inflation). For most people, including the owners of unincorporated businesses and professional persons, the House bill would have moderated the effects of high and graduated rates.

Rate reduction, perhaps along with widening of brackets, will remain as a goal of tax reform. By reducing the highest rates, much could be accomplished without large revenue loss. But for political reasons, cutting rates through the whole income range may seem necessary if high brackets are given relief. Such broad reform would be more costly than budget needs are likely to permit in the near future.

Capital as the Chief Base for Higher Tax Burdens

To get revenue as a partial offset to relief features, and in accomplishing what are designated as reforms, the law adds burdens. Most such increases take the form of heavier taxes on the return to capital.

By far the largest is removal of the investment tax credit. Capital outlays will now cost more. The greatest number of taxpayers *directly* facing higher taxes on this score are the hundreds of thousands of owners of unincorporated businesses and of corporations small enough for owners to see how the company is burdened.

Large businesses, however, must shoulder the first impact of the bulk of the tax increases. These companies employ millions of workers, supply the entire consuming public, and are owned by millions of shareholders. Tax changes hurting big business will affect everyone adversely, albeit indirectly.

The returns to equity capital suffer the initial impact. (The 1964 law in withdrawing the 4 percent dividend credit also concentrated a tax increase on the owners of equity capital.) Shareholders will continue to bear the burden except as the higher taxes can be shifted to others—for the most part, to consumers. To some extent, perhaps, suppliers will absorb some of the burden as they reduce prices in trying to prevent sales from dropping. Some decline must be expected in the demand for new capital equipment.

The Act's other changes which bring substantial revenue increase do so by adding to taxes, or removing tax preferences, largely associated with capital—less depreciation on most new buildings; smaller loss reserves for financial institutions; heavier taxes on producers of natural resources; and higher burdens on capital gains, some retirement plans, trusts, and investments in farms. Economic progress may suffer from these 1969 actions which were inspired by such a laudable objective as the reduction of inequity in sharing the costs of government. The relative discrimination against capital received almost no explicit attention in the discussions of 1969.

In forcing some recipients of income from capital to pay more tax, Congress, one can assume, was responding correctly to public sentiment for curtailing the use of tax shelters. Nevertheless, reducing the after-tax yield of capital will have effects other than merely getting more revenue. The amount and the allocation of new capital will be affected.

Expenditure on certain types of new capital formation will be discouraged. Per dollar of additional revenue obtained by tax-raising features of the Act, the retarding effects on personal and business savings, and on capital formation, may be relatively great. Much of the higher tax will probably come out of saving rather than consumption, and most of the tax relief, going to lower income groups, will probably provide only a little increase in saving compared with consumption. The new tax burdens seem much more likely to hurt than to help economic progress as it depends upon capital.

Perhaps we must accept the tax changes of 1969 which increase burdens on capital as irreversible. The problem which results, however, cannot be dealt with as well as reasonably possible by resigned acceptance of a *fait accompli*. Capital accumulation is of such importance for economic progress that we ought to give earnest consideration to methods of encouraging (or avoiding discouragement of) saving and investment. One suggestion is "forced saving" by means of taxes high enough to yield a budget surplus. Treasury repayment of debt would put funds into the capital market. This method, however, conflicts with concepts of freedom and standards of efficiency as some of us envisage them.

Repeal of Investment Credit

One of the most important changes is the elimination of the investment tax credit. No reversal seems probable. Nevertheless, the implications of what has been done need to be examined.

The repeal not only adds to burdens. It also discourages a type of capital formation which relates directly to economic progress, especially cost reduction. The credit was designed to favor outlays for new machinery and equipment. These involve more than additions to the stock of productive capital; they also embody the latest in technological progress.

The credit had been a major element of the economic program of President Kennedy. It seemed to be producing the constructive results predicted by its advocates. Suddenly in April 1969, however, Administration spokesmen reversed positions of support which they had been taking. Earlier, some influential Democrats had shifted from support to criticism of the credit. Yet the support rested on economic arguments which presumably had lasting validity.

Why did both Republican and Democratic leaders change their positions? An outsider will not know how much weight properly to assign to various factors—desire because of anti-inflationary needs to reduce near-term business spending on machinery, anti-business sentiment, or a belief that such a position has political appeal; opportunity to "get" revenue to permit tax relief, e.g., ending the 10 percent surcharge; belief that need for machinery and equipment would be relatively less in the 1970's; a feeling that for the same revenue some alternative provisions yielding better results could be devised; and doubtless others. Belief that investment in new equipment would rise from an already high level and add to inflation pressures was cited in 1969, along with assertions that since the investment credit could not be "turned on and off," complete termination would be the best move.

The Congressional committees alloted the credit little time on their busy schedules. Business leaders, having been assured that the credit was a permanent feature of the tax system, were not prepared for the sudden change in official views. A few industries were more concerned with other tax issues and directed their influence to what seemed more important. Some businessmen had never been enthusiastic supporters of the credit as compared with lower tax rates or better depreciation rules.

President Nixon, applying the term "subsidy" to the credit, indicated that alternatives with higher priority would be proposed. None were specifically identified. But the Administration advocated a 4 percent rate reduction (2 percentage points) to take effect in the 1970's. Some members of the Senate Finance Committee criticized this proposal to reduce the tax on corporations when some of the proposed relief for individuals was being opposed by the Administration. Business leaders and the news media accorded little attention to this proposal. Supporters, however, believed that it would go considerable distance to compensate for repeal of the investment credit and that it would favor efficiency, new investment, and cost reduction.

Some discussions treated the elimination of the 10 percent surcharge as an offset to the tax increase of the repeal of the investment credit. The repeal, however, increased burdens *permanently* whereas the surcharge had always been assumed to be *temporary*. An "exchange" of this sort was anything but reasonably equal. To set off the two as about the same was to ignore the vastly different amounts over a period of years.

A source of additional concern arises at this time from the unsatisfactory state of the tax treatment of depreciation. Originally, introduction of the investment credit was said to be related to the 1962 revision of the tax treatment of depreciation. The two together made up a "package" to reduce tax impediments to modernization and expansion. The depreciation reform of that year remains inconclusive because of the lack of general acceptance of one element, the reserve-ratio test. The investment credit was cited as a device to facilitate disposal of older equipment and the replacement with new as required to comply with the reserve-ratio test.

Existing depreciation provisions are made distressingly obsolete by the continuation of inflation—and at a speed which makes the use of historical cost in computing capital recovery (consumption) allowances increasingly unsatisfactory. In effect, businesses, incorporated and unincorporated, are *now liable to tax (at high rates) on more than net income*, more, that is, when current prices, not those of the past, are recognized as relevant for replacing capital equipment. Somewhat indirectly, the repeal of the investment tax credit aggravates the problem of the inadequacy of allowances for capital consumption as a production cost. The repeal raises the *after-tax* cost of new machinery and equipment. This cost increase comes at a time when inflation raises the pre-tax cost and as depreciation rules still limit capital recovery to original dollar amounts.

Depreciation of Buildings

One set of the changes will eventually add some $930 million a year to the tax on owners of buildings by restricting the use of accelerated depreciation. This action results in part from evidence that structures do not generally lose value as rapidly as the tax deduction rules have allowed since 1954. (Whether the estimates of total useful lives are reasonably accurate will be debated.) Depreciation schedules based on a useful life of 40 years would permit 2½ percent deduction in the first year under the straight-line method but 5 percent under the double-declining-balance method. The prices obtainable from the actual sale of buildings, however, have not typically reflected such price declines in early years. Owners have been able to deduct as an expense a depreciation item greater than the actual loss in value during early years of a building's life (or of one ownership). The owner may have had a considerable cash flow but little or no income tax liability.

When the amount not yet deducted as depreciation had declined to a modest figure, the building may still have had substantial market value. If the owner then sold, a portion of what he received was often treated as a capital gain (but some being subject to recapture rules) and taxable at a rate lower than would have applied to the rental income. The new buyer then had his purchase price as a value from which he could begin to deduct depreciation.

In effect, arrangements such as this permitted the conversion of rental income into capital gains which, upon being realized, were taxed at a rate half—or less than—the rates applicable to ordinary corporate or personal income. When conditions leading to this treatment were combined with substantial debt financing (high leverage), some owners obtained large returns on their equity investments and yet paid comparatively little income tax. Understandably, the drive for removal of tax shelters directed attention to this possibility.

The 1969 changes are criticized, however, as certain to discourage the flow of capital into new buildings. And the market for older building will become less attractive. The law, however, does continue the favorable treatment for rental housing and also adds provisions to encourage rehabilitation. These features can be expected to attract relatively more funds than before into residential construction and maintenance. Such bias may, or may not, seem desirable in principle.

The ending of accelerated depreciation applies to factory buildings and other business plant structures. Frequently, they relate intimately to the introduction of new equipment (e.g., a chemical plant or a refinery) or the expansion and modernization of existing facilities. The conditions cited in defense of denying accelerated depreciation for commercial buildings do not as a rule apply to structures used for manufacturing, public utilities, and some other businesses. In such industries, the conversion of rental income of buildings into capital gain would be exceptional. The new rules will discourage the expansion and modernization of productive facilities.

For several years, strong demand, supported by favorable tax treatment, led to large amounts of new building. But the effects have included increases in construction costs and land prices—and by more than prices generally. To what extent has the generous tax treatment been translated into cost-raising factors? The answer is not clear. Adverse effects of the tax on quality have also been alleged. Criticisms of some new structures attribute poor quality, in part, to newcomers to investment in real estate, attracted by the "fast buck" and aided by the tax law in sacrificing the longer run to the early years of large capital recovery. Perhaps the change in tax treatment will moderate slightly the upward pressure on construction costs and land prices. Perhaps there will be more concern for quality, for buildings which will have longer productive lives.

Time will be needed for analysis of developments. An open mind and alert observation will be called for to identify results and then to adjust tax laws accordingly.

Complexity and Simplification

The Act contains some of the most intricate and complex provisions ever embodied in a tax law. An impression of stupifying complexity will strike anyone picking up the law; the impression will remain after hours or days of study. To some extent the feeling will be temporary because as new features are mastered several of them will be seen to replace old ones no less difficult.

In many ways, however, a substantial *net* addition of complexity has been imposed upon both the public and the Internal Revenue Service. Despite widespread belief in the desirability of tax simplification, this law at one point after another moves away from simplicity. The degree of added complexity will remain in question until after new regulations have been proposed, administrative practices established, and judicial interpretations handed down. Unfortunately, the costs—time and trouble, money, and diversion of effort and talent—will be huge.

Yet for millions of taxpayers and the IRS, this law does simplify matters somewhat. The greater use of the standard deduction accomplishes at least a small amount of simplification for many individuals.

Several provisions reduce or eliminate tax preferences and thus modify the alternatives open to individuals and businesses. Such shortening of the list of possible tax shelters can hardly meet with the approval of persons who could once consider them as realistic alternatives. But reducing the list of practical possibilities has as an indirect result the elimination of need to engage in some intricate legal arrangements for escaping tax. They will no longer produce significant tax saving. For example, narrowing the gap between the tax rate on long-term capital gains and that on other income, especially larger amounts of earned income, will at times simplify tax planning. Some alternatives, though still open, will no longer warrant serious study.

The accumulation of complexity has reached such a state that one part of the continuing job of improving the tax system ought to be serious and sustained effort for reducing complications.

How Much Help for Dealing with Problems of the Cities?

Does the new tax law make some contribution to the financial problems of cities? Congressional testimony gave almost no explicit attention to State-local problems other then the tax exemption of municipal bond interest, which remains unrestricted. The architects of the law had concerns other than those of local government finance. Indirectly, however, their work does have some favorable bearing (and some unfavorable, notably repeal of the investment tax credit, which weakens slightly the economic base of all communities).

The concentration of tax relief on low and lower middle income groups will help them to pay for their many needs. The needs include, of course, services financed by state-local taxes. City governments, however, will not find it easy to tap this increase in spendable—and "taxpayingable"—income. When people are free to spend more, their private rather than collective (governmental) wants may take precedence. Nevertheless, the freeing of all who are below the "poverty line" from Federal income tax ought to make some welcome, albeit not monumental, reduction in the most insistent pressures for more local government spending, while increasing the capacity to pay taxes for the services being provided. As Congress and the Executive Branch face appeals for more Federal aid, they can recall that the 1969 law assures some tax relief in 1970 and more each year to the $9.1 billion of 1974.

Pollution constitutes one of the problems of growing concern for local governments. New tax provisions will aid private firms in reducing the pollution from facilities in place before 1969. Consequently, city, county, town, and state anti-pollution programs will get a little indirect help.

Changes in the tax treatment of real estate depreciation will tend to direct new investment away from commercial and industrial construction toward residential—new buildings for rental and expenses for rehabilitation. Rental residential facilities will receive a stimulus which will help in meeting housing needs. Prevention and improvement of the existing housing stock will contribute toward better conditions.

Effects of Revenue Change

In judging the probable effects of significantly large changes in total revenue, considerations of two different types call for attention: (1) the effects on total buying power and the resulting significance for controlling inflation and (2) the rate of growth of Federal spending and of government's role in the economy.

Control of Inflation. The 10 percent surcharge and the higher rates of excise taxes were originally supported as devices for fighting inflation. So was the 6-month extension of the surcharge into 1970 at 5 percent and the excises for a longer time. But the law does grant net tax relief for the future and increases Social Security benefits by 15 percent at once—and has been criticized for doing so. In view of the continuation of inflation, tax relief may seem inappropriate. Dealing with inflation pressures in the 1970's has been made more difficult, according to some economists.

The tie between total tax collections and inflation is often expressed in simple terms. The higher the total of Federal tax revenue, the smaller the purchasing power which individuals and businesses will have to spend. The less, therefore, can such private buyers do to raise the price level. When total buying is at a level already high, any increases in dollar demand will tend to "pull up" prices. By the same reasoning, heavier taxes which reduce private spending power, of businesses or consumers, will tend to keep prices from going up. Tax reductions, however, will raise disposable income, encourage buying, and under some conditions work against efforts to end inflation.

While connections of this sort between taxes, effective buying demand, and inflation clearly exist, the total set of relations which affect the price level are more complex. The complete analysis must involve the relation of Treasury receipts and expenditures (budget deficits and surpluses) to the financial conditions of capital and money markets, e.g., interest rates and the availability of loans. The conditions in financial markets depend upon the many parts of both demand and supply for credit. Federal Reserve policies influence the availability of credit and interest rates.

For controlling inflation, the effectiveness of one against another level of tax payments will depend in part upon the extent to which consumers and businesses alter their saving as well as their buying. (The disappointing effects of the 10 percent surcharge resulted in part from consumer curtailment of saving rather than of consumption.) An increase in saving, however, relieves potential pressure on markets for consumer goods and services, adds to the supply of funds for investment, and tends to reduce interest rates. The net effects of tax changes on total savings cannot be forecast accurately.

In relating tax changes to inflation, one possibility is sometimes overlooked. "Higher" taxes may in fact *raise government spending.* Consumer and business spending goes down, but the larger inflow of revenues invites more Federal expenditure. An undeniable fact of contemporary life is the force of tremendous pressure for growth of Federal spending. The effects of taxes on total demand and upward pressure on prices will not by any means be limited to the effects in the private sector.

What will be the probable effect of personal tax relief on pressures for higher wage rates—especially in 1971 and 1972? Perhaps the increase in personal exemptions (and larger deductions) will moderate the demands on employers for wage increases and the cost-and price-raising effects of higher wage rates. If so, some indirect relief of inflation pressure will result. But there can be little hope that it will be large. And any rise in Social Security taxes is likely to be an offsetting factor. Moreover, the addition of heavier tax burdens on businesses (including Social Security taxes on employers) will raise costs.

Repeal of the investment tax credit was defended as helping to dampen inflationary pressure by curtailing demand for new equipment. Businesses have less cash and less incentive to install new machinery. This particular decline in demand, however, concentrates on an element which helps to reduce cost—new equipment and machinery.

In short, the Act of 1969 may make the control of inflation more difficult in the 1970's, but the net effect of divergent forces remains to be seen. Action appropriate to conditions as they do develop can be devised in the future.

Growth of Government. Even though the Act will make total collections in 1972 and beyond lower than if prior law were to prevail, Federal revenues will be higher than in 1970. They will rise by enough to finance more than a little growth in Federal spending.

Will this growth be fast enough, however, to satisfy "needs"? Expenditure programs of high appeal will call for more dollars. Existing programs will continue to claim funds even though shifts in relative priorities "ought" to remove some of the "legitimacy" of older programs. Automatically rising revenues, it is said, reduce the actual pressure for thorough justification of much Federal spending. One obstacle to best analysis of spending programs results from the easy availability of more and more tax dollars, year after year, and without any action of Congress to vote tax increases. If money is there, many uses will compete for it—and government gets bigger.

Some of the demands for satisfying "collective" wants appear, gather support, and grow because taxes reduce the capacity of individuals and businesses to provide for themselves. "Adequate" financing for meeting the many needs of families, of voluntary associations, and of local communities becomes impossible, in part because of high Federal taxes. Thus rising taxes add to the pressures for more government spending.

The "collective" propensity to spend may be every bit as great as that of individuals. "Needs" press. The hope of getting something paid for by others adds to the inclination to seek governmental provision. When the flow of dollars into the Treasury expands, so, it seems, will spending—and with scarcely perceptible lag. Budget surpluses are likely to encourage greater spending. The result is not only bigger government. Efforts to check inflation also suffer. Heavy tax burdens intended to control inflation by reducing private spending may therefore do little more than expand the role of government.

Growth of government can come about without an explicit vote of more taxes to pay for more spending. The law of 1969 reduces this possibility. Of course, decisions of 1969 for tax reduction in, say, 1973 do not foreclose new action then to expand spending. But doing so would require that more of the spending decisions of 1973 be related to tax decisions made at the same time.