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PROPOSAL: Compulsory Bond Purchase as Compromise to Income Tax Rate Increases

Stanley Veliotis* and Kristen Gray**

Abstract

It is a common-held expectation that the U.S. federal government will need to increase cash receipts over the next decade. While the highest marginal income tax rates for many years were more than twice what they have been in the last three decades, it is expected that political pressures will not allow more than a modest increase in the current marginal tax rates. This Article proposes that the formerly prevalent higher marginal rates be reinstated on excessive personal services income, which is least likely to be subject to disincentive effects. However, to address probable insurmountable political resistance, the portion of the rate in excess of the 39.6% tax rate should be converted to an asset for the taxpayer - U.S. savings bonds. Besides providing the government with an injection of cash, these bonds are a form of compulsory savings, along the lines of the Keynesian "deferred pay" proposal. The approach provides a way for financially fortunate Americans to reinvest in their country, a patriotic theme reminiscent of War Bond drives of the last century, as well as a tangible commitment to global lenders that such Americans share their financial risk.

I. INTRODUCTION

The United States is in need of immediate cash flow with the current global economic meltdown, two wars and national debt already at \$7.5 trillion dollars.¹ The deficit is expected to increase by approximately \$9 trillion over the next decade,² which suggests that the U.S. will be in this disadvantageous position for at least several years. There have been a variety of suggestions to increase cash flow through the tax law, such as increasing income tax rates, reducing marginal tax

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1. U.S. Dept. of the Treas., *Monthly Statement of the Public Debt of the United States: August 31, 2009*, Table 2, available at <http://www.treasurydirect.gov/govt/reports/pd/mspd/2009/opds082009.pdf> [hereinafter *Monthly Statement*].

2. Jonathan Weisman & Deborah Solomon, *Decade of Debt: \$9 Trillion*, WALL ST. J., Aug. 26, 2009, at A1.

benefits of itemized deductions or imposing surtaxes on specific items such as employer-provided health insurance benefits. Despite the fact that all of these actions may generate cash flow for the U.S. government, they are an economic expense for the affected taxpayer and likely will be resisted in the current political climate. In this Article, we propose a compromise - a compulsory bond purchase program to satisfy current governmental needs while also creating a direct benefit for the taxpayer.

Under the proposal, taxpayers will be required to purchase government bonds based upon a percentage of their income derived from certain personal services beyond \$500,000. The income above this threshold will be “taxed” using a progressive rate structure starting at 45%, and increasing in 5% increments for bands of income, until reaching a maximum marginal rate of 75%. The new charges in excess of the 39.6% marginal income tax rate will automatically be converted into U.S. government bonds. These bonds will receive interest annually but will not have a fixed maturity date. Instead, the principal begins to be returned upon the earlier of the taxpayer’s death or reaching seventy years of age (with some hardship exceptions). However, the federal government may redeem the bonds sooner, such as in the case of budget surpluses.

Besides providing the government with an injection of cash, these bonds are a form of compulsory savings, along the lines of the Keynesian “deferred pay” proposal advanced at the start of World War II. The approach also provides a way for financially fortunate Americans to reinvest in their country, a patriotic theme reminiscent of War Bond drives of the last century, as well as a signal to global lenders that the most successful (and often high-profile) Americans share their financial risk. Also, by repaying the bond principal to those taxpayers who purchased them, the proposal improves on typical scenarios in which government reduces tax rates in good years for *all* taxpayers, not just those who paid high taxes in prior years. While one can argue that the compulsory aspect of the bond purchases may provide disincentives for working, or may be viewed as confiscatory in nature, we provide counter-arguments.

This Article proceeds as follows. Part II details the U.S. government’s need for cash flow and the difficulty in addressing this need by increasing marginal tax rates. Part III describes the proposal to institute compulsory bond purchases. Part IV estimates how much money may be raised annually from such a program. Part V compares the proposal to U.S. war bonds of the last century as well as analogous compulsory arrangements outside the U.S. Part VI addresses possible

objections to the proposal, while Part VII highlights some implementation issues that would need to be addressed further if the proposal is enacted.

II. U.S. GOVERNMENT'S NEED FOR INCREASED CASH FLOW

Since late 2008, when the global economic crisis unfolded, and especially after President Obama took office in 2009 and began to propose and enact broad-sweeping legislation, the U.S. is expecting increasing record deficits. This problem confounds what already was considered a precarious position for the U.S. economy entering the 21st century.³ While the U.S. is already committed to spending \$787 billion on stimulus to address the current crisis, there have been opinions that even more stimulus spending might be needed.⁴ Also, proposed legislation for climate control and broadened health care is expected to require even more federal outlays.⁵ The deficit is expected to increase by approximately \$9 trillion over the next decade, which indicates that the U.S. will be in drastic need for cash flow for the foreseeable future.⁶

Meanwhile, as of the end of August 2009, U.S. government bonds held by the public totaled nearly \$7.5 trillion.⁷ Almost half of this debt is held by foreign countries, including \$801 billion by China and \$725 billion by Japan.⁸ Annual interest payments on government debt

3. See, e.g., PETER G. PETERSON, *RUNNING ON EMPTY: HOW THE DEMOCRATIC AND REPUBLICAN PARTIES ARE BANKRUPTING OUR FUTURE AND WHAT AMERICANS CAN DO ABOUT IT* (Farfar, Straus & Giroux, 2004).

4. See, e.g., Deborah Solomon, *Calls Grow to Increase Stimulus Spending*, WALL ST. J., July 6, 2009, at A1; Jonathan Weisman & John D. McKinnon, *Democrats Weigh Extending Key Parts of Stimulus*, WALL ST. J., Oct. 3, 2009, at A2 (noting that, in light of unemployment reaching 9.8% (the highest since 1983), stimulus spending may reach \$900 billion).

5. See, e.g., Ian Talley & Stephen Power, *SENATORS TO UNVEIL DRAFT CLIMATE BILL*, WALL ST. J., Sept. 30, 2009, at A5; Janet Adamy, *The Health-Care Debate: A Clear Signal on Total Cost, Less Clarity on How to Pay*, WALL ST. J., Sept. 11, 2009, at A5. These ambitious plans are already drawing criticisms for various reasons, including their effect on the deficit. See, e.g., Michael J. Boskin, *Obama Needs a Move to the Middle*, WALL ST. J., July 23, 2009, at A15; A SQUEAKER, WITH MORE TO COME; *Climate Change, HEALTH CARE AND THE BUDGET*, ECONOMIST, July 4, 2009, at 24; Hal Weitzman, *Hot Air Over Cap-and-trade*, FIN. TIMES, Sept. 22, 2009, at 2.

6. Weisman & Solomon, *supra* note 2 (also citing Congressional Budget Office's more conservative \$7 trillion projection over the same decade). For details on the CBO's budget, see *Projected Deficits and Surpluses in CBO's Baseline, August 2009*, available at <http://www.cbo.gov/ftpdocs/105xx/doc10521/budgetprojections.pdf>. See also John D. McKinnon, *Group Tied to Obama Urge Tax Increase*, WALL ST. J., Sept. 30, 2009, at A5 ("Republicans and some Democrats also have been sounding the alarm on spending. Congressional Democrats also appear increasingly concerned about the government's fiscal situation. House Democrats are considering including criteria for reducing long-term deficits in next year's budget resolution.")

7. *Monthly Statement*, *supra* note 1.

8. U.S. Dept. of the Treas., *Major Foreign Holders of Treasury Securities*, available at <http://www.treas.gov/tic/mfh.txt> (listing holders as of July 30, 2009).

was \$451 billion for fiscal year 2008 and \$368 billion for the first eleven months of fiscal year 2009,⁹ and is expected to be nearly \$477 billion for fiscal year 2010.¹⁰ The combination of snowballing interest and principal payments, further deficit spending and pressure by foreign countries, including their calls for other currencies to act as global players¹¹ and reduction of foreign government purchases of U.S. debt,¹² puts the U.S. fiscal house in a more precarious situation.¹³

Even before the global economic meltdown, there were concerns about the need to raise funds. Writing shortly before the crisis, Professors Joel Slemrod and Jon Bakija noted:

The end of 2010 . . . also marks the unofficial beginning of when the baby-boom generation begins to retire and when the fiscal pressure of Social Security and Medicare promise to accelerate. Although the near-term political focus will be on the fate of the Bush tax cuts and the alternative minimum tax, what to do about the growing long-term fiscal imbalance will almost certainly have to move to center stage. Some have suggested that an efficient new tax might

9. U.S. Dept. of the Treas., *Interest Expense on the Debt Outstanding*, available at http://www.treasurydirect.gov/govt/reports/ir/ir_expense.htm. These interest payments are on all government debt, not just debt held by the public.

10. U.S. Dept. of the Treas., *Detail of Other Treasury Accounts* 115, available at <http://www.ustreas.gov/offices/management/budget/budgetinbrief/fy2010/BIB-OtherTreasuryAccounts.pdf>.

11. See, e.g., Angela Monaghan, CHINESE OFFICIALS CALL FOR END TO DOLLAR'S GLOBAL DOMINANCE, DAILY TELEGRAPH, July 6, 2009, at 2; Dennis K. Berman, *The Game: Inevitable End to Dollar's Reserve Role?*, WALL ST. J., Sept. 1, 2009, at C1; David Marsh & Andy Seaman, *China's Love-hate Relationship with the Dollar*, FIN. TIMES, Sept. 9, 2009, at 9.

12. Floyd Norris, *Asia Reduces Its Appetite for U.S. Debt; Off the Charts*, INT'L HERALD TRIB., Aug. 22, 2009, at 10 (noting that U.S. will "have to turn to other buyers, including American citizens . . . to finance the deficits."). See also Rob Copeland, *Treasury's Debt Plan: More Sales of TIPS*, WALL ST. J., Aug. 5, 2009, at C4 (government to announce plans to increase sales of inflation-protected bonds because China prefers them). Indeed, there is also the risk that even if foreign countries wanted to continue to buy U.S. debt, they may not have enough savings. William Eagle, *G20 to Discuss Future of Economic Stimulus*, VOICE OF AM., Sept. 21, 2009, available at <http://www.voanews.com/english/2009-09-21-voa52.cfm> ("I do not think I will buy government bonds any more to finance this debt because I am not sure that the [U.S.] will be in a position to pay the bonds back. . . . It is also said all the world's savings are not large enough to [pay for] the deficits that the United States will produce over the next 10 years," quoting a Canadian expert).

13. See, e.g., Tom Raum, *Mountain of Debt: Rising Debt may be Next Crisis*, Associated Press, July 3, 2009, available at <http://abcnews.go.com/Politics/wireStory?id=7995188>; Dirk J. Bezemer, *This is not a Credit Crisis – It is a Debt Crisis*, 29(3) ECON. AFF. 97 (Sept. 2009). See also ROBERT D. HORMATS, *THE PRICE OF LIBERTY: PAYING FOR AMERICA'S WARS* 298-99 (Henry Holt & Company 2007) ("Decades of success in mobilizing enormous sums of money [for wars and other] governmental needs have led Americans to believe that ample funds will be readily available in the event of a future . . . emergency. But that can no longer be assumed. Budget constraints could limit the availability or raise the cost of resources to deal with new emergencies. If government debt continues to pile up, deficits rise to stratospheric levels, and heavy dependence on foreign capital grows, borrowing the money needed will be very costly.").

be part of the long-term solution, but this debate has hardly begun.¹⁴

To help fund the government, many think the U.S. will need to raise taxes,¹⁵ just as many states¹⁶ and other countries¹⁷ are contemplating or have enacted tax increases in light of budget problems brought on by the global economic crisis. The Department of Treasury estimates that the expected increase of the present highest marginal income tax

14. JOEL SLEMRUD & JON BAKIJA, *TAXING OURSELVES, A CITIZEN'S GUIDE TO THE DEBATE OVER TAXES* 309 (MIT Press 4th ed. 2008). The Social Security Administration confirms the dire situation the Social Security Trust fund is in, recently predicting that program costs will start exceeding program revenues in 2016 and the fund will be exhausted by 2037, citing the current economic crisis as an aggravating factor. Mark Lassiter, *Social Security Board of Trustees: Economic Downturn Leads to Worsening of Long-Range Financing Outlook* (May 12, 2009), available at <http://www.ssa.gov/pressoffice/pr/trustee09-pr.htm>.

15. Roger C. Altman, *We'll Need to Raise Taxes Soon*, WALL ST. J., June 30, 2009, at A15. Mr. Altman was Deputy Secretary of the Treasury under President Clinton. See also John Fund, *The Weekend Interview with David Walker: Warning: The Deficits are Coming!*, WALL ST. J., Sept. 5, 2009, at A11 (reporting interview with David Walker, former head of the Government Accountability Office, "taxes are going up, for reasons of math, demographics and the fact that elements of the population that want more government are more politically active."); *The Small Business Surtax*, WALL ST. J., July 14, 2009, at A12 (opining that predictions from 2008 that Obama would need to raise income tax rates to nearly 60% are likely to materialize); McKinnon, *supra* note 6 ("Center for American Progress says the size of projected budget gaps requires considering options including tax increases."); Alexander Bolton, *Buffett Tells Dems Rich Need To Pay More*, HILL, Sept. 10, 2009, available at <http://thehill.com/homenews/senate/58129-buffett-to-meet-with-senate-dems#>.

16. See Conor Dougherty, *States and Towns Lean on Taxpayers*, WALL ST. J., Sept. 26, 2009, at A5; *States Balancing Budgets With Income Tax Increases, NCSL Says*, ST. TAX TODAY, July 21, 2009 (citing increases in tax rates and/or tax bases in California, Delaware, Hawaii, Massachusetts, Maine, New Jersey, New York, Oregon, and Wisconsin). Income tax rates have also been recently raised in North Carolina. *North Carolina Lawmakers Approve, Governor Will Sign Budget With Tax Increases*, ST. TAX TODAY, Aug. 6, 2009. Governors in Connecticut and Pennsylvania are also contemplating tax rate increases. *Connecticut Governor Proposes Revised Budget With Tax Increases*, ST. TAX TODAY, Aug. 3, 2009; Brad Bumsted & Mike Wereschagin, *Pennsylvania Governor Rendell Says Tax Increase A Must*, McCLATCHY-TRIB. BUS. NEWS, June 17, 2009.

17. In June, the OECD recommended that EU states raise taxes or stop planned tax cuts. *OECD Pushes For Tax Increases, Delayed Tax Cuts*, WORLDWIDE TAX DAILY, June 26, 2009. Meanwhile, many countries have increased taxes or are likely to. Anthony Faiola, *World's Wealthy Pay a Price in Crisis; Nations Raise Taxes, Tighten Regulations*, WASH. POST, Sept. 15, 2009, at A1. For other countries, see, e.g., John F. Burns, *British Plan to Raise Taxes and Debt Sets Off Political Sparring*, N.Y. TIMES, Apr. 23, 2009, at A4 (individual income taxes); Vanessa Houder, *Corporate Tax Rises Widely Feared*, FIN. TIMES, Sept. 21, 2009, at 4 (UK); *Spain Looks to Tax Increases to Rescue Economy*, WORLDWIDE TAX DAILY, Sept. 29, 2009; *Mexico Proposes Tax Increases as Part of 2010 Budget*, WORLDWIDE TAX DAILY, Sept. 10, 2009; ALKMAN GRANITSAS, *Greek Voters Consider a Leftist Economic Remedy – Socialists Gain Support for Elections Sunday With an Offer to Tax the Rich, Spend More and Run the Government Better*, WALL ST. J., Oct. 3, 2009, at A14; Alkman Granitsas, *Greeks Vote Socialists Into Power*, WALL ST. J., Oct. 5, 2009, at A13 (describing how the socialist party, having just won election, plans to raise taxes); *Tax Increases Inevitable In France?*, WORLDWIDE TAX DAILY, Aug. 5, 2009.

rate of 35% to its recent maximum of 39.6% for individual taxpayers will generate revenue of nearly \$13 billion in 2011 to as high as \$44 billion in 2019.¹⁸ Furthermore, these revenue increases are projected to be approximately 50% higher if the current 15% tax on qualified dividends and long term capital gains is increased to 20% for wealthier taxpayers.¹⁹

Our own revenue estimates computed from raising the marginal rate to 39.6% are slightly higher than the Treasury's. Of approximately 96 million tax returns filed for 2007, approximately 4.5 million reported adjusted gross income (AGI) over \$200,000, many of which likely faced a 33% or 35% marginal tax rate.²⁰ These 4.5 million taxpayers reported a combined taxable income of approximately \$2.4 trillion. If we assume approximately \$1.5 trillion of this amount would be subject to a marginal tax rate of 39.6% rather than 35%, we project that approximately \$71 billion per year in additional taxes would be raised.²¹

Whether we use the Treasury's recent estimate or our own, it is doubtful the income tax rate increase to 39.6% will be sufficient to raise the amount of funds the U.S. needs to make a dent in deficit spending and debt pay down. Obviously, one solution is to raise marginal tax rates even higher. For example, extending our estimate of a \$71 billion increase when rates are raised to 39.6%, it is possible an additional \$83 billion (up to approximately \$154 billion) would be raised if the 35% rate was instead raised to 45%.²²

However, it is clear that as a political matter, it will be difficult to raise income tax rates, especially raising the highest marginal rate

18. As of May 2009, the Department of Treasury's so-called "*Green Book*" is contemplating marginal tax rates in 2011 to rise above the current 35% rate to 36% for certain taxpayers and to 39.6% as the highest bracket, since the tax rate reductions of earlier this century automatically revert to their prior levels. It also proposes raising the capital gains and qualified dividend tax rate from 15% to 20% for high income taxpayers. "High income" is determined by levels of adjusted gross income, net of standard deduction and personal exemptions, and is in the area of \$200,000 to \$250,000, based on marital status. Table 1 of the *Green Book* sets forth the projected revenue from the tax increases. U.S. Dept. of the Treas., *General Explanations of the Administration's Fiscal Year 2010 Revenue Proposals* (May 2009), available at <http://www.treas.gov/offices/tax-policy/library/grnbk09.pdf> [hereinafter *Green Book*].

19. *Id.* at Table 1.

20. Based on data from the following: I.R.S., *Publication 1304*, Table 1.4, available at <http://www.irs.gov/pub/irs-soi/07in14ar.xls>. Of these 4.5 million returns, just over one million reported AGI above \$500,000, and approximately 390,000 reported AGI over \$1 million.

21. This calculation assumes \$200,000 is the cutoff before marginal tax rates reach their cap. The estimate of \$71 billion is likely overstated because, for example, parts of this taxable income are likely taxed at favorable rates, such as qualified dividends and long-term capital gains.

22. One may argue that it is not simply a matter of doubling the tax rates to receive double the amount of gross dollars since higher tax rates might lead to lower taxable income due to potential disincentive effects for taxpayers incurring this additional tax expense.

above the 39.6% rate that existed at the start of this century in the start of the Bush term. During the presidential campaign, candidate Obama needed to counter candidate McCain's characterization of Obama as "redistributor in chief" and that McCain would keep taxes lower.²³ When pressed during the campaign on whether he would raise taxes, Obama conceded that he would allow many Bush tax cuts to revert to prior levels, but only for those earning over \$250,000.²⁴ Candidate Obama knew then, and also appreciates now that he is in office, how difficult it is to raise income tax rates.²⁵ Even recent examples of proposals to raise tax rates beyond 39.6% or to scale down allowable tax deduction for the wealthy find the Democrats couching the changes in terms of paying for health care reforms.²⁶ Any whisper of Democratic attempts to raise tax rates immediately is criticized, especially if it is perceived as violating Obama's campaign promise of not raising taxes on those earning under \$250,000.²⁷

While marginal income tax rates have been as high as 94% during World War II and 92% during the Korean War, the highest rates

23. See, e.g., Jeff Mason, *McCain, Obama Present Different Views on Taxes*, BOSTON GLOBE, June 10, 2008, available at http://www.boston.com/news/nation/articles/2008/06/10/mccain_obama_stake_out_divergent_paths_on_taxes/.

24. See, e.g., Laura Meckler, *Campaign '08: McCain vs. Obama: In the General Election, Sharp Battle Lines Over Policy*, WALL ST. J., June 6, 2008, at A7.

25. For an exhaustive review of the history (and retreat) of progressive taxation in the U.S., see Marc Linder, *Eisenhower-Era Marxist-Confiscatory Taxation: Requiem for the Rhetoric of Rate Reduction for the Rich*, 70 TUL. L. REV. 905 (1996). For more recent papers, see Martin J. McMahon, Jr., *The State of Federal Income Taxation Symposium: Rate, Progressivity, and Budget Process: Symposium Article: The Matthew Effect and Federal Taxation*, 45 B.C. L. REV. 993, n.109 (Sept. 2004) (citing papers summarizing the history of progressive taxes in the U.S.).

26. See, e.g., Greg Hitt & Martin Vaughan, *Health Bill in House Relies on Wealth Tax*, WALL ST. J., July 11, 2009, at A1; John D. McKinnon, *DEMOCRATS TARGET HIGH EARNERS TO HELP FUND HEALTH PLAN*, WALL ST. J., Sept. 3, 2009, at A4.

27. In an August 2009 press release, the Republicans on the House Ways & Means Committee cited a Washington Post article: "While President Obama had previously called for extending Republican-enacted tax cuts for families earning less than \$250,000, the Washington Post is reporting that, 'in light of the new deficit figures, [OMB Director] Orszag hinted that Obama may revisit some of those decisions when he submits his next budget in February.'" OBAMA FLOATS ANOTHER MIDDLE CLASS TAX HIKE TRIAL BALLOON; Administration Issues Second Tax Hike Warning in August (Aug. 25, 2009), available at <http://republicans.waysandmeans.house.gov/News/DocumentSingle.aspx?DocumentID=142402> (last visited Oct. 4, 2009). However, the Washington Post article, which the Republican press release provides a hyperlink to, does not contain such a quote. See Lori Montgomery, *DEFICIT PROJECTED TO SOAR WITH NEW PROGRAMS; 10-YEAR ESTIMATE OF \$9 TRILLION FUELS CRITICS OF PRESIDENT'S AGENDA*, WASH. POST, Aug. 26, 2009, at A1. The Washington Post informs us that the Republicans cited an early online version of the article, which was later clarified when it went to final posting on the website as well as in print. See also McKinnon, *supra* note 6 (citing Obama Press Secretary immediately disavowing implications from September 2009 Sunday television comments from each of Obama's Treasury Secretary and Economic Adviser that failed to rule out middle class tax increases).

dropped precipitously when President Reagan entered office in 1981. At 70% in 1980, the highest rate was decreased to 50% and then to 28% by 1988 at the end of Reagan's presidency, and then it rose back up, when President Clinton raised it to 39.6% starting in 1993.²⁸ Whether Republicans or Democrats have been in control, it has been difficult to move marginal income tax rates back beyond 39.6%.²⁹

It is possible that Congress may seek to increase tax revenues not only by allowing the marginal tax rates to revert to 39.6% but also by expanding the income tax base.³⁰ For example, Congress is contemplating taxing certain health insurance benefits.³¹ Also, "stealth taxes" may help raise effective marginal tax rates, such as the current proposal to reinstate the phase out of total itemized deductions and per-

28. Historical income tax rate data is provided at the following: I.R.S., *Personal Exemptions and Individual Income Tax Rates, 1913-2002*, available at <http://www.irs.gov/pub/irs-soi/02inpetr.pdf>. It is interesting to note that during World War II, President Roosevelt issued an executive order limiting salaries to \$25,000 after taxes "in order to correct gross inequities and to provide for greater equality in contributing to the war effort." Taking the position that for reasons of 'morale,' 'no American citizen ought to have a net income, after he has paid his taxes, of more than \$25,000 a year,' Roosevelt had proposed 'a special war supertax' to limit a married couple's after-tax income from all sources to \$50,000. Congress, which nullified his executive order, never acted on his proposal to enact the supertax." Linder, *supra* note 25, at 940 (footnotes omitted). In more recent times Congress, in egregious cases, has sought to enact what amounts to a confiscatory tax. For example, Congress toyed with the possibility in early 2009 of taxing, at a rate of 90%, bonuses paid to certain employees of American International Group, Inc. (AIG), a recipient of government bailout money. See, e.g., Greg Hitt & Aaron Lucchetti, *House Passes Bonus Tax Bill — 90% Hit Would Affect Major Banks; Senate Mulls Similar Action Amid AIG Furor*, WALL ST. J., Mar. 20, 2009, at A1. There have also been excess profits tax regimes, which seek to tax profits of business above certain minimum thresholds. See, e.g., Anita Wells, *Legislative History of Excess Profits Taxation in the United States in World Wars I and II*, 4 NAT'L TAX J. 237 (Sept. 1951); E. Gordon Keith, *The Excess Profits Tax Act of 1950*, 4 NAT'L TAX J. 193 (Sept. 1951).

29. See Linder, *supra* note 25.

30. Government may also seek to expand or create tax bases other than the income tax base. One example is the current discussion of a national consumption or value-added tax. See, e.g., Daniel J. Mitchell, *VATs Mean Big Government*, WALL ST. J., June 4, 2009, at A15. Another example is the cap-and-trade approach to energy, which many argue amounts to a new tax on energy. See, e.g., INHOFE TO KERRY: CAP-AND-TRADE IS DEFINED AS TAX, A GREAT BIG ONE, U.S. FED. NEWS SERVICE, Sept. 28, 2009; Nick Snow, *CBO Says HR 2454 Would Add \$846 Billion in Taxes*, OIL & GAS J., June 15, 2009. The CBO report, dated June 5, 2009, is available at <http://www.cbo.gov/ftpdocs/102xx/doc10262/hr2454.pdf>. A third example is not allowing the estate tax to be repealed. See, e.g., Martin Vaughan, *Bid to Block Estate-Tax Repeal*, WALL ST. J., Aug. 13, 2009, at D3; Jonathan Weisman, *Estate Tax Faces Its Own Life-and-Death Struggle*, WALL ST. J., Sept. 19, 2009, at A5.

31. See, e.g., Laura Mecler et al., *Obama Backs Health Surtax: Proposal Targets Millionaire Families to Help Fund Overhaul of Medical Care*, WALL ST. J., July 23, 2009, at A1; Janet Mosenbach, *Income Taxation of Employer-Provided Health Insurance*, 124 TAX NOTES 478 (2009); Janet Adamy & Greg Hitt, *Tax ON 'CADILLAC' PLANS DRAWS FLAK*, WALL ST. J., Sept. 19, 2009, at A4.

sonal exemptions for high income taxpayers, which expires in 2010,³² or by recent proposals such as reducing the marginal tax benefit of itemized deductions to 28% for taxpayers in a higher tax bracket.³³ Even if these three items are implemented, the Treasury expects only between \$16 billion and \$66 billion a year to be raised.³⁴ Again, these will not be enough to provide sufficient cash flow for the government over the next decade.

III. THE COMPULSORY BOND PURCHASE PROPOSAL

It is not the intent of this Article to enter the political and economic debates over the merits or downsides of progressive taxation. It is also not our intention to implement a penalty on excessive compensation, along the lines of Internal Revenue Code Sections 162(m) or 409A.³⁵ Instead, we proceed with the assumption that the federal government must raise cash flow, and if the public will not stand for marginal income tax rates above 39.6%, and if other methods of raising revenues are insufficient, we propose a compromise.

The proposed approach calls for increased cash flow to the government by requiring taxpayers earning high levels of certain types of income to purchase bonds from the government. As detailed further below, we believe that taxpayers who receive income from employment and self-employment above a certain level are best situated to help provide cash flow for the government. However, the approach does not impose an expense on these taxpayers. Every student of accounting learns that cash outflow is not necessarily the same as an expense. In this case, the individual's balance sheet is not impacted - a current asset (cash) is exchanged for a longer term asset (bond). Furthermore, if we consider the U.S.'s aggregate "income statement," when the U.S. pays interest on internal debt (*i.e.*, debt held by its citizens, also frequently referred to as "we owe it to ourselves"), aggre-

32. Green Book, *supra* note 18, at 75-76. By "stealth tax," we refer to the effective incremental marginal rate that applies to taxpayers beyond the nominal marginal tax rate because many tax benefits decrease and burdens increase as AGI escalates. See Stephen J. Entin, *Mommy, What's a Stealth Tax?*, WALL ST. J., Mar. 11, 2003, at A14, for a layman's discussion. Earlier proposals, which expected to raise an average of \$30 billion a year by limiting specific deductions (*e.g.*, charities, interest expense) for high income taxpayers, have apparently failed to progress. See, *e.g.*, John D. McKinnon & Martin Vaughan, *White House Rethinks Tax Hikes: Obama Open to Revising Plan to Cap Breaks on Mortgage Interest and Donations*, WALL ST. J., Mar. 5, 2009, at A3; McKinnon, *supra* note 26.

33. Green Book, *supra* note 18, at 87.

34. Data calculated from Green Book, *supra* note 18, at 128-130 (Table 1 and Appendix A).

35. For a recent article discussing such issues, see Joy Sabino Mullane, *Incidence and Accidents: Regulation of Executive Compensation Through the Tax Code*, 13 LEWIS & CLARK L. REV. 485 (2009).

gate U.S. income is not impacted because the government's interest expense equals its citizens' interest income. Contrast that to the setting in which the U.S. borrows from creditors outside the U.S.-the U.S.'s interest expense is not offset by its citizens' matching income: instead, the interest leaks beyond the U.S.'s borders.

We propose to raise marginal income "tax" rates targeted to personal service income. This includes salaries of employees and net earnings from self-employment of all others. However, we only target such income over \$500,000 a year under the following rate structure:

- \$500 thousand to 1 million: 45%
- 1 to 2 million: 50%
- 2 to 4 million: 55%
- 4 to 6 million: 60%
- 6 to 10 million: 65%
- 10 to 25 million: 70%
- Above 25 million: 75%³⁶

Personal services income below \$500,000 and all other income will be taxed in the normal fashion.

However, the excess charge over 39.6% is not permanently lost to the taxpayer. Instead, it is converted to bonds for which the federal government is obligor. The government will annually pay interest on the bonds to the taxpayer at the then current rate of inflation, in a fashion somewhat similar to the Treasury's I-Bonds.³⁷ Furthermore, we propose that this interest be taxed similarly to I-Bonds, currently taxable by the federal government and tax-exempt for state tax purposes.

Unlike conventional bonds, these bonds will not have a fixed maturity or be transferable by the holder. Instead, the bonds begin to ma-

36. We stop our rate increases at 75% for two reasons. First, most states impose income tax, with some being as high as 11% (e.g., Hawaii, discussed *supra* note 16), and our targeted taxpayers would likely also have to pay Medicare tax (1.45% for employees, approximately 2.9% for self-employed). To impose a charge that in some cases might approach 90% appears confiscatory in nature. We believe that there should be some spendable cash flow derived from the good fortune of such steep salaries, even beyond \$25 million. Linder, *supra* note 25, at 923 and accompanying text, cites Republican Senator Reed, arguing to cut tax rates in 1956 down to 75%: "it seems reasonable enough that any individual be permitted to keep at least one quarter" of his income. As to our starting point of \$500,000, we chose this number because it is double the \$250,000 amount that was often used by Obama during and after the campaign as a threshold amount for considering who would not see possible tax rate increases. See Meckler, *supra* note 24 (discussing the \$250,000 threshold).

37. U.S. Dept. of the Treas., TreasuryDirect, *I-Bonds Rates & Terms*, available at http://www.treasurydirect.gov/indiv/research/indepth/ibonds/res_ibonds_iratesandterms.htm. Another bond vehicle offered by the U.S., also designed to protect against inflation, is the so-called TIPS, See *Treasury Inflation-Protected Securities (TIPS)*, available at http://www.treasurydirect.gov/indiv/research/indepth/tips/res_tips.htm. See Copeland, *supra* note 12 (describing China's preference for the protection of TIPS).

ture once the taxpayer turns 70 years old, under rules similar to the distribution requirements for Individual Retirement Accounts, including paying out as an annuity over the remaining expected life of the taxpayer. The bonds would be paid earlier in several cases. First, the bonds are redeemed upon death of the taxpayer, at which point the principal amounts are paid to the human beneficiaries of the taxpayer or to U.S. charities designated by the taxpayer. If the beneficiaries are humans, they will be paid in the form of an annuity over their expected remaining lifetimes.

There are two other instances in which we propose that the bonds may be redeemed earlier. First, the federal government may redeem them at any time, with no early redemption premium. For example, the federal government may encounter budget surpluses - similar to those last enjoyed under President Clinton. It is conceivable that a technological breakthrough, such as discovery of a new energy source, could provide the U.S. government with a 21st century version of the post-Cold War "peace dividend" or Clinton's "internet boom." Returning funds in future "good" years to bond holders who provided cash flow in the difficult years is more equitable than an approach that lowers tax rates in future "good" years, because the beneficiaries of reduced tax rates may not necessarily be the same individuals who suffered high taxes during the difficult years.

Second, for certain hardships during the taxpayer's lifetime, amounts necessary to pay costs related to the hardship may be permitted. In this case, rules similar to those used to avoid 10% penalties on early withdrawals from pre-tax retirement accounts may be applied (*e.g.*, medical bills).³⁸ We also propose that the bonds be available for liquidation in the event of the taxpayer's bankruptcy in order to pay debts to unrelated parties.

At this initial stage of consideration, we believe taxpayers should not be permitted to post the bonds as collateral for loans. Our concern is that a "market" for the bonds may indirectly occur, which might violate the spirit of our design that the bonds not be transferable before the maturity dates indicated earlier.

Finally, we recommend that the redemption of the principal of the bonds not be a taxable event for income tax purposes, since it will be viewed as a return of capital. However, just as is the case with most other savings vehicles, we expect the bonds to be part of the decedent's taxable estate. Therefore, methods currently employed to avoid estate tax can be used to shield estate tax on the bonds, such as

38. I.R.C. § 72(t)(2) (2009).

the decedent leaving the bonds to a spouse or donating to a U.S. charity.

IV. ESTIMATES OF CASH FLOW FROM BONDS

In this section we provide rough estimates of how much money possibly could be raised from the bond sales. The first computation, made with assumptions that likely underestimate the bond purchase calculations, estimates how many bonds would be sold to the taxpayers for whom we have aggregate Internal Revenue Service (IRS) data. For the approximately 18,000 taxpayers with over \$10 million in AGI in 2007, we project that they would have purchased approximately \$20 billion in bonds under the proposal.³⁹ For the 28,000 taxpayers with AGI between \$5 and \$10 million, the amount is \$10 billion;⁴⁰ for the 109,000 taxpayers with between \$2 and \$5 million of AGI, the amount is at least \$5 billion.⁴¹ These calculations show that it can be expected that at least \$35 billion of bond purchases would occur per year; if conservative assumptions we employ in our calculations were relaxed, it is likely that these estimates would be doubled.⁴²

Forecasting based on aggregate data is obviously difficult. Furthermore, detailed information on salaries of specific taxpayers is not provided by the IRS nor is it publicly available. Nonetheless, we have attempted to calculate how much in bonds could be sold based on the

39. This calculation is derived from statistics provided in IRS Publication 1304, *supra* note 20. For ease of calculation, the \$20 billion figure assumes salary income and business profits are earned evenly among the taxpayers, and that a tax return that reports salaries does not report business profits (and vice versa). Due to the progressive nature of the bond purchase rates, these assumptions dramatically underestimate the purchases. There were over 18,000 tax returns with total AGI of \$561 billion that each reported AGI over \$10 million. Of these returns, 15,000 reported salaries of \$90 billion and 13,000 reported \$89 billion of business/profession and partnership/Subchapter S income.

40. This calculation is determined in a fashion similar to the method described in note 39. There were over 28,000 tax returns with total AGI of \$192 billion that each reported AGI between \$5 and \$10 million. Of these returns, 23,000 reported salaries of \$52 billion and 21,000 reported \$41 billion of business and partnership/Subchapter S income.

41. This calculation is determined in a fashion similar to the method described in note 39. There were 109,000 tax returns with total AGI of \$325 billion that each reported AGI between \$2 and \$5 million. Of these returns, 87,000 reported salaries of \$104 billion and 80,000 reported \$80 billion of business and partnership/Subchapter S income.

42. As detailed *supra* note 39, we make assumptions that underestimate the calculation of purchases. These assumptions also lead to the inability to trigger purchases by those with AGI under \$2 million. A very rough calculation that suspends these assumptions approximately doubles the amount of likely sales to those with AGI over \$2 million. It also would allow us to calculate bond purchases by those with AGI under \$2 million. There were nearly 900,000 tax returns with total AGI of \$765 billion that each reported AGI between \$500,000 and \$2 million, reporting \$335 billion of salaries and \$180 billion of business and partnership/Subchapter S income. Note that 726,000 taxpayers reported the salaries of \$335 billion; however, again, we do not know how many of these earned over \$500,000 in salaries.

personal service income of 1,155 individuals for whom estimated earnings information is available through public sources.

In the sport of baseball alone, the top one hundred paid players will earn an average of \$13 million in 2009.⁴³ High salaries are also paid to athletes in other major team sports, such as basketball, football, and hockey, and prize winnings are in the multiples of millions for the elite players in golf, auto racing, and boxing.⁴⁴ The most financially successful celebrities and performers in the arts, such as actors and musicians, also annually earn in the millions of dollars, oftentimes more than most sports figures.⁴⁵ Furthermore, many of these public figures earn millions in endorsement deals and appearance fees. Turning to the business world, in 2007, there were nearly 1,000 reporting officers of publicly traded firms who each earned over \$1 million in salary and bonus.⁴⁶

We calculate \$1.487 billion as a rough estimate of the amount of bonds that would be sold to these individuals, summarized in Exhibit 1. This calculation is determined by taking the individual's reported income and applying our proposed rates listed above. We ignore any tax deductions or tax shelters these individuals may actually have, as we assume they likely offset other income they may have, such as portfolio income. The "Bonds Sold" column represents the additional funds the U.S. government would annually receive above the tax rate of 39.6%.

43. Calculations based on salary data in Associated Press, *Baseball's Top 100 Highest-Paid Players*, FOX SPORTS, Apr. 9, 2009, available at <http://74.125.95.132/search?q=cache:iHnYdlDnChUJ:feeds.foxsports.com/mlb/story/9434658/Baseball%27s-top-100-highest-paid-players+fox+sports+baseball%E2%80%99s+top+100+highest-paid-players&cd=1&hl=en&ct=clnk&gl=us>.

44. For a list of the highest paid fifty athletes in 2007, see Jonah Freedman, *Ranking the 50 Highest-Earning Athletes in the U.S.*, SPORTS ILLUSTRATED, available at <http://sportsillustrated.cnn.com/more/specials/fortunate50/2008/index.html>. For our calculations in Exhibit 1, the athletes who are baseball players have been removed to avoid duplication.

45. For data on these celebrities, see *The Celebrity 100*, FORBES, June 3, 2009, available at http://www.forbes.com/lists/2009/53/celebrity-09_The-Celebrity-100_EarningsPrevYear.html.

46. Data provided by Compustat, a service of Wharton Research Data Services. Frequently, these employees also enjoy additional income based on factors outside their control, such as stock-based compensation windfalls or severance/golden parachutes. However, to be conservative, we omitted these amounts from our calculations. Because data on publicly traded firms' compensation for key insiders is readily available, there are many studies of this data. For example, Forbes analyzes the total compensation of CEOs at the top 500 publicly traded firms. They report an average salary for these top 500 CEO's of \$11.4 million. Scott DeCarlo, *What the Boss Makes*, FORBES, Apr. 22, 2009, available at <http://www.forbes.com/2009/04/22/compensation-chief-executive-salary-leadership-best-boss-09-ceo-intro.html>. See also Ellen E. Schulz, *Pay of Top Earners Erodes Social Security*, WALL ST. J., July 21, 2009, at C4 (reporting that highly paid employees, including primarily executives, received nearly \$2.1 trillion of the \$6.4 trillion in total U.S. pay in 2007). NOTE THAT THE SUM OF THE SALARIES REPORTED IN IRS DATA FOR THOSE WITH AGI OVER \$500,000 IS APPROXIMATELY A QUARTER OF THE \$2.1 TRILLION. See IRS Publication 1304, SUPRA notes 20.

EXHIBIT 1: Summary of Projected Bonds Sold for Various Taxpayers
(dollar amounts in millions)

| | <u>Number of Taxpayers</u> | <u>Services Income</u> | <u>Bonds Sold</u> |
|--|--------------------------------|----------------------------|-----------------------|
| Celebrities | 25 | \$2,168 | \$ 707 |
| Athletes (Other than Baseball Players) | 44 | 1,089 | 294 |
| Baseball Players | 100 | 1,307 | 280 |
| Key Employees at Publicly Traded Firms | 986 | 2,062 | 206 |
| | <u>1,155</u> | <u>\$6,626</u> | <u>\$1,487</u> |

Extrapolating from these calculations to the full population is difficult. It seems reasonable to speculate that this amount would be much larger when we factor in all other taxpayers earning over \$500,000 in annual personal service income. For example, there are approximately three thousand other players in the four major team sports not accounted for above, many of whom also earn over \$500,000. There are countless profitable privately held firms, for which salary information is not publicly available, but at which manager salaries are likely comparable to publicly traded firms.⁴⁷ Turning to professional service firms, the average partner earns \$1.26 million at the 100 top-grossing law firms,⁴⁸ and clearly there are thousands of partners/directors/key executives in accounting⁴⁹ and other consulting/personal/financial service firms who also earn over \$500,000.⁵⁰

If only 1,155 individuals can generate nearly \$1.5 billion in bond sales – it seems reasonable to expect that it is possible to achieve the minimum of \$35 billion we estimated previously based on aggregate IRS data for the 155,000 taxpayers with AGI over \$2 million. After relaxing the assumptions made in making those aggregate calculations, including all who earn over \$500,000 a year, it would not be surprising if ulti-

47. The estimated average salary of 302,000 chief executive officers in all industry sectors across the U.S. is \$160,440; information is not provided on how many earn over \$500,000. Bureau of Labor Statistics, *May 2008 National Occupational Employment and Wage Estimate*, available at http://www.bls.gov/oes/2008/may/oes_nat.htm#b00-0000.

48. Aric Press & John O'Connor, *Lessons of the Am Law 100*, AM. LAW., May 1, 2009. The estimated average salary of 554,000 lawyers is \$124,750 (a figure that includes non-partners); information is not provided on how many earn over \$500,000. Bureau of Labor Statistics, *supra* note 47.

49. THE AVERAGE NET INCOME PER CPA FIRM PARTNER IS \$407,000 FOR FIRMS WITH MORE THAN 50 EMPLOYEES. EXCLUSIVE SURVEY: KEY DATA HELP STRATEGIC FIRMS WITH 2009 PARTNERSHIP PLANNING, PARTNER'S REPORT, Jan. 2009. This average was likely brought down by the many CPA firms other than the "Big 4."

50. For example, the estimated average salary of 34,000 anesthesiologists is \$197,570; information is not provided on how many earn over \$500,000. Bureau of Labor Statistics, *supra* note 47.

mately nearly \$100 billion in bonds are sold per year to hundreds of thousands of taxpayers.

V. COMPULSORY BONDS AS TOOL FOR AMERICANS TO SAVE AND REINVEST IN THE U.S.: A 21ST CENTURY “WAR BOND”

In a sense, the proposed compulsory bonds are akin to “War Bonds” sold by the U.S. government to help fund its wars in centuries past. While the onset of the current economic crisis was more attributable to a crisis of confidence in markets rather than the fact that the U.S. is presently engaged in two protracted military actions in Iraq and Afghanistan, the current demands on government are similar to the demands of past large wars. Robert Hormats, writing shortly before the economic crisis that unfolded at the end of 2008, summarized the history of U.S. financing of wars:

For much of America’s history, the White House and Congress have recognized the inevitability of massive borrowing when the nation’s security has been threatened, and for the most part they have tried to structure that borrowing to strengthen national unity. Hamilton called a well-funded debt a “national blessing” because it gave Americans who held federal securities an interest in supporting the fledgling post-Revolutionary government. Lincoln saw bond sales as a way to more closely tie greater numbers of Northerners to the Union’s cause. [Woodrow Wilson’s and Franklin Roosevelt’s Treasury secretaries] initiated patriotic bond drives to enable Americans not directly engaged in the world wars to make a contribution.⁵¹

Hormats also reports that the “most striking aspect of wartime financing was the degree [of Americans’] economic sacrifices. . . . Fiscal policy was structured to strengthen support for the war effort by demonstrating that it was being financed fairly, and by using bond drives as devices for encouraging large numbers of people to demonstrate their patriotism.”⁵² Marketers of the bonds provided a “more compelling way to use the concept of the future to sell bonds,” presenting them not as a financial investment but as “an investment in Americans’ lives and in the nation itself,” including the use of posters such as “Your Bonds Are a STAKE in the Future.”⁵³ Furthermore, beyond war financing, Treasury officials viewed the bond sales as a means to

51. HORMATS, *supra* note 13, at 290.

52. *Id.* at 132-33.

53. LAWRENCE R. SAMUEL, PLEDGING ALLEGIANCE: AMERICAN IDENTITY AND THE BOND DRIVE OF WORLD WAR II 52 (1997).

curtail the rising threat of inflation, “the home front equivalent of a treacherous foreign foe.”⁵⁴

We concede that America’s war bonds were *voluntarily* purchased, by the wealthy *and* not so wealthy, to show patriotism during war.⁵⁵ In our proposal, we “impose” patriotism, and it is imposed solely on the highest earners. However, this may be considered only fair because the success of many of these individuals is often only made possible by the success of their country. By taking a stake in their country’s future financial stability, these taxpayers are investing (reinvesting) in their country’s ability to provide them future success and security. It also provides a signal to creditor nations that these Americans, many of whom have high public profiles, share their risk in investing in the U.S.

We also concede that collecting cash of between \$35 and \$100 billion a year, as we project in Section IV, may not make a dramatic direct impact on the government’s budget.⁵⁶ However, this approach would help instill confidence in foreign creditors. In the business setting, it is not uncommon for lenders (and equity investors) to require that employees and other equity investors have “skin in the game.” For example, many real estate deals carefully scrutinize loan-to-value ratios to make sure the buyer/borrower has enough of a down payment, and many debt covenants on large loans contain ratios related to levels of debt to equity.

Furthermore, the compulsory bond will help such taxpayers create and secure their own personal wealth.⁵⁷ Americans are notorious for

54. *Id.* at 10. Government could not only fund the war, but also stem inflation “simultaneously by taking money out of consumers’ hands and putting it into its own.” *Id.*

55. It is interesting to note that by 1941 advisors favored Roosevelt to force individuals to buy the bonds, arguing compulsion would avoid the experience of World War I fund raising, during which community pressure stigmatized those who would not buy bonds. Ultimately, advocates of the voluntary purchase approach won, arguing that it would “make the country war-minded” and “give people an opportunity to do something” more for the war effort. RONALD H. BAILEY, *The Home Front: U.S.A. 108-09* (1978). See also DONALD JOHN MARKWELL, JOHN MAYNARD KEYNES AND INTERNATIONAL RELATIONS: ECONOMIC PATHS TO WAR AND PEACE 217-18 (2006) (describing policy makers urging of the Roosevelt administration to adopt a version of Keynes’ compulsory savings/deferred pay proposal (discussed *infra* notes 67-76 and accompanying text)); SAMUEL, *supra* note 53, at 29 (because not enough bonds were being sold at one point, “As a backup, a compulsory savings plan was prepared to be quickly put in place on July 1, 1942, should the Treasury’s bond program continue to falter”).

56. For a similar opinion in the context of raising income tax rates, see David Wessel, *Taxing Rich Wouldn’t Close the Gap, but would Shrink it*, WALL ST. J., Sept. 3, 2009, at A4 (also citing Professor Slemrod – “The 1990’s suggests we could raise more money from high-income people . . . and still have a strong economy”).

57. While this Article is proposing compulsory bond purchases for those making over \$500,000, it is possible to imagine extending the program to middle income taxpayers (or even lower income taxpayers) if a need arises. See SLEMROD & BAKIJA, *supra* note 14, at 286-87

being consumers rather than savers,⁵⁸ unlike the citizens of many of our creditor countries.⁵⁹ While there are debates over whether suppression of consumption might be damaging during an economic recovery, all agree savings must increase.⁶⁰ Many economists agree that most tax incentives to increase savings have a limited, even ambiguous, impact on net savings.⁶¹ In our case, we use the tax law to force Americans' savings by compelling the bond purchase.⁶² As noted by one author, writing about the war bonds:

From a lay point of view, bonds made one feel richer, whereas taxes made one feel poorer, and common sense suggested that gaining the support of ordinary citizens would be easier . . . if Americans felt they were not only contributing to a national cause but also gaining financially. . . . Bonds would act as a physical reminder of the owner's stake in the European war, stand as a symbol of unity to potential enemies, and ultimately be the seeds for postwar economic prosperity Bonds thus represented not only a means of combating wartime inflation but a promise of postwar economic stability and prosperity.⁶³

Furthermore, by providing for repayment of bond principal to those taxpayers who bought them, the proposal improves on typical scenarios in which government reduces tax rates in good years for *all* taxpayers, not just those who paid high taxes in prior years.

Many economists now take seriously the idea that certain people are unable to commit to save as much as they 'should' and that the problem is particularly severe for low- and moderate-income people, as both pressures to spend today and the consequences of under-saving are the worst for this group. . . . This could support a case for going beyond removing distortions [in the tax law as to incentives] and perhaps subsidizing saving among low-income people, as well as creating institutions that do a better job of getting low- and moderate- income people in the habit of saving.

58. PETERSON, *supra* note 3, at 202 (writing before the recent economic crisis, which has clearly dampened U.S. consumption, "America's propensity to consume and its disinclination to save are deeply ingrained in the [American] psyche"). Meanwhile, there are signs that U.S. consumers are continuing their appetite for spending even as their incomes lag, as evidenced by Commerce Department data for August 2009. Martin Crutsinger, *Consumer Spending Jumps 1.3 percent in August*, ASSOC. PRESS, Oct. 1, 2009.

59. For a comparative analysis between 1993 and 2006 of household net saving rates as a percentage of their disposable income in the U.S. and other countries, see OECD FACTBOOK 2008: Macroeconomic Trends: Economic Growth: Household Saving, available at <http://lysander.sourceoecd.org/pdf/factbook2008/302008011e-02-02-02.pdf>.

60. PETERSON, *supra* note 3, at 202. Additionally, "[n]o one could disagree with [the] objective" of "a significant increase in net savings by households." *Id.* Indeed due to the current crisis, many Americans have cut back on consumption and thus have led to the highest savings rates in 15 years. Rich Miller & Alison Sider, *Surging U.S. Savings Rate Reduces Dependence on China (Update2)*, June 26, 2009, available at http://www.bloomberg.com/apps/news?pid=20601109&sid=aome1_t5Z5y8. But see Crutsinger, *supra* note 58 (suggesting that August 2009 data shows Americans may be returning to consuming more than they earn).

61. PETERSON, *supra* note 3, at 202.

62. Peterson believes that if we wanted a significant increase in net savings "we would have to make it *mandatory*." *Id.* (emphasis in original).

63. SAMUEL, *supra* note 53, at 11, 15, 29.

Turning to outside the U.S., there have been instances in other countries where compulsory loans somewhat similar to our proposal have been used or contemplated. For example, China has required employees to lend money to their employers,⁶⁴ Brazil law allows for compulsory loans to finance certain public calamities,⁶⁵ and Israel has also employed such loans.⁶⁶ Experience in three other countries – England, the Soviet Union, and Germany – are discussed next.

In late 1939, the famous economist John Maynard Keynes argued for a compulsory loan program as a way for England to pay for the soon-to-arrive World War II and to avoid inflation.⁶⁷ He proposed that employers withhold a portion of workers' pay and deposit it with the government Post Office Savings Bank as a form of compulsory savings.⁶⁸ The money would be kept in interest bearing accounts and

64. In China, “[i]n an ideologically inoffensive move designed to make socialist ‘worker ownership’ compatible with individual incentives and profits, enterprises were allowed to issue incentive shares to [workers so that they would have] greater incentives to make the enterprise more profitable. In the early 1980s, however, as enterprises became insolvent, incentive shares originally intended to boost worker morale transmogrified into compulsory bonds forced onto employees by money-losing enterprises as a substitute for monetary compensation.” Lan Cao, *The Cat That Catches Mice: China’s Challenge to the Dominant Privatization Model*, 21 *BROOK. J. INT’L L.* 97, 156 (1995).

65. In article 148 of the Brazilian Constitution, the federal union may institute “*empréstimos compulsórios*,” which are compulsory loans to defray extraordinary expenses resulting from public calamities, war, and in the event of a public investment that is urgent and of relevant national interest. José Marcos Domingues, *Environmental Fees and Compensatory Tax in Brazil*, 13 *LAW & BUS. REV. AM.* 279, 283 (2007). In 1986, in an effort to help combat inflation and draw capital for projects, the government implemented a compulsory loan, under which a 28% surcharge was imposed on gas sales and 30% on new car sales. These loans were to be refunded in three years with interest of 6% a year. Government economists also expected the transfer of funds to the government to dampen demand for consumer goods. Juan de Onis, \$100-BILLION TAX PLAN BASED ON Compulsory Savings; Brazil MIDDLE CLASS TO FUND AID TO POOR, *L.A. TIMES*, July 26, 1986, at 3; MICHAEL BRUNO ET AL., *INFLATION STABILIZATION: THE EXPERIENCE OF ISRAEL, ARGENTINA, BRAZIL, BOLIVIA AND MEXICO* 236 (MIT Press 1988).

66. See description of the loans in Warren L. Young, *Tax Illusion and Savings Perception: The Case of Compulsory Loans*, 122 *DE ECONOMIST* 440 (1970) (describing Absorption loans, Defence loans and other loans; some loan certificates, which were long term bonds that bore interest, were linked to the cost-of-living index, and redemption could be opted for on or before bond maturity and were negotiable, although they were received only after a great lag, and, even after distribution, market trading in the certificates only proceeded after another long lag).

67. ROBERT SKIDELSKY, *JOHN MAYNARD KEYNES, FIGHTING FOR FREEDOM, 1937-1946* 55 (Viking Press 2000). Keynes argued that citizens had a choice: “compulsory savings or compulsory inflation.” *Id.* at 59. Keynesian economics have experienced a revival after the onset of the 2008 economic crisis. See, e.g., Justin Fox, *The Comeback Keynes*, *TIME*, Nov. 3, 2008, at 60; *The Keynes Comeback*; John Maynard Keynes, *ECONOMIST*, Oct. 3, 2009, available at http://www.economist.com/books/displaystory.cfm?story_id=14539560 (describing newly published books about Keynes); Pietro Alessandrini & Michele Fratianni, *Resurrecting Keynes to Stabilize the International Monetary System*, 20 *OPEN ECONOMIES REV.* 339 (July 2009).

68. SKIDELSKY, *supra* note 67, at 55.

repayable after the war in installments - the higher the wages, the lower the repayment percentage.⁶⁹

Keynes' approach would "drastically [restrict]" the consumption of the rich "without imposing penal, disincentive tax rates."⁷⁰ The approach was the only means whereby "war sacrifices could be in proportion to ability to bear them."⁷¹ A contemporary of Keynes summarized the comparative advantage the compulsory bond approach had over taxation:

The advantage most urgently claimed for both compulsory lending and compulsory saving is that, as compared with taxation, they preserve the incentive to work. Workers will be more willing to work harder and longer if they feel that they are only temporarily deprived of the fruits of their labor, and that they may enjoy these fruits after the war when goods are once more abundant. [Another] advantage [is] that large total levies on all income groups become more acceptable when a promissory note is substituted for a tax receipt. Finally, the compulsory lending and saving schemes would create a reserve of individual purchasing power for the post-war period.⁷²

However, the English government objected, with what amounted to procedural concerns, including a desire for more data on the effects of the proposal.⁷³ More critically, Keynes was unable to obtain the support of workers, who considered it "highly doubtful" that the loans would be repaid, particularly because of, in their view, the long tradition of broken promises by the government to workers.⁷⁴ In the end, Keynes struck an "unsympathetic chord" with the socialistically inclined Labourites.⁷⁵ While Keynes' plan drew much attention of influential policy makers in the U.S.,⁷⁶ his plan was not implemented in England.

In 1930's Soviet Russia, there was what amounted to a compulsory deduction from workers' wages for the purchase of government

69. *Id.*

70. *Id.*

71. DUDLEY DILLARD, *THE ECONOMICS OF JOHN MAYNARD KEYNES* 252 (Prentice-Hall 1948).

72. Paul Randolph, General Counsel of the Treasury, Fiscal Policy and Inflation, Speech Before the American Academy of Political and Social Science (Nov. 30, 1942), available at <http://www.taxhistory.org/Civilization/Documents/Fiscal/hst29024.htm>.

73. SKIDELSKY, *supra* note 67, at 69-70.

74. DILLARD, *supra* note 71, at 321 (also pointing out that the workers were concerned that even if the loans were repaid, inflation would have reduced their value).

75. *Id.* See also DONALD E. MOGGRIDGE, *MAYNARD KEYNES, AN ECONOMIST'S BIOGRAPHY* 631 (Routledge 1992) (the left leaning press, Labour party, and trade union leaders were all hostile to Keynes' plan).

76. MARKWELL, *supra* note 55, 215-19.

bonds.⁷⁷ It was customary for workers at a union local's meeting to vote to subscribe to the bonds because no worker "dared to oppose a resolution in a union meeting."⁷⁸ Early on, workers felt the cash flow pain and thus started selling off the bonds.⁷⁹ The government responded by requiring permission of a special committee before any sale, and such permission would be granted only in serious need cases, such as illness.⁸⁰ The compulsory bond program continued for several more decades, including a sharp reduction by 1953, and then was ultimately abandoned in 1957, at which time a twenty year moratorium on repayment was imposed.⁸¹

After World War I ended, Germany was required to make reparations to the victors of the war. This required cash flow. The German government decided to implement a graduated compulsory loan program, to be subscribed to by all persons with over a hundred thousand marks in property, during the second half of 1922, and such bonds would not bear interest until the latter part of 1925.⁸²

Although the German post-World War I approach was short-lived, a version of it was offered in late 2008 by a little-known Social Democrat candidate fighting an uphill battle to be governor of a German state – his "unconventional idea" was that Germans with cash and real estate assets over \$750,000 (slightly over \$1 million) should be forced to lend the government two percent of their assets for 15 years at an interest rate no higher than 2.5 percent.⁸³ He was quoted as saying: "A compulsory state bond would be a rapidly effective instrument to mobilize additional funds to overcome the economic crisis [and] would be very fair because only the very wealthy would be drawn on."⁸⁴

77. CALVIN B. HOOVER, *ECONOMIC LIFE OF SOVIET RUSSIA* 251-52 (Macmillan & Co. Ltd 1931).

78. *Id.* at 251.

79. *Id.* at 252.

80. *Id.*

81. ALEC NOVE, *AN ECONOMIC HISTORY OF THE U.S.S.R.* 254, 309, 323-24 (Penguin Press 1969). For a quantitative analysis of the bond's economics, see Franklin D. Holzman, *An Estimate of the Tax Element in Soviet Bonds*, 47 *AM. ECON. REV.* 390 (1957).

82. See GERALD D. FELDMAN, *THE GREAT DISORDER: POLITICS, ECONOMICS, AND SOCIETY IN THE GERMAN INFLATION* 428 (Oxford Univ. Press 1997); GUSTAV STOLPER, KARL HAUSER & KNUT BORCHARDT, *THE GERMAN ECONOMY 1870 TO THE PRESENT* 81 (Harcourt, Brace & World, Inc. 1967).

83. *German Politician Wants Compulsory Bond for Rich People*, Spiegel Online, Dec. 22, 2008, available at <http://www.spiegel.de/international/germany/0,1518,597945,00.html>.

84. *Id.* In the January 2009 election, this politician and his party failed to beat the incumbent. World Elections, *Hesse 2009: Results*, Jan. 19, 2009, available at <http://welections.wordpress.com/2009/01/19/hesse-2009-results/>.

Of the three described approaches, our proposal is closest to the Keynes approach – the compulsory savings (also known as “deferred pay”) proposal. Because our approach compels purchases from very high earners, it differs from the Soviet approach, which applied to all workers and whom, as is the norm in Communist regimes, typically had the same low salary. Our approach also differs from the German setting, which calculated the bond purchase based on current wealth, which is a function of past income of any nature and all endowments. Our approach is based on current earnings from personal services and it cannot be viewed as confiscatory as the German approach. Since our proposal is similar to Keynes’ approach, which was defeated primarily because of union worker’s objections, our version’s targeting of high earners will help it succeed in the 21st century U.S.

VI. ADDRESSING POSSIBLE OBJECTIONS TO THE COMPULSORY BOND PROPOSAL

A. *Is the Bond Purchase a Form of Confiscatory Taxation?*

Professor Linder, in his extensive analysis regarding the historical debate over progressive taxation in the U.S., discusses resistance to what arguably are confiscatory tax rates. He expresses the view of the American Bar Association in 1951 as it resisted progressive tax rates as high as 92%:

Of special interest to the members of the ABA was the claim that ‘the elimination of the wealthy and middle class through . . . [progressive taxation] . . . was absorbed by the democracies from the Communist Manifesto . . . [and] has made it almost impossible for lawyers any longer to leave much of an estate. . . . The same thing is true of their clients.’⁸⁵

Linder also cites Senator Dirksen, in 1956, as stating that “If you are going to have socialism all you need is heavy progressive income tax and confiscatory estate taxes so that when a man leaves this earth the government just takes all.”⁸⁶

The concerns just described are not present under our compulsory bond program, because the government will not confiscate these excessive salaries; it merely constrains how the taxpayer can invest them until the bond is redeemed. Furthermore, as noted earlier, our proposal does not impose an expense on the taxpayer. Instead, it imposes a constraint on how a portion of their wealth may be used until redemption, since we require it to be saved (invested in government bonds)

85. Linder, *supra* note 25, at 957-58.

86. *Id.* at 967.

and paid out to the holder when he reaches 70 years old or to his heirs or charities after death. The government does not permanently keep the money.

B. *Would the Compulsory Bond Program Create Disincentive to Work?*

Another concern that might be raised is whether the compulsory bond purchase program will deter economic activity of affected taxpayers. Obviously, to the extent the government needs cash flow and is compelled to raise taxes, our approach is an improvement in that it permits the affected taxpayers to maintain their wealth. Andrew Mellon, one of the best known American capitalists and secretary of the Treasury for over a decade, stated in 1924 that, "it is a well-known fact that most people of great wealth use a comparatively small amount of their incomes for their own and their families' personal physical needs."⁸⁷ To the extent his view still applies, our proposal continues to allow taxpayers to save; again, we merely reduce their investment choices by directing some of their savings into government bonds.

The question arises whether individuals might stop exerting the efforts necessary to earn the excessive amounts that would become subjected to compulsory bond purchases. The loss of such efforts could be seen as a loss to the economy. Again, we do not seek to fight the battle over the merits of progressive taxation, including its effect on incentives to earn; however, we do offer the following arguments in support of our approach.

The tax law has long been used to provide incentives and disincentives. For example, the tax law provides a reduced tax rate on capital gains to motivate capital formation. Incentives, such as a 15% (instead of 35%) tax rate on the gains on sales of investments held at least one year, makes sense when funds could be put to different uses (*e.g.*, interest on low risk bonds are taxed at high rates, while returns to stocks, which are often high-risk, are typically taxed at lower rates). However, there is something very different about tax incentives and disincentives when we speak of labor. Compensation is paid for labor and if any time spent performing compensable labor is taxed on the margin at the same rate, we do not expect that the individual will "go elsewhere," as they might with their investment funds.⁸⁸ Except for

87. Linder, *supra* note 25, at 161.

88. For a discussion of the preference to have compensation taxed as self-employment income as opposed to employment income, see James E. Long, *The Income Tax and Self-Employment*, 35(1) NAT'L TAX J. 31 (March 1982). Note that this setting involves the worker continuing to work: he merely decides whether he does so as an employee or as a self-employed person.

the choice to not work as discussed below, the employee cannot go to a country with lower tax rates to work because, as a U.S. citizen, he is still obliged to pay U.S. income tax.⁸⁹ In other words, a person's labor is not as mobile as his capital.

In analyzing labor decisions, economists speak of a "reservation wage rate," a rate of compensation under which the laborer rejects a given job. However, one economist recently pointed out that, when analyzing a tradeoff between the marginal hour of work and leisure, it is wrong to assume the marginal utility of work is zero beyond the pay rate because leisure is taken as intrinsically satisfying; in other words, many economists wrongly view work as having a cost of the value of the lost leisure.⁹⁰ To most casual observers, high end earners have a certain (often necessary) passion for their livelihoods, which provides them utility; for instance, if an hour of labor generates \$100 of salary and an hour of leisure is worth \$100 to the worker, the worker will prefer to work the marginal hour as long as he derives any enjoyment from the work itself.

As casual observers of human behavior, most would agree that some activities by taxpayers would be undertaken regardless of tax rates. We expect that the highest paid baseball player, Alex Rodriguez of the New York Yankees, would play just as hard for \$500 thousand a year as he would for his 2009 annual salary of \$33 million.⁹¹ Although often viewed as a cliché or hyperbole, there can still be sincerity when a prospective job applicant claims he loves the field so much "he'd work for free." A renowned European basketball player, Ricky Rubio, was recently quoted as saying that he would play for free to be able to play in the U.S.A.'s National Basketball Association.⁹²

There are probably more than a thousand professional sports players who earn over \$500 thousand a year and likely would play just as hard whether their marginal tax rate on salary over \$500 thousand was 35% or 45%. This is also true of many professionals outside of sports. Think of the many *pro bono* cases lawyers take on - or the research articles tenured faculty continue to publish (probably not a good example, given the rarity of professors earning over \$500 thousand in

89. Even if the citizen wishes to surrender their U.S. citizenship, it is very difficult to avoid paying taxes for a long period. See I.R.C. § 877 (26 U.S.C. § 877 (2008)).

90. David A. Spencer, *Work for All Those Who Want it? Why the Neoclassical Labor Supply Curve is an Inappropriate Foundation for the Theory of Employment and Unemployment*, 30 CAMBRIDGE J. ECON., 459, 461 (2006).

91. Data available at source reported at *supra* note 43.

92. Henry Abbott, *Ricky Rubio Would Play for Free*, June 24, 2009, available at <http://myespn.go.com/blogs/truehoop/0-41-141/Ricky-Rubio-Would-Play-for-Free.html>.

personal services income!). It is also true for actors. For example, in 2001, Keanu Reeves, a box office major attraction, was reported as not always seeming “motivated by money. In fact, on several films he has literally handed over part of his salary to other actors or crew.”⁹³

Turning to the corporate world, including highly paid corporate officers, one could argue that a CEO might prefer to ease up, or perhaps even retire, rather than work harder for a bonus that will be taxed at higher rates than before. A half century ago, J. Keith Butters summarized the findings of many who studied executive behavior. The consensus was that taxes are not a determinant in the effort exerted by executives, given that cash was not their only motivation to work hard.⁹⁴ He concluded, “[i]f continued high taxes are required . . . I know of no evidence pertaining to the United States which indicates that the harmful effect of taxes on work incentives is currently so great as to require immediate tax reductions despite these needs.”⁹⁵ Other articles at the time were of a similar view, not only for corporate executives but for other occupations as well.⁹⁶ Papers published in the subsequent decades confirm the lack of power that taxes have on labor decisions.⁹⁷

As noted earlier, a contemporary of Keynes, in summarizing the comparative advantage the compulsory loan and savings approaches

93. Tom King, *A NOT-ALWAYS-EXCELLENT ADVENTURE: ACTION STAR KEANU REEVES WANTS TO PLAY THE FIELD*, WALL ST. J., Sept. 6, 2001, at W8. *But see also* Linder, *supra* note 25, at 974-75 (citing comments by tax-cutting President Reagan, himself a former actor, who noted that some actors would quit after making a certain number of movies rather than pay a 90% tax rate).

94. J. Keith Butters, *Taxation, Incentives, and Financial Capacity*, 44 AM. ECON. REV. 504, 508 (May 1954) (noting that taxes may impact the use of deferrals, etc.). For more modern examples, see Abigail Hofman, *Work to Live not Live to Work*, Euromoney, Oct. 2006 (“Investment banking is exciting, addictive and financially rewarding. . . . For financiers, money is only part of [why we work]. Anyone who’s been in the industry longer than 15 years and still works for the money is a failure. However, self-image is often defined by work. ‘I am a managing director on Wall Street. Therefore I am.’ And the money is a way of keeping score.”); Nathan Cobb, *TAKE THE MONEY AND RUN? NOT THEM - FOR THE WEALTHY, JOB SATISFACTION GOES BEYOND MAKING RICHES*, Boston Globe, May 7, 2000, at A1 (interviewing an executive: “We have other people in the company worth over \$100 million, too. . . . ‘Why do we work?’ Because we really believe we have that mission.”).

95. Butters, *supra* note 94, at 510.

96. George Break, *Income Taxes, Wage Rates and The Incentive to Supply Labor Services*, 6 NAT’L TAX J. 333, 353 (Dec. 1953) (concluding that “income tax, even with relatively high marginal rates, is not likely to have serious disincentive effects so far as the aggregate supply of labor services is concerned”).

97. See, e.g., D.B. Fields & W.T. Stanbury, *Income Taxes and Incentives to Work: Some Additional Empirical Evidence*, 61(3) AM. ECON. REV. 435 (June 1971); Long, *supra* note 88. See also Joel Slemrod, *The Dynamic Tax Economist*, 56(3) TAX LAW. 611, 613 (2003) (“no convincing evidence that either aggregate labor supply or saving responds in a significant way to taxes. . .”).

had over taxation, noted that their “advantage most urgently claimed, compared with taxation, [is that they] preserve the incentive to work. Workers will be more willing to work harder and longer if they feel that they are only temporarily deprived of the fruits of their labor. . . .”⁹⁸ In other words, the worker “might well look at the growth of his total assets.”⁹⁹ Of course, the prospects of redemption of the bond would have to be “*vivid* so that the taxpayer would be glad to work more in order to accumulate such claims.”¹⁰⁰

By limiting our compulsory bond charges to personal service income, as opposed to all income, we believe we have limited any disincentive effects. There is no reason for bond holders to be as concerned as holders in the Soviet Union or post-World War I Germany about the value of their investment because we have included an inflation protection element. Furthermore, even if employees would not work as hard if they were to be taxed at higher marginal tax rates, clearly they would not be as de-motivated by a bond purchase (even if compelled) as they would by an outright tax, for which they will never see the money again.

VII. IMPLEMENTATION ISSUES

If the proposed approach is implemented, several issues requiring further consideration will arise. As to more mundane, procedural aspects, we note that current tax forms would require some additional lines, perhaps even a dedicated schedule, to calculate the amounts, including the segregation of income subject to the bond purchase from income subject to conventional income tax.

Also, will the approach allow for any form of lifetime income smoothing? For example, if a taxpayer has \$5 million of earnings from his sole proprietorship in one year, but lost that same amount over the next three years, how would this be handled? Our current leaning is, in the interest of ease of administration, not to allow any provisions similar to net operating loss carryforwards¹⁰¹ or the long-shelved income averaging approaches.¹⁰²

98. Randolph, *supra* note 72. Another advantage is “that large total levies on all income groups become more acceptable when a promissory note is substituted for a tax receipt.” *Id.*

99. *Id.*

100. ALBERT G. HART, DEFENSE WITHOUT INFLATION 122-23 (Twentieth Century Fund 1951) (emphasis in original).

101. 26 U.S.C. § 172(a), (b).

102. Income averaging was repealed for years after 1986. For a layman’s description of the approach, see Robert J. LaConte, *How to Handle Ten-Year Averaging and Income-Averaging Computations for This Season*, 20(2) PRACTICAL ACCOUNTANT 41 (Feb. 1987).

For taxpayers with cross border activities or relations, obviously there will be complications, primarily in the area of foreign tax credits. Examples include a Canadian who plays baseball in the U.S. for half the season, or an expatriate who is working in the U.S. for only three years. In the past, the IRS appeared to not want to treat refundable-type taxes as creditable for foreign tax credit purposes,¹⁰³ while the U.S.-Israel treaty allows Israeli compulsory loans to be creditable (with a reversal of the credit when the bond is redeemed).¹⁰⁴ Consideration will also be needed as to how to treat short term assignees to the U.S., perhaps with provisions similar to “totalization” agreements. These agreements permit certain expatriates to the U.S. to avoid paying U.S. social security taxes as long as they are sent to the U.S. for a short period of time and they are maintained by their current foreign employer in that country’s social security system.¹⁰⁵ We also expect some administrative complications for employers under expatriate equalization agreements; these are agreements under which employers often agree to pay their employees’ taxes; which often leads to tax “gross ups” – how would compulsory bonds (an asset) be treated under such plans?¹⁰⁶

The IRS would have to be even more vigilant in patrolling for taxpayers who seek to convert ordinary income into capital gain – or, under our approach, personal services income into *any* other kind of income. However, we do not expect that taxpayers should be penalized for entering into valid deferred compensation arrangements. For example, if Alex Rodriguez and the New York Yankees agree to a valid deferral arrangement that meets the currently required rules for tax deferral, which smoothes out his earnings over 30 years instead of 10; that is acceptable.

As with most newly enacted legislation, transition issues arise. It may be unfair to impose the bond purchases on those who have, in their own budgeting minds, already committed part of their future salaries to servicing, for example, costs of their residences. Thus, we recommend that the plan start no sooner than the tax year after

103. See, e.g., Rev. Rul. 67-187, 1967-1 C.B. 185 (special tax levied by Canada on corporations was not a tax but a compulsory loan and therefore not creditable since it was refunded, with interest, 18 to 36 months later). See also Rev. Rul. 59-70, 1959-1 C.B. 186 (describing Brazil’s compulsory loan arrangement and analyzing whether it qualified for foreign tax credit).

104. Article 26, Relief from Double Taxation, ¶ 2, available at <http://www.irs.gov/businesses/international/article/0,,id=169560,00.html>.

105. For example, see the U.S.-U.K. Totalization Agreement, SocialSecurityOnline, available at http://www.ssa.gov/international/Agreement_Pamphlets/uk.html.

106. See Stanley Veliotis, *The Effect of the U.S. Stimulus Tax Rebates on Equalization Programs*, 40(3) COMPENSATION & BENEFITS R. 60 (May/June 2008) (describing complications the 2008 Bush tax rebates had on equalization arrangements).

enactment, and perhaps include a gradual phasing in of the application of the rates to bands of income. For example, for the first year, the 45% rate could be applied to income between \$2 and 4 million, instead of the amount above \$500,000; in the following year, the rates we note above would then apply.

Some may argue that the proposal is fraught with administrative burdens, leading to transaction costs, both explicit and implicit. They may object that the IRS is designed to collect taxes, not act as “bank” or “broker” in terms of its new role of calculating bonds. There are two responses. First, we do not contemplate that the IRS will manage any aspect of the bond sales or redemptions other than the initial calculations, based on annual income tax filings, of how many bonds are to be sold to the taxpayer. All other aspects are to be handled by the Department of Treasury, just as it handles its other bonds. Second, even if the IRS took on more than a mere facilitator role, it would not be the first time the IRS played the role of “banker.” In 2008, to help support the crumbling housing market, a provision of the tax code was enacted that provided a tax credit for first time home buyers; the credit is paid back to the government in many cases after passage of time, and thus, amounts to a loan to the taxpayer.¹⁰⁷

Furthermore, there may be marketing concerns in educating the affected public about the proposal. In modern U.S. politics, what we call something can make all the difference.¹⁰⁸ For example, in the debate over the extent of health care reform in summer 2009, Obama and his advisors found that they needed to focus on “linguistic strategy.”¹⁰⁹ Earlier we described Keynes’ difficulty in convincing the British government to implement his compulsory savings plan. He later recognized that he had made a “tactical mistake” in talking about the term “compulsory savings” and later “substituted the more diplomatic ‘deferred pay’ in subsequent expositions.”¹¹⁰ To obtain

107. The first-time homebuyer credit was included in the Housing and Economic Recovery Act of 2008, Pub. L. No. 110-289, § 3011, 122 Stat. 2654, 2888-92. For homes purchased in 2008, the credit operates like an interest-free loan because it must be repaid over a 15-year period. The credit was expanded in 2009 for homes purchased in 2009, increasing the amount of the credit and eliminating the requirement to repay the credit, unless the home ceased to be the principal residence within the 36-month period beginning on the purchase date. For more on this new law, see Carol A. Pettit, *CRS Reports On First-Time Home Buyers’ Credit*, TAX NOTES, Mar. 20, 2009.

108. See, e.g., FRANK LUNTZ, *WORDS THAT WORK: IT’S NOT WHAT YOU SAY; IT’S WHAT PEOPLE HEAR* (Hyperion 2007).

109. Jonathan Weisman, *Obama Allies Find Words Fail Them*, WALL ST. J., Aug. 25, 2009, at A4. Dr. Luntz (referenced *supra* note 108) discussed this terminology on an August 25, 2009 Fox News show, available at <http://www.foxnews.com/search-results/m/26037234/war-of-words.htm>.

110. SKIDELSKY, *supra* note 67, at 59.

better acceptance by the high income earners of the compulsory bond program, experts should be engaged to review the use of terminology, perhaps even employing some of the patriotic themes discussed earlier in connection with helping to influence Americans to voluntarily buy war bonds. The government should also consider publicizing the plan to foreign holders and potential buyers of U.S. debt, and highlight how hundreds of thousands of Americans, including high profile Americans, now share their risk in a material way.

The current proposal includes bond purchases only for those taxpayers earning personal services income. It is possible the U.S. government may seek to expand the type of income subject to the purchases to all types of ordinary income (*i.e.*, all income that is not taxed at preferential rates, such as capital gains or qualified dividends). However, it may be best to focus any expansion of the base to income that is not likely to be subject to disincentive effects. Examples could include income from fortuitous events,¹¹¹ such as gambling winnings and punitive damage awards, and income from events for which performance has already occurred, such as alimony and pensions.

Finally, this Article does not address the significant macroeconomic aspects of requiring certain citizens to buy long-term bonds from the government. For example, economists could disagree on the differential effects that taxes versus borrowing have on inflation, a topic also involved in the Keynes' compulsory savings proposal discussed earlier. While the compulsory bond proposal involves inflation-protected bonds, the government should also be concerned about the effects of inflation on citizens who are *not* the bond holders.¹¹² Also, money that is borrowed by the government is money that is not available for investing in industry. For example, a compulsory bond purchaser may "feel free to reduce savings in other forms."¹¹³ Because we view our proposal as a compromise between the government's need to raise

111. Some may argue that there are aspects of personal services income that are also a fortune of luck, such as Alex Rodriguez being gifted with an ability to hit a 95 mph baseball, or the case of a CEO in the right place at the right time, especially if rewarded with stock-based compensation. See, e.g., MARIANNE BERTRAND & SENDHIL MULLAINATHAN, *Are CEOs Rewarded for Luck? The Ones without Principals are*, 116(3) Q. J. ECON. 901 (2001); Robert Daines et al., *The Good, the Bad and the Lucky: CEO Pay and Skill* (Working Paper), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1291573.

112. For example, nearly half of 266 economists surveyed in August 2009 expect inflation in the next few years. Sara Murray, *Economists are Split on Inflation*, WALL ST. J., Aug. 31, 2009, at A4. See also Clive Crook, *It is Never Too Early to Fear Inflation*, FINANCIAL TIMES, Sept. 14, 2009, at 9; Copeland, *supra* note 12 (describing China's desire for more TIPS bonds because of their concern over possible inflation).

113. HART, *supra* note 100, at 122.

cash flow during the next several years and the likelihood that the public will not permit a dramatic enough income tax rate hike, we do not address these issues further in this Article.

VIII. CONCLUSION

As a means of funding forecasted expenditures as well as reducing the current national debt, the U.S. government should establish a compulsory bond purchase program if it is unable to accomplish increases in the marginal income taxes rates. Through this program, rather than incurring an added tax expense, high service income taxpayers would receive government bonds for payments incurred past the standard 39.6% marginal rate. These bonds will provide personal savings for the taxpayer as well as a method to invest in the country by delivering the much needed cash flow to the U.S. government. It also would provide a signal that these affluent and in many cases high-profile Americans share the risk that foreign creditors have in America's ability to repay.

