

Taxes, Power, and Personal Autonomy

ALICE G. ABREU*

Any distributional pattern with any egalitarian component is overturnable by the voluntary actions of individual persons over time.¹

I. INTRODUCTION

Tax systems can give, even as they are taking away. What tax systems can give is power, and the power they can give is of different kinds. First, a tax system can give people² the power to avoid the

* Charles Klein Professor of Law and Government, Temple University School of Law. I am deeply indebted to my friend and colleague, Rick Greenstein, who not only inspired me to study jurisprudence but whose guidance continues to enrich my education. For the countless lunches spent discussing the tax system and the hours spent discussing the thoughts that eventually made it into this piece, I thank him. I am also grateful for the care and thoughtfulness with which Jane Baron, Rob Bartow, and Donna Byrne read prior drafts. Participants in the Temple Law School Faculty Colloquium provided much guidance on an early draft, and Amy LaBelle, Ken Martin and Brent Saunders, Temple '96, provided dedicated research assistance. Financial support was provided by Temple University School of Law, but all errors are mine.

1. ROBERT NOZICK, ANARCHY, STATE, AND UTOPIA 164 (1974). I want to thank Professor Steve Rieber for bringing this statement to my attention. Steve Rieber, *Freedom and Redistributive Taxation*, 10 PUB. AFF. Q. 63 (1996).

2. As even economists have long acknowledged, all taxes are ultimately paid by people. See STAFF OF JOINT COMM. ON TAX., 103D CONG., 1ST SESS., METHODOLOGY AND ISSUES IN MEASURING CHANGES IN THE DISTRIBUTION OF TAX BURDENS, JCS-7-93, 20 (1993) [hereinafter JCT PAMPHLET]. Thus, even taxes nominally imposed on entities or other jural persons are actually paid by people, although the identity of those people might be difficult to ascertain. The development and application of the microeconomic discipline of distributional analysis, which is devoted to determining how the tax burden is actually distributed among income classes, is discussed in more detail in Part IV.

imposition of all or part of the tax.³ A system that grants such power does so by attaching different consequences to different behavioral choices. The federal income tax offers many such choices—a head tax would offer almost none.

Second, a tax system can give people the power to shift the economic burden of the tax to someone else.⁴ A tax system so designed gives the bearer of the nominal burden the choice of either shifting or retaining the economic burden of the tax.⁵ A system that taxes corporate entities gives the entity the choice of shifting the burden of the tax to any one

3. Under a system that grants such power, choosing one type of behavior would result in the payment of X amount in tax, while choosing another type of behavior would result in the payment of X plus (or minus) Y amount in tax. A system that requires realization illustrates the importance of the ability to choose. Under such a system, a taxpayer who owns a share of stock purchased for \$1 but now worth \$101 will have no income as a result of that appreciation (unless the taxpayer is a dealer in securities and the mark to market rules of I.R.C. § 475 apply) if she chooses to retain the share. She will owe no federal income tax with respect to her ownership of the share and X will therefore equal 0. By contrast, if the taxpayer chooses to sell the share for \$101, she will have income of \$100 and will have to pay tax on that income. Her federal income tax liability will therefore be $X + Y$, where Y is the amount of tax attributable to the sale of the share. Of course, realization is not an inevitable component of any tax system, even an income tax system. See Henry Ordover, *Revisiting Realization, Accretion Taxation, The Constitution, Macomber, and Mark to Market*, 13 VA. TAX REV. 1 (1993); David J. Shakow, *Taxation Without Realization: A Proposal for Accrual Taxation*, 134 U. PA. L. REV. 1111 (1986); Victor Thuronyi, *The Taxation of Corporate Income—A Proposal for Reform*, 2 AM. J. OF TAX POL'Y 109 (1983); Mark L. Louie, Note, *Realizing Appreciation Without Sale: Accrual Taxation of Capital Gains on Marketable Securities*, 34 STAN. L. REV. 857 (1982); Fred B. Brown, "Complete" Accrual Taxation, 33 SAN DIEGO L. REV. (forthcoming December 1996); cf. Dan Subotnik, *On Constructively Realizing Constructive Realization: Building the Case for Death and Taxes*, 38 KAN. L. REV. 1 (1989); Lawrence Zelenak, *Taxing Gains at Death*, 46 VAND. L. REV. 361 (1993); Charles O. Galvin, *Taxing Gains at Death: A Further Comment*, 46 VAND. L. REV. 1525 (1993). See generally Jeff Strnad, *Periodicity and Accretion Taxation: Norms and Implementation*, 99 YALE L.J. 1817 (1990).

4. See *infra* part IV. In particular, see text accompanying notes 23, 50-54, for an explanation and discussion of the differences between the nominal and economic burdens of a tax.

5. Traditional economic analysis proceeds as if the burden is shifted because it must be shifted, that is, as if behaving so as to maximize immediate economic gain is a law as inexorable as the law of gravity. I disagree. The decision to maximize immediate economic gain proceeds from the existence of a choice to do so, as I develop more fully in part IV.C.

of a number of potential bearers.⁶ A system of taxing shareholders on corporate income as accrued would curtail that choice.⁷

6. Even though the corporate income tax has been a part of the federal income tax system for nearly a century (a federal tax was imposed on the income of corporations in 1909), economists still do not know who actually pays it. They agree that corporations are merely the creatures of state law, and, as such, cannot actually bear the burden of the tax. Some individual must actually suffer its imposition, but economists cannot agree on who those individuals are. Thus, it is possible that the tax is shifted to the providers of labor, in the form of lower wages, to the providers of capital, in the form of smaller returns, to consumers, in the form of higher prices, to suppliers, in the form of lower prices paid for materials, or to some combination of all of these. For analysis of the problem of determining the incidence of the corporate income tax, including a discussion of the difficulty of defining the concept of incidence itself, see William A. Klein, *The Incidence of the Corporation Income Tax: A Lawyer's View of a Problem in Economics*, 1965 WIS. L. REV. 576, 602 nn.104-07 (1965). See generally JCT PAMPHLET, *supra* note 2; MARIAN KRZYZANIAK & RICHARD A. MUSGRAVE, *THE SHIFTING OF THE CORPORATION INCOME TAX* (1963); JOSEPH A. PECHMAN, *FEDERAL TAX POLICY* 141-46 (5th ed. 1987); J. Gregory Ballentine, *The Incidence of a Corporation Income Tax in a Growing Economy*, 86 J. POL. ECON. 863 (1978); John G. Cragg et al., *Empirical Evidence on the Incidence of the Corporation Income Tax*, 75 J. POL. ECON. 811 (1967); Jane G. Gravelle & Laurence J. Kotlikoff, *The Incidence and Efficiency Costs of Corporate Taxation When Corporate and Noncorporate Firms Produce the Same Good*, 97 J. POL. ECON. 749 (1989); Arnold C. Harberger, *The Incidence of the Corporation Income Tax*, 70 J. POL. ECON. 215 (1962); Laurence J. Kotlikoff & Lawrence H. Summers, *Tax Incidence*, in 2 HANDBOOK OF PUBLIC ECONOMICS 1043, 1050-65 (Alan J. Auerbach & Martin Feldstein eds., 1987); George Mundstock, *Taxation of Intercorporate Dividends Under an Unintegrated Regime*, 44 TAX L. REV. 1, 18-39 (1989). For a cognitively-based explanation of the persistence of the corporate income tax notwithstanding the inability to ascertain the identity of its bearers, see Edward J. McCaffery, *Cognitive Theory and Tax*, 41 UCLA L. REV. 1861, 1883-86 (1994).

7. Such a system is just one of a number of proposed designs for integrating the corporate and individual income taxes, and much scholarly attention has been paid to these designs. See, e.g., William D. Andrews, *Proposals of the American Law Institute on Corporate Acquisitions and Dispositions and Reporter's Study on Corporate Distributions*, A.L.I. FED. INCOME TAX PROJECT, SUBCHAPTER C (1982); *Reporter's Study Draft: Subchapter C (Supplemental Study)*, in A.L.I. FED. INCOME TAX PROJECT (1989); Alvin C. Warren Jr., *Reporter's Study of Corporate Tax Integration*, A.L.I. FEDERAL INCOME TAX PROJECT (1993); Krister Andersson, *Implications of Integrating Corporate and Shareholder Taxes*, 50 TAX NOTES 1523 (1991); Ernest S. Christian, Jr., *Integrating Corporate and Shareholder Taxes*, 48 TAX NOTES 1519 (1990); Peter L. Faber, *Taxation of Corporations and Shareholders: Premises of the Present System*, 22 SAN DIEGO L. REV. 5 (1985); John K. McNulty, *Reform of the Individual Income Tax by Integration of the Corporate Income Tax*, 46 TAX NOTES 1445 (1990); Scott A. Taylor, *Corporate Integration in the Federal Income Tax: Lessons from the Past and a Proposal for the Future*, 10 VA. TAX REV. 237 (1990); George K. Yin, *Achieving Corporate Integration Through Double Taxation*, 56 TAX NOTES 1365 (1992); George K. Yin, *A Different Approach to the Taxation of Corporate Distributions: Theory and Implementation of a Uniform Corporate-Level Distributions Tax*, 78 GEO. L.J. 1837 (1990); cf. Jeffrey L.

That tax systems attach consequences to the exercise of taxpayer choice is not news. Legislatures have long recognized that taxpayers can choose between various courses of action and have often used the existence of choice as an instrument of social or economic policy.⁸ Courts and commentators have struggled with what can accurately be characterized as the abuse of choice—taxpayer attempts to cast transactions in a particular form devoid of business purpose or substance—and have filled many pages trying to develop talismanic formulae for distinguishing acceptable use from unacceptable abuse.⁹

Kwall, *The Uncertain Case Against the Double Taxation of Corporate Income*, 68 N.C. L. REV. 613 (1990) (questioning the prudence of corporate integration in light of equitable and revenue-based concerns); Rebecca S. Rudnick, *Who Should Pay the Corporate Tax in a Flat Tax World?*, 39 CASE W. RES. L. REV. 965 (1988-89) (proposing the redesign of the corporate income tax as a viable alternative to corporate integration).

8. For a recent and thoughtful illustration of this concept, see Michael Livingston, *Risky Business: Economics, Culture and the Taxation of High-Risk Activities*, 48 TAX L. REV. 163 (1993). For a good synopsis of the literature on the merits of and policies inherent in the use of the tax law to foster particular choices, see Edward A. Zelinsky, *Efficiency and Income Taxes: The Rehabilitation of Tax Incentives*, 64 TEX. L. REV. 973 (1986).

9. See, e.g., Walter J. Blum, *Motive, Intent and Purpose in Federal Income Taxation*, 34 U. CHI. L. REV. 485 (1966-67); Yitzhak Hadari, *Tax Avoidance in Linear Transactions: The Dilemma of Tax Systems*, 15 U. PA. J. INT'L BUS. L. 59 (1994); Joseph Isenbergh, *Musings on Form and Substance in Taxation*, 49 U. CHI. L. REV. 859, 864-82 (1982); Geoffrey J. Lanning, *The Real-Politik of Taxation: Substance and Form, Tax "Lawmaking", and the Basic Tax Ideologies*, 34 WAYNE L. REV. 1485 (1988); Saul Levmore, *Recharacterizations and the Nature of Theory in Corporate Tax Law*, 136 U. PA. L. REV. 1019 (1988); Joshua D. Rosenberg, *Tax Avoidance and Income Measurement*, 87 MICH. L. REV. 365, 382-83 (1988); Lee A. Sheppard, *Substance over Form in Subchapter C*, 44 TAX NOTES 642 (1989).

Drawing the line between acceptable, and indeed, intended, use and unacceptable, unintended abuse has always been difficult. In general, I would consider abusive any attempt at reaping benefits that the Legislature did not intend to bestow. I would consider as acceptable any transaction that carried out the Legislature's intended purpose. For me, determining the Legislature's purpose is crucial and it does not surprise me that the debate about the role of purpose, and the manner in which purpose is ascertained, has garnered the attention of tax scholars. See Deborah A. Geier, *Interpreting Tax Legislation: The Role of Purpose*, 2 FLA. TAX REV. 492 (1995); Deborah A. Geier, *Commentary: Textualism and Tax Cases*, 66 TEMP. L. REV. 445, 448 n.8, 456 (1993); Edward A. Zelinsky, *Text, Purpose, Capacity, and Albertson's: A Response to Professor Geier*, 2 FLA. TAX REV. 717 (1996). For a comprehensive catalogue of tax scholarship on the role of purpose, see Geier, *Interpreting Tax Legislation: The Role of Purpose*, *supra*, at 494 n.5, and Geier, *Commentary: Textualism and Tax Cases*, *supra*, at 448 n.8, 456 n.42. See generally WILLIAM N. ESKRIDGE, JR., *DYNAMIC STATUTORY INTERPRETATION* (1995); Richard K. Greenstein, *Text as Tool: Why We Read the Law*, 52 WASH & LEE L. REV. 105 (1995).

An illustration of the way I distinguish between use and abuse might be helpful. I consider an individual's purchase of municipal bonds, the interest on which is exempt from federal income tax under I.R.C. § 103, to be an acceptable use of the tax system. Such an individual purchaser is doing precisely what the Legislature intended—loaning

Public finance economists have kept countless computers busy trying to track and predict the consequences of the exercise of choice, that is, determining the likely distribution of the tax burden.¹⁰ What legislatures and public finance economists have failed to do, and what commentators have done entirely too little of, is engage in a critical appraisal of the values implicated by the existence of varying amounts of choice.¹¹ An analysis of the ways in which tax systems confer and distribute power is long overdue.¹²

money to an entity under circumstances which allow that entity to pay less than a market rate for the money. By contrast, I think that Evelyn Gregory engaged in unacceptable abuse when she caused her wholly owned corporation to transfer Monitor shares to Averill and then caused the liquidation of Averill. *Gregory v. Helvering*, 27 B.T.A. 223 (1932), *rev'd*, 69 F.2d 809 (2d Cir. 1934), *aff'd*, 293 U.S. 465 (1935). Mrs. Gregory's actions were abusive because the benefits of what is now I.R.C. § 355 were not intended to apply to a transaction without a business purpose.

10. See, e.g., *DO TAXES MATTER?* (Joel Slemrod ed., 1990); JOSEPH A. PECHMAN, *TAX REFORM, THE RICH AND THE POOR* (2d ed. 1989); *HOW TAXES AFFECT ECONOMIC BEHAVIOR* (Henry J. Aaron & Joseph A. Pechman eds., 1981); *THE ECONOMICS OF TAXATION 3-84* (Henry J. Aaron & Michael J. Boskin eds., 1980); HORST C. RECKTENWALD, *TAX INCIDENCE AND INCOME REDISTRIBUTION* (Stolper trans., 1971).

11. Notable exceptions are Sheldon D. Pollack, whose May 18, 1995 testimony before the Senate Finance Committee, as well as his prior published work, notes the relationship between values and tax system design, (Sheldon D. Pollack, *The Flat Tax: A Dissenting View*, reprinted in 67 *TAX NOTES* 1253 (1995); Sheldon D. Pollack, *Tax Reform: The 1980's in Perspective*, 46 *TAX L. REV.* 489 (1991)), Donna M. Byrne, who has used philosophical notions of fairness to appraise progressive taxation (Donna M. Byrne, *Progressive Taxation Revisited*, 37 *ARIZ. L. REV.* 739 (1995)), and Marjorie Kornhauser, who has analyzed progressivity from a feminist perspective, (Marjorie Kornhauser, *The Rhetoric of the Anti-Progressive Income Tax Movement: A Typical Male Reaction*, 86 *MICH. L. REV.* 465 (1987)). As Professor Pollack has pithily observed, "intellectual honesty requires that assertions such as that the income tax ought to be either flat or progressive need to be justified in terms of moral and ethical principles." Pollack, *The Flat Tax*, *supra*, at 1254. More recently, Gene Steuerle noted the importance of choice by defining "losers" as individuals "whose options might be further restricted" under proposed revisions to the Code. Gene Steuerle, *The Multiple Goals of Tax Reformers*, 69 *TAX NOTES* 231 (1995).

12. Although non-corporeal entities are also subject to taxes, I refer to the empowerment of individuals because, in the end, only people pay taxes. See *supra* note 2. Only people can make the decisions that will result in the payment of various amounts of taxes and shift, and ultimately bear, the economic burden of those taxes. For an examination of the latter contention (viewed from a distributional standpoint), see Martin Feldstein, *Imputing Corporate Tax Liabilities to Individual Taxpayers*, 41 *NAT'L TAX J.* 37 (1988); cf. Victor Thuronyi, *The Concept of Income*, 46 *TAX L. REV.* 45, 77-79 (1990) (arguing that, in any analysis of distributional fairness, non-corporeal entities cannot have "income" in the Haig/Simons sense). It is therefore appropriate to focus on individuals as the object of empowerment, rather than on the organizations and non-corporeal entities they might control and through which they might operate.

The key to this analysis is appreciating that tax systems, like the coins in which they are ultimately paid, have two sides. On one side is the burden they impose. That side is easy to see and is shared by all tax systems.¹³ The optimal distribution of the tax burden has long been debated and its actual and projected distribution frequently analyzed.¹⁴ It is the other side of tax systems that is hard to see. On the other side is the empowerment that tax systems grant when they give individuals the ability to affect either the amount of tax that will be collected or the identity of the bearer of the resulting economic burden.¹⁵ Because not all tax systems empower and because I believe that the extent to which a tax system empowers reflects and implements important values, it is appropriate to engage in an analysis of the ways in which particular tax systems empower and to examine who is empowered.

The way in which a tax system empowers is, I submit, perhaps even more important than the way in which it burdens. There are three reasons for this. First, empowerment can affect progressivity, generally by reducing it. Traditionally, the negative aspects of a tax system—its distribution of burdens—have determined its progressivity.¹⁶ Yet, empowerment, which is generally positive, can offset the negative aspect

13. In *Freedom and Redistributive Taxation*, Steve Rieber draws on the work of Nozick, Gooding, Klymlicka, and Cohen to posit a provocative view of the way in which tax systems impose a burden. Rieber argues that taxes constrain “the freedom to perform the action that is taxed.” Rieber, *supra* note 1, at 63, 64. While I am persuaded by the argument that taxes constrain freedom, I disagree with the implication that all they do is constrain. This Article attempts to show that a tax system’s design can vary the degree of constraint by also including the opportunity to exercise choice. Thus, while the existence of a gift tax can constrain the freedom to make a gift, as Professor Rieber posits, the decision to raise revenue by enacting a gift tax, rather than, say, a wealth tax, gives individuals who might be subject to the tax a quantum of power to decide on the imposition of the tax that they would lack under a system that taxed wealth.

14. Distributional analysis is a mature discipline replete with tools for measuring the distribution of the tax burden and enriched by debate about the adequacy of those tools and the desirability of particular outcomes. See *infra* Part IV.A.

15. Of course, the notion that law can empower is not new. Indeed, it is at the root of H. L. A. Hart’s attack on Austin’s positivist view of law. H. L. A. HART, *THE CONCEPT OF LAW* 40-41 (1961). Hart considered law to be more than a set of commands that impose duties (the Austinian commands of the sovereign). Rather, he considered law to be a system that allows individuals to engage in acts (like contracting for behavior that will take place in the future) that they would not be able to do in its absence. In Hart’s view, the law of contract empowers by providing assurances of things to come. Those assurances free individuals to enter into transactions and expect results that would not exist in their absence. Thus, like the tax law, the law of contracts empowers, even as it constrains. *Id.*

16. See *infra* note 37 and accompanying text.

of the burden.¹⁷ Empowerment can therefore reduce the net burden imposed by a tax system, and, by doing so, reduce its overall progressivity.¹⁸ To analyze the distributive impact of a system in its entirety, tax policy should ask not only how much the system takes away and from whom (the burden side of the progressivity equation), but also how much it gives and to whom (the benefits side of a new progressivity equation). In other words, tax policy should move from a consideration of gross burdens to a consideration of net burdens.¹⁹ To do this, tax policy must analyze the ways in which tax systems empower and must identify who they empower. Whether the result is a different measure of progressivity or the addition of another concept separate from and additional to progressivity is a matter for further development.

Second, empowerment can affect the visibility, and consequently the accountability, of a tax system. When a system places its burden on someone who has the power to shift that burden, it effectively taxes people who will often not know that they are being taxed—or at least they will not know that they are being taxed until they take one or more courses in microeconomics. Taxation that is invisible is even worse than taxation without representation.²⁰ One cannot rebel against, much less

17. As I discuss more fully in Part II, although the grant of the power to choose is not necessarily positive, in the context of a system of taxation the grant of such power is largely positive.

18. Basic algebra confirms that a positive factor, when added to a negative factor, reduces the size of the negative factor and produces a net figure that is less negative than the original negative alone. To illustrate, $-4 + 2 = -2$. I would rather be at -2 than -4 , even if, ideally, I would prefer to be at or above 0. If the burden of the tax is the -4 and empowerment is the $+2$, basic algebra illustrates how empowerment can reduce the net burden. To obtain a complete picture of the distribution of the tax burden, the -2 's, the net, and not the -4 's, the gross, should be distributed. Yet, current tax policy distributes the -4 's and does not even acknowledge the existence of the $+2$'s. Perhaps this is because the positive factors cannot easily be measured in numbers. Nevertheless, the difficulty of assigning a number to the factor as an empirical matter should not detract from the desirability of taking the factor into account as a conceptual matter.

19. As I discuss more fully in Part II.A., the netting process that I propose and that I illustrated in note 18, *supra*, is not precise, at least not with traditional measurement techniques, because the burden can be measured in dollars while the benefit cannot.

20. Adam Smith listed that which I now call visibility as the second of four maxims that he thought should apply to taxes in general. ADAM SMITH, AN INQUIRY INTO THE NATURE AND CAUSES OF THE WEALTH OF NATIONS 362 (1952). Smith's second maxim began by stating that "[t]he tax which each individual is bound to pay ought to be certain, and not arbitrary. The time of payment, the manner of payment, the quantity to be paid, ought all to be clear and plain to the contributor, and to every other person." *Id.* Perhaps anticipating Doernberg and McChesney's work more than a

attempt to change or reform, that which one does not know is there. That economists may be able to ascertain where the burden eventually lands and then convey that knowledge to the appropriate elected officials, should be scant comfort to anyone who believes that, as a normative matter, people ought to know the magnitude of the contribution their government is asking them to make.²¹

Third, but perhaps most importantly, empowerment vests in private individuals the authority to decide how the burden of a tax shall be allocated. This can affect the distribution of burdens within a tax system. In a tax system where the nominal burden of paying the tax coincides with its economic burden, the government decides who pays and how much they pay. By contrast, in a tax system that permits the economic burden to be shifted, the nominal bearer decides who bears the economic burden as well as how much burden they bear.²² Under such a system, taxation proceeds, at least proximately, from the nominal bearer's exercise of her power to shift the economic burden of the tax. Such a system has great potential for treating similarly situated individuals differently, something that policy-makers ought seriously to consider. Good tax system design should eschew, not ensure, capricious taxation.

Because the grant of the power to choose can affect who is taxed and how much they are taxed, an analysis of the ways in which tax systems empower and a determination of who it is that they empower should

century later, Smith continued by noting that “[w]here it is otherwise, every person subject to the tax is put more or less in the power of the tax-gatherer, who can either aggravate the tax upon any obnoxious contributor, or extort, by the terror of such aggravation, some present or perquisite to himself.” *Id.*; see also Richard L. Doernberg & Fred S. McChesney, *On the Accelerating Rate and Decreasing Durability of Tax Reform*, 71 MINN. L. REV. 913 (1987).

In his pioneering article on the relationship between cognitive theory and the tax law, Professor Ed McCaffery discusses the visibility of taxes from another perspective and suggests that hidden taxes are effective precisely because they are hidden. McCaffery, *supra* note 6, at 1875-76.

21. Relying on the willingness of legislators to enact provisions consistent with a particular distributional policy is satisfactory only if one is willing to trust them to behave, unchecked, in ways that are consistent with one's own distributional policies. It is also highly paternalistic. See *infra* notes 72-73 and accompanying text; see also Michael J. Graetz, *Paint-by-Numbers Tax Lawmaking*, 95 COLUM. L. REV. 609 (1995); McCaffery, *supra* note 6, at 1935-36. Indeed, public knowledge of the tax burden may be an important part of maintaining the accountability of public officials. Ironically, that same knowledge argues against the adoption of “return free” systems and other simplification measures that would render the income tax significantly less visible than it is now.

22. As I discuss more fully in part IV.C., shifting the economic burden of taxation involves the exercise of choice. That economists can predict how numbers of individuals will exercise that choice and the degree to which they will exercise it does not abrogate the existence of the choice.

become a standard part of tax policy analysis. A review of the current federal tax system reveals that the system grants many choices, but that it generally grants those choices to people who possess material wealth. It seems to distribute choices progressively, just as it does burdens. Although empowerment cannot be measured in dollars, its grant to the wealthy reinforces certain values and has important political, social, and psychological effects. Those effects color the public perception of the tax system and affect relationships between individuals and perhaps even the way individuals view themselves.

Part II of this Article shows that traditional tax policy analysis has hitherto proceeded on the assumption that tax systems impose burdens and introduces two concepts that can lead to a more complete analysis of tax system design: avoidance power and burden power. Parts III and IV then explore these two concepts in more detail. Part V uses the two most significant tax systems in this country, the federal income tax system and the federal employment tax (social security) system, to bring both concepts together and to illustrate how an examination of the ways in which specific tax systems empower and an identification of who the systems empower, can permit an analysis of the values that inhere in tax system design. Part VI examines the relationship between empowerment and values, and Part VII concludes by suggesting that the analysis of choice developed here could be applied to the ongoing debate regarding alternatives to the federal income tax system and should become a standard part of tax policy analysis.

II. BURDENS AND POWERS

If pessimists are people who look at a half full glass and pronounce it half empty, then tax scholars are generally pessimists. Tax scholars generally view taxes as burdens, or instruments of removal. Thus, public finance economists study how taxes burden individuals, distinguishing between such things as the nominal and the economic burden of taxes,²³ and try to determine how the burden of various types of taxes is distributed among the population.²⁴ They also study how taxes burden the economy by causing people to change their behavior in ways

23. See *infra* Part IV.A. for an explanation and discussion of the concepts of nominal and economic burdens.

24. See *infra* Part IV.B. for a discussion of distributional analysis.

inconsistent with the operation of an efficient market, dubbing the resulting effects the excess burden of the tax.²⁵ Policy-makers use the results of such economic analyses to judge the desirability of various taxes.²⁶

25. Alan Auerbach has defined excess burden, or the deadweight loss from a tax system, as “that amount that is lost in excess of what the government collects.” 1 HANDBOOK OF PUBLIC FINANCE ECONOMICS, 67, 61-126 (Alan J. Auerbach & Martin Feldstein eds., 1985) [hereinafter HANDBOOK]. The excess burden of a tax accounts for the difference between the amount of revenue that would be raised if people did not alter their behavior and the amount of revenue actually raised after the new tax (or tax increase) is in effect, and exists even when the tax is, like a cigarette tax, intended to induce the behavioral change. The concept of excess burden explains why a particular tax, say, a tax on cigarettes, might raise less revenue than could be predicted by taking the amount of the tax proposed for each pack, say, 5 cents, and simply multiplying it by the number of packs sold in the year preceding the enactment of the tax, say, 100 units. Economists assert that the number derived from that simple calculation—in this case, 5 dollars—will almost certainly be greater than the amount of tax actually raised because fewer packs will be sold following the enactment of the tax. See Bruce Bartlett, *Cigarette Taxes, Smuggling, and Revenues*, 63 TAX NOTES 1493 (1994). Some people will buy fewer, or even no packs of cigarettes to avoid the payment of the tax, while others might choose to buy cigarettes on the black market. *Id.* at 1496. Both of these behavioral responses will cause the government to lose not only the tax revenue it could have collected from the unsold packs, but any additional tax revenue it would have collected on account of the profit the sellers of the cigarettes would have made by selling those unsold packs. That the tax burdens the economy is evident. *Id.* at 1498.

The excess burden of a tax is not just the cost of the tax payment remitted to the government. As Daniel Shaviro has pointed out, “[a]ny economist worth his salt can tolerantly shrug his shoulders about high tax payments, pointing out that such payments are merely transfers from one person’s individual bank account to society’s collective bank account, rather than overall losses that diminish society’s monetary wealth.” Daniel N. Shaviro, *State and Local Taxation: The Current Judicial Outlook*, 22 CAP. U. L. REV. 279 (1993). Steve Rieber makes a similar point about the freedom that one person loses when a particular activity is taxed. Rieber, *supra* note 1. Rather, the excess burden is the distortional effect of the tax—that is, the extent to which the existence of the tax causes people to engage in behavior that they would not otherwise engage in. See JCT PAMPHLET, *supra* note 2, at 26-29. For an explanation of the development of the concept of excess burden, see 1 HANDBOOK, *supra*, at 61-126.

26. A debate over the extent to which revenue estimates should be “dynamic,” that is, take into account likely behavioral effects, rather than “static,” that is, fail to take into account such effects, has raged in recent years. Some parties to the debate have argued that revenue estimates are static and thus irrelevant, others have argued that even if dynamic, revenue estimates are not dynamic enough because they hold certain macroeconomic variables constant, and still others have maintained that any attempt at dynamism is tantamount to alchemy. For a representative and recent sampling of the literature on this debate, see Graetz, *supra* note 21, at 668-77; Kenneth J. Kies, *The Revenue Estimating Process—Letting in the Light and Letting Out the Hot Air*, 69 TAX NOTES 373 (1995); *Economists Continue to Square Off Over “Dynamic” Scoring*, 69 TAX NOTES 275 (1995); Testimony given at HEARINGS held on January 11, 1995, available in LEXIS, 95 TNT 7-10, 7-16, 7-32, 7-33, 7-34, 7-35, 7-36, 7-40, 7-41, 7-42, 7-43, 7-44; *Economists Discourage GOP From Adopting ‘Dynamic’ Scoring*, 66 TAX NOTES 303 (1995).

Not surprisingly, traditional tax policy analysis has also proceeded from the notion that taxes are burdens. Students of tax policy have endeavored to ascertain the extent to which a tax system achieves the goals of equity, efficiency, and simplicity.²⁷ Implicit in each of these goals is a view of tax systems as the purveyors of burdens.

Equity has two dimensions: horizontal and vertical.²⁸ Horizontal equity follows from the view that those with equal ability to pay should bear equal tax burdens. Vertical equity follows from the view that the tax burden should rise as ability to pay rises.²⁹ Both concepts address the distribution of burdens, not blessings.

The desire for efficiency also proceeds from a view of taxes as burdens. A tax is judged to be more or less efficient depending on the degree to which it interferes with the allocation of resources in the

27. While a complete listing would probably include ability to raise revenue, ease of administration and other factors, scholars most often cite the goals of equity, efficiency, and simplicity, perhaps as a proxy for a more complete analysis. See MICHAEL J. GRAETZ & DEBORAH H. SCHENK, *FEDERAL INCOME TAXATION—PRINCIPLES AND POLICIES* 30-35 (3d ed. 1995). For the more complete listing, see Joseph Sneed, *The Criteria of Federal Income Tax Policy*, 17 STAN. L. REV. 567, 568 (1965).

28. The use of ability to pay as a criterion for tax system design harkens back at least to Adam Smith, who urged that “[t]he subjects of every state ought to contribute towards the support of the government, as nearly as possible, in proportion to their respective abilities; that is, in proportion to the revenue which they respectively enjoy under the protection of the state.” SMITH, *supra* note 20, at 361. While the notion of ability to pay is most frequently cited in support of a system of progressive taxation, it is equally (and perhaps even more accurately) cited in support of a system of proportional (or flat) taxation. For a critique of the use of ability to pay as a standard for taxation, see JOHN F. WITTE, *THE POLITICS AND DEVELOPMENT OF THE FEDERAL INCOME TAX* 50 (1985) and Jeffrey A. Schoenblum, *Tax Fairness or Unfairness? A Consideration of the Philosophical Bases for Unequal Taxation of Individuals*, 12 AM. J. TAX POL’Y 221 (1995). Nevertheless, as Professor Graetz has noted, “[t]he ability-to-pay criterion enjoys broad acceptance as a fundamental tenet of tax justice, although the details of its implementation are controversial.” Michael J. Graetz, *The Troubled Marriage of Retirement Security and Tax Policies*, 135 U. PA. L. REV. 851, 861 (1987).

29. During the past decade, a rich debate has erupted on the question whether the concept of horizontal equity is really different from the concept of vertical equity. Louis Kaplow, *Horizontal Equity: Measures in Search of a Principle*, 42 NAT’L TAX J. 139 (1989); Richard A. Musgrave, *Horizontal Equity, Once More*, 43 NAT’L TAX J. 113 (1990); Louis Kaplow, *A Note on Horizontal Equity*, 1 FLA. TAX REV. 191 (1992); Richard A. Musgrave, *Horizontal Equity: A Further Note* 1 FLA. TAX REV. 354 (1993); Paul A. McDaniel & James R. Repetti, *Horizontal and Vertical Equity: The Musgrave/Kaplow Exchange*, 1 FLA. TAX REV. 605 (1993). Regardless of who is finally regarded as the winner of this debate (if anyone ever is), it is still the case that, traditionally, horizontal and vertical equity have been regarded as *desiderata* in tax policy.

economy. The less a tax interferes, the more efficient, and thus the more desirable, it is.³⁰ Only a view that something is burdensome accounts for the conclusion that less of it is better.

The desire for simplicity also stems from the notion of taxes as burdens. Complex systems are less desirable than simple systems because they are more burdensome. They take more time to learn and are more costly to administer than simple systems. Complex systems are also more burdensome for another, rarely acknowledged, reason: they offer more opportunity for the exercise of choice. Although having choice is often good, it is not free. As I discuss more fully in Part VI.A., the existence of choice carries with it the need to acquire knowledge about the available choices and the assumption of responsibility for its ultimate exercise.

Tax systems can provide the opportunity to exercise two qualitatively different kinds of choices. First, a tax system can give taxpayers the ability to make choices that will affect the amount of taxes they will pay.³¹ Because taxpayers who can exercise that type of choice have the power to avoid liability for all or part of a tax by changing their behavior, I will refer to the power to choose such a course of conduct as *avoidance power*. People with avoidance power benefit even if they choose not to exercise that power. The power to choose is important in and of itself.

Second, a tax system can place the nominal burden of the tax on parties with the power to shift the economic burden elsewhere. People with such power must, of course, choose whether to exercise it. Their choice determines who ultimately bears the economic burden of the tax. I will refer to the power to shift the economic burden of the tax as *burden power*.

These two powers do not exist in independent spheres. Because an individual can exercise burden power so as to avoid the economic burden of the tax, burden power could be seen as but one application of avoidance power. Nevertheless, the powers are qualitatively different and therefore benefit from separate analysis.

30. The theory of optimal taxation seeks to establish the point at which government can raise the maximum amount of revenue while creating the minimum excess burden. 1 HANDBOOK, *supra* note 25, at 86. The easiest way to solve the problem of optimal taxation is to enact taxes that do not distort behavior. Auerbach posits a tax on pure profits as such a tax and suggests that, at least theoretically, one could design a non-distortionary progressive tax on genetic characteristics associated with ability. He recognizes, however, the practical impossibility of actually enacting such a tax. *Id.*

31. This includes the power to reduce that level to zero, that is, to avoid imposition of the tax altogether.

The power to shift the burden of the tax differs qualitatively from the power to avoid it for two reasons. First, a person who avoids the imposition of the tax by exercising avoidance power avoids both the nominal and economic burdens of the tax. By contrast, a person who can only avoid the economic burden of the tax by shifting it retains the nominal burden. Such a person retains the compliance obligations as well as the primary liability for payment of the tax, and must endure any economic consequences that attend the shift. Second, bestowing on certain individuals the power to shift has policy implications that are different from, and perhaps more disturbing than, the policy implications of bestowing only the power to avoid. While an exercise of avoidance power will simply result in the collection of fewer taxes, leaving government to decide how else to raise revenue, exercising burden power allows the nominal taxpayer to decide who will pay the amount that she is unwilling to provide.³² Burden power thus differs from avoidance power because burden power privatizes the decision of who will pay and hides the very existence of the tax. I will discuss these issues further in Part IV.

III. AVOIDANCE POWER: CHOICE WITH RESPECT TO THE MAGNITUDE OF THE TAX BURDEN

A. The Value of Personal Autonomy

Whether a tax system gives those who are subject to it any avoidance power depends on its design. For instance, a head tax provides little avoidance power, but a tax on champagne gives individuals the power to avoid the tax by refraining from purchasing champagne, or by purchasing bootleg champagne. The champagne tax is high in avoidance power because individuals could avoid it completely by changing their

32. To the extent that the government imposes taxes to raise revenue, it is possible to argue that any avoidance has the effect of an indirect shift. As long as the government needs to raise X amount of revenue, if person A pays $X-Y$, it is reasonable to posit that the government will have to raise Y from another source. The difference between this type of burden shifting and the type of burden shifting I will discuss in Parts III and IV involves the question of who decides. If the government decides to raise Y from source Z , that decision will be made by the government. If, instead, person A exercises her power to shift so that person B ends up bearing the economic burden of the tax rather than person A , it is person A who decides that B should pay, not the government, at least not directly.

behavior at an acceptable cost—the cost of not consuming legal champagne. A head tax is low in avoidance power because taxpayers cannot avoid it without incurring unacceptably high costs—the loss of life, or expatriation and the loss of citizenship and community.³³

The design of a tax system, including the extent to which it confers avoidance power, reflects the values of its designers. Tax systems, after all, do not follow the laws of nature. The design of a tax system is not ordained by anything even remotely analogous to the law of gravity.³⁴

33. Avoidance that results from a change in behavior that changes the status of an individual from one subject to the tax to one not subject to the tax is not only conceptually permissible but is actually intended by the design of the system. A system that taxes the purchase of champagne allows individuals to avoid the imposition of the tax by assuming the status of non-purchasers rather than of purchasers. Few would seriously contend that a person who refrains from becoming a purchaser of champagne solely to avoid the tax thereon should nevertheless be subject to the tax because her motivation was avoidance of the tax and not a distaste for champagne. The power to choose behaviors (buying champagne and paying the tax or not buying champagne and not paying the tax) is part of the fabric of the system, and it would be wrong to punish a taxpayer for exercising a choice that the system gives her. The failure to recognize that tax systems can empower by their design leads to confusion regarding the legitimacy of choices exercised by taxpayers. The effects of this confusion are nowhere more evident than in the recent proposals to tax United States citizens who renounce their citizenship to avoid the payment of federal taxes. The Senate introduced an expatriation proposal (a revised version of an earlier proposal by the Clinton administration) as an amendment to the Self-Employed Persons Health Care Deduction Extension Act of 1995, H.R. 831, 104th Cong., 1st Sess. (1995). Although the amendment was ultimately defeated, the Senate did include in the final version of H.R. 831 an amendment requiring the Joint Committee to study the expatriate tax issue further. Pub. L. No. 104-7, § 6, 109 Stat. 93 (1995). The Senate amendments to H.R. 831 (both the defeated tax proposal and the enacted “study” proposal and the many variations that have been proposed since then) reflect the widespread view that expatriates ought to be taxed in a way that neither United States citizens nor non-resident aliens are taxed; that they are doing something that the system did not intend for them to be able to do. That something is to choose whether to be subject to the tax laws of the United States. Yet, our system provides that choice. Although some people do not have a choice regarding the acquisition of United States citizenship because they are born here, all of us have a choice regarding its retention. The possession of United States citizenship is not meaningless. Citizenship carries with it a number of benefits, as well as a number of burdens. Those who are willing to give up the benefits should be permitted to shed the burdens as well. Recognizing the degree to which tax systems, by design, provide for the exercise of choice would allow us to distinguish between the appropriate and expected exercise of choice and its abuse. For an illustration of how the analysis developed here can be used to illuminate the issues regarding the taxation of expatriation, see Alice G. Abreu, *The Difference Between Expatriates and Mrs. Gregory: Citizenship Can Matter*, 67 TAX NOTES 692 (1995), reprinted in 10 TAX NOTES INT’L 1612 (1995), and Alice G. Abreu, *Taxing Exits*, 30 U.C. DAVIS L. REV. 1087 (1996) (also summarizing the fate of the numerous proposals to change the taxation of expatriates).

34. In a recent article, Professor John Miller draws upon the work of John Rawls to argue that tax laws, like the rules of baseball, are creational because their enactment “creates something that did not exist before.” John A. Miller, *Indeterminacy, Complexity, and Fairness: Justifying Rule Simplification in the Law of Taxation*, 68

WASH. L. REV. 1, 69 n.319 (1993) (citing John Rawls, *Two Concepts of Rules*, 64 PHIL. REV. 3, 24-29 (1955)). Professor Miller, drawing on the Rawlsian notion that rules lead to the formation of practices and thus define the practice, goes further and posits that tax laws are even more "creational" (or constitutive) than other types of laws. Whereas other types of laws address some event or condition that would exist even in their absence, or codify an existing or accepted moral imperative, in Professor Miller's view, tax laws do neither of those things. *Id.*

I disagree with Professor Miller. I would certainly acknowledge that the connection between particular tax laws and actions that occur in society irrespective of those laws is harder to see than the connection between murder and the laws that proscribe it. The connection between tax laws and morality is also not immediately apparent. I do, however, believe that the same sort of connection exists. The creation of a tax system is an imperative of group (*i.e.*, societal) living. Although tax systems as we now know them did not exist in aboriginal societies, systems of communal sharing did. Members of numerically small societies share food, protection from the elements, and defense against predators. The existence of an organized society implies, by its very definition, the existence of different roles for different members of it, and the existence of different roles necessitates sharing. A society in which members are expected to share the proceeds of a hunt with others is, in effect, imposing a tax upon that hunt. It is not outlandish to suspect that in such a society, failure to conform to the norm of sharing would be seen as a moral failing and would be punished with ostracism or worse. It is also not outlandish to suggest that members of such a society might prefer to keep the entire proceeds of the hunt for themselves rather than sharing it with the rest of the community. Although the consequences of failing to share would be more direct in such societies (*e.g.*, in the form of ostracism or inability to receive other necessities) than in societies that have adopted formal systems of taxation which require payment in a fungible currency, this does not make the imperative to share any less compelling nor the failure to do so any less moral. *See, e.g.*, RICHARD B. LEE, *THE DOBE !KUNG*, 48-50, 97-102 (1984); NAPOLEON A. CHAGNON, *YANOMAMO—THE FIERCE PEOPLE* 7, 34, 91 (George & Louise Spindler eds., 1968); John A. Price, *Sharing, The Integration of Intimate Economies*, 17 ANTHROPOLOGICA 3, 14, 16 (1975) (I thank my colleague, Peter Severeid for bringing some of these sources to my attention). In the most basic of senses, then, I heartily agree with Justice Holmes that taxes are the price we pay for civilization. *See infra* note 41. Indeed, I might go even further and say that taxation, that is, the means by which we share resources, is an essential part of civilization.

While the existence of a system of taxation is, in my view, an imperative of organized societal living, the particular contours of that system reflect the values of those who design it. Thus, who will be asked to share and the extent to which they will be asked to share depends on what the particular society values. The rules of a tax system, then, are unlike the rules of baseball in two ways. First, the behavior in question would exist even in the absence of the rules. That is, in an organized society, people would share resources. The game called *sharing* would exist even in the absence of definitive rules setting forth its parameters. *See LEE, supra*, at 48-50. Second, the content of the rules reflects shared values. In that sense, the rules of the game of sharing, or of paying taxes, do not constitute the behavior. Rather, they describe the values and aspirations the society holds. In Rawlsian terms, then, tax laws are not constitutive, they are descriptive. John Rawls, *Two Concepts of Rules*, 64 PHIL. REV. 3, 24-29 (1955).

In *The Transparency of Rules*, my colleague, Rick Greenstein, argues that the distinction between constitutive and descriptive rules is a false one. Richard K. Greenstein, *The Transparency of Rules* (presented at the Annual Meeting of the

Unlike the falling of a pebble released from a hand, a particular tax system is not the inevitable result of forces which humans can understand, perhaps control and sometimes escape from, but cannot alter. Rather, tax systems are products of human creation. They exist because they serve human objectives, reflecting the values of their designers. A tax system's design can reveal much about those values. In other words, our choice of an income tax over a head tax as a mechanism for raising revenue is not accidental.

Values dictate the answer to one of the fundamental questions that any tax system must answer: Who decides how much each member of the society will pay? While one answer to that question simply points to Congress—by enacting the system, *it* decides—such an answer fails to recognize the ways in which taxpayers themselves might be the decision-makers. To the extent that taxpayers can alter their tax liability by changing their behavior, it is they who decide. Under a system that provides opportunities for the exercise of taxpayer choice, even taxpayers who choose not to alter their behavior are making a choice that affects their tax liability. That is the thesis of this Article: The design of a tax system determines who makes the ultimate decision about who pays and how much they pay.

The decision to adopt a tax system that provides opportunities for taxpayers to exercise choice, and thus allows them to determine their own tax liability, reflects deference to the value of personal autonomy. Adoption of the federal income tax system, which confers much avoidance power, rather than a head tax system, which would confer almost none, reflects the importance of personal autonomy in our socio-political tradition.³⁵

The way in which a tax system distributes the ability to preserve personal autonomy implicates deeply held values. A tax system can distribute such powers, and whatever burdens they may impose, either progressively, regressively, or proportionately. A tax system that evidences equal respect for the personal autonomy of all who are subject to it would give all who are subject to it the same amount of power. Such a system would reflect the value that personal autonomy ought to

American Philosophical Association, Pacific Division, April 6, 1996; unpublished manuscript on file with the author). The difference, he maintains, is one of degree and not of kind, so that, in his view, even the rules of baseball are both descriptive and constitutive. In his terms, perhaps all I am saying here is that tax laws are more transparent than the rules of baseball.

35. Personal autonomy is at the root of values that we have elevated to the status of rights, such as privacy. See Hyman Gross, *Privacy and Autonomy*, in *PRIVACY* 169 (John Chapman & J. Roland Pennock eds., 1971), reprinted in *PHILOSOPHY OF LAW* 340 (Joel Feinberg & Hyman Gross eds., 4th ed. 1991).

be distributed equally. By contrast, a system that bestowed the greatest amount of personal autonomy on those with the greatest amount of material wealth would reflect the high value of such wealth. And, a system that bestowed the greatest amount of power on those with the smallest amount of material wealth would reflect either a disdain for such wealth or an attempt to compensate for diminished wealth. Once a system is identified as the giver of power, analysis of the distribution of that power becomes as imperative as the analysis of the distribution of its burdens.

B. Power and Progressivity

The distribution of both benefits and burdens affects the progressivity of a tax system. Any analysis of one without the other is bound to be incomplete. Traditional tax policy analysis has suffered from such incompleteness. While traditional tax policy analyzes the distribution of the financial burdens of taxation,³⁶ it has failed to analyze the distribution of the powers that a system of taxation can bestow.³⁷ Traditional

36. As Donna Byrne has pointed out to me, traditional tax policy analysis is incomplete even within the parameters that it sets out to examine because it focuses on fiscal burdens. As Professor Byrne maintains, tax systems can impose non-fiscal burdens that the traditional analysis simply ignores. See Byrne, *supra* note 11.

37. That taxes have traditionally been viewed as creating only burdens is not surprising given the perspective of those who have been at the forefront of tax policy analysis (*i.e.*, economists who are trained to consider the effects of a tax on the economy). From that traditional viewpoint, taxes that induce a change in taxpayer behavior reduce market activity and thus burden the economy. All taxes, from this perspective, are non-neutral. Nevertheless, to say that all taxes are non-neutral is not to say that taxation cannot be used to stimulate economic activity. However, the use of taxation to stimulate economic activity typically involves reducing taxes for one type of activity over another, which has the effect of creating a preferred class of activity. The use of taxation to induce economic activity presupposes the existence of a uniform tax. Once the tax is in place, any reduction in it creates a preference. Such a reduction in tax is equivalent to an outlay of funds for the activity and is often referred to as a tax expenditure. See Stanley S. Surrey, *Tax Incentives as a Device for Implementing Government Policy: A Comparison with Direct Government Expenditures*, 83 HARV. L. REV. 705 (1970); Stanley S. Surrey, *Federal Income Tax Reform: The Varied Approaches Necessary to Replace Tax Expenditures with Direct Governmental Assistance*, 84 HARV. L. REV. 352 (1970); Stanley S. Surrey & Paul R. McDaniel, *The Tax Expenditure Concept: Current Developments and Emerging Issues*, 20 B.C. L. REV. 225 (1979); Stanley S. Surrey & Paul R. McDaniel, *The Tax Expenditure Concept and the Budget Reform Act of 1974*, 17 B.C. INDUS. & COM. L. REV. 679 (1976); Boris I. Bittker, *Accounting For Federal Tax Subsidies in the National Budget*, 22 NAT'L TAX J. 244 (1971); Stanley S. Surrey & William F. Hellmuth, *The Tax Expenditure*

tax policy has thus been unidimensional. It has viewed taxes as the creators of burdens to be minimized, equalized, and, ideally, neutralized.³⁸ It has not even noticed that by providing opportunities for the exercise of taxpayer choice, tax systems can empower.³⁹

Budget—A Reply to Professor Bittker, 22 NAT'L TAX J. 528 (1969). But see Edward A. Zelinsky, *James Madison and Public Choice at Gucci Gulch: A Procedural Defense of Tax Expenditures and Tax Institutions*, 102 YALE L.J. 1165 (1993); but cf. Edward A. Zelinsky, *Efficiency and Income Taxes: The Rehabilitation of Tax Incentives*, 564 TEX. L. REV. 973 (1986). Analyzing the effect of a reduction in taxes in a world with taxes is different from analyzing the effect of the introduction of a tax to a world without taxes. The former can induce a particular type of economic activity by creating a preference for it, while the latter will necessarily burden whatever activity it is imposed upon. It is therefore entirely consistent to say that the introduction of a tax creates a non-neutrality which, once created, can be exploited for the purpose of achieving some higher economic or social objective. HANDBOOK, *supra* note 25, at 86.

38. Although consideration of benefits in the study of the distribution of tax burdens has sometimes been suggested, the benefits referred to in that context consist of government transfer payments, which can also be seen as negative taxes and thus as a conceptually necessary part of an analysis of total distribution. See, e.g., CONGRESSIONAL BUDGET OFFICE, REDUCING ENTITLEMENT SPENDING 39-45 (1994); Edgar K. Browning, *The Burden of Taxation*, 86 J. POL. ECON. 649 (1978). See generally HOUSE SUBCOMM. ON HUMAN RESOURCES OF THE COMM. ON WAYS AND MEANS, SOURCES OF THE INCREASES IN POVERTY, WORK EFFORT, AND INCOME DISTRIBUTION DATA, WMCP NO. 2, 103d Cong., 1st Sess. 152-53 (Comm. Print 1993) (gauging an entity's economic well-being by measuring both its tax burden and its cash, and non-cash, pre-tax income—including government transfer payments and employer-provided fringe benefits); ROBERT J. MYERS, SOCIAL SECURITY 455 (3d ed. 1985), quoted in Nancy J. Altman, *The Reconciliation of Retirement Security and Tax Policies: A Response to Professor Graetz*, 136 U. PA. L. REV. 1419, 1425 n.26 (1988); Graetz, *supra* note 21, at 657-61; Kornhauser, *supra* note 11, at 492-93 & n.98 (offering a provocative view of the relationship between taxes, government welfare payments to the poor, and government "welfare payments" to the rich and middle-class). Cf. Vladimir Salzyn, *Designing an Optimal Personal Income Tax Rate Structure: Goals and Criteria*, 26 OSGOODE HALL L.J. 577, 586 (1988) (acknowledging that vertical equity cannot be analyzed without accounting for government transfer payments, but noting that a proportional tax coupled with government transfer payments is not necessarily fair as measured against a progressive tax). The relationship between empowerment and the decision to effect some transfer payments directly, and others through the tax system, is a complex and interesting one, but its exploration must await another day.

39. It is interesting to note that the excess burden of a tax results from the taxpayer's exercise of power. The attribute that leads to the excess burden is the behavioral sensitivity of the tax. To the extent that people behave so as to avoid the tax, they are also avoiding transactions whose benefits are then lost to the economy, creating a deadweight loss. The attribute that creates the bulk of the excess burden, is, then, the ability to refrain from engaging in the taxed activity. That ability to refrain exists because the taxpayer has the ability to choose to refrain. Thus, the very attribute that leads to the excess burden—the ability to choose to refrain from engaging in the behavior that gives rise to the tax—also empowers the taxpayer. It gives the taxpayer the power to choose to become subject to the tax, or not.

There is little question that systems of taxation are, indeed, burdensome. Few people like to pay taxes,⁴⁰ as politicians know only too well, and many devote considerable amounts of energy to advocating their reduction or abolition. But that is not the only possible view of taxes. Justice Holmes is reported to have said that “[t]axes are what we pay for a civilized society.”⁴¹ Just as Holmes was able to see positive where others saw only negative, so it should be possible to examine

40. I did, however, once hear of a client who liked his tax bill to be large because he saw the size of his tax bill as a reflection of how well he was doing. Many in the government would undoubtedly like to clone this fellow.

41. Justice Holmes is reported to have made a remark to this effect when a law clerk came upon him as Holmes was preparing his own federal income tax return and the clerk wondered why Holmes was not more disturbed by the task in which he was engaged. JEROME R. HELLERSTEIN, *TAXES, LOOPHOLES AND MORALS* 7 (1963). In a letter to Harold J. Laski, dated May 12, 1930, Holmes wrote, “I pay my tax bills more readily than any others—for whether the money is well or ill spent I get civilized society for it.” Letter from Justice Oliver Wendell Homes to Harold J. Laski (May 12, 1930), in 2 *HOLMES-LASKI LETTERS* 1247 (Mark DeWolfe Howe ed., 1953). Publicly, Justice Holmes communicated his feeling on the relationship between taxes and civilized society when dissenting in *Compania General de Tabacos de Filipinas v. Collector of Internal Revenue*, 275 U.S. 87, 100 (1927) (Holmes, J., dissenting), where he said that “[t]axes are what we pay for civilized society.” Those words are now engraved in the stone over the entrance to the main IRS building in Washington, D.C. MORTIMER LIPSKY, *A TAX ON WEALTH* 122 (1977); see John A. Miller, *Indeterminacy, Complexity, and Fairness: Justifying Rule Simplification in the Law of Taxation*, 68 WASH. L. REV. 1, 69 n.321 (1993). Franklin D. Roosevelt later used the statement as a prelude to remarking that “[o]ne sure way to determine the social conscience of a Government is to examine the way taxes are collected and how they are spent. And one sure way to determine the social conscience of an individual is to get his tax-reaction.” 5 *THE PUBLIC PAPERS AND ADDRESSES OF FRANKLIN D. ROOSEVELT* 522, 523 (Samuel I. Rosenman ed., 1938).

Justice Holmes publicly made his famous statement regarding taxes and civilization in the context of attempting to distinguish taxes from penalties. He distinguished the two by pointing out that taxes had a positive side, while penalties had none. Thus, he noted that “every exaction of money for an act is a discouragement to the extent of the payment required, but that which in its immediacy is a discouragement may be part of an encouragement when seen in its organic connection with the whole.” *Compania General de Tabacos*, 275 U.S. at 100 (Holmes, J., dissenting). Taxes are different from penalties, he said, because taxes have a positive side—they buy civilization in the form of the goods and services provided by the government. Penalties, on the other hand, do not have as their purpose the affirmative acquisition of goods or services. Penalties, according to Justice Holmes, have as their purpose only the prevention of certain conduct. While preventing the conduct in question may have positive consequences, the purpose of the penalty is to prevent its occurrence, whereas the purpose of the tax is to raise revenue to fund government services. Indeed, Holmes noted that the government can lawfully tax conduct that it cannot prevent, whereas it would be foolish for the government to penalize conduct if the imposition of the penalty would not prevent it, or perhaps more accurately, deter it. *Id.*

benefits where traditional tax policy has examined only fiscal burdens.⁴² Tax policy analysis need not remain unidimensional. A multidimensional analysis should yield a more complete picture of a tax system. Looking at tax systems as vehicles for empowerment provides such a multidimensional view and will permit analysis of, and answers to, a crucial question: Who should get to choose?

If progressivity is defined broadly, a system that distributes both its burdens and its powers progressively is, as a whole, less progressive than one that distributes its burdens progressively and its powers regressively, or proportionately.⁴³ The progressive/progressive system takes away with one hand (through progressive taxation), but gives with the other (through progressive distribution of powers), and thus empowers in proportion to the taking.⁴⁴ By contrast, the progressive/regressive system takes away progressively (through progressive taxation), but empowers in inverse proportion to the taking. By taxing progressively and empowering regressively, it confers its powers on those least subject to the taking. Of course, a progressive distribution of benefits (such as in the overall progressive/progressive system), might be desirable. Whether it is depends on the value placed on a progressive system of taxation.⁴⁵

42. Not surprisingly, the Internal Revenue Service has subscribed to Holmes' positive view of taxation. Not only is Holmes' aphorism inscribed over the entrance to IRS headquarters, the preface to Form 1040 now includes a statement from the Commissioner and a chart that explains the allocation of funds received by the federal government, presumably in an effort to make taxpayers feel better about paying taxes. As I will develop later, however, the positive attributes of taxation are greater than what taxation can buy. It is what a tax system itself, through its structure, can give those who are subject to it, independent of the purchasing power of the revenue raised, that reflects the deeply held values of those who design it.

43. A discussion of the question whether it is necessary to adopt such a broad redefinition of the concept of progressivity to incorporate analysis of the positive aspects of tax systems follows *infra* after the text accompanying note 49.

44. Note that the analysis of the distribution of powers is subject to all of the same debates as the analysis of the distribution of burdens. Thus, decisions about the unit of analysis and the period of analysis must be made, just as they need to be made with respect to the distribution of the tax burden. For a good analysis of the offsetting effects of regressive tax distribution versus progressive benefit distribution, see GEOFFREY KOLLMAN, CONGRESSIONAL RESEARCH SERVICE, SOCIAL SECURITY: THE RELATIONSHIP OF TAXES AND BENEFITS (1992), available in Westlaw, 1993 WL 751855; DON FULLERTON & DIANE L. ROGERS, WHO BEARS THE LIFETIME TAX BURDEN? (1993); C. Eugene Steuerle & Jon M. Bakija, *How Social Security Redistributes Income*, 62 TAX NOTES 1763 (1994).

45. The merits of progressivity have long been hotly debated. See Walter J. Blum & Harry Kalven, *The Uneasy Case for Progressive Taxation*, 19 U. CHI. L. REV. 417 (1952); CHARLES O. GALVEN & BORIS BITTKER, THE INCOME TAX: HOW PROGRESSIVE SHOULD IT BE? (1969); Harold M. Groves, *Toward a Social Theory of Progressive Taxation*, 9 NAT'L TAX J. 27 (1969); Alfred G. Buehler, *Ability to Pay*, 1 TAX L. REV. 243 (1946); Walter J. Blum, *Revisiting the Uneasy Case for Progressive Taxation*, 60

However uneasy the case for progressive taxation might remain today, it is fair to say that the question of progressivity continues to be significant in the formulation of contemporary tax policy.⁴⁶ Given that the degree of progressivity that any tax system provides is an important attribute of that system, the progressivity of any system ought to be ascertained as precisely as possible. Yet, tax legislation over the last decade has tended to mask the degree of progressivity in the system. It has used the front door to progressivity—the rate structure—less, and the back door to progressivity—limitations on, and phaseouts of, deductions as adjusted gross income rises—more.⁴⁷ Whatever the political merit of this approach, its effect on the overall progressivity of the tax system

TAXES 16 (1982); see also ALVIN RABUSHKA & ROBERT E. HALL, *THE FLAT TAX* (2d ed. 1995); Byrne, *supra* note 11; Pollack, *supra* note 11; Schoenblum, *supra* note 29; Joseph Bankman & Thomas Griffith, *Social Welfare and the Rate Structure: A New Look at Progressive Taxation*, 75 CAL. L. REV. 1905 (1987). Professor Coven has wryly observed that “Because the winner of the debate [over the merits of progressivity] cannot be objectively determined, and because the debate itself is entertaining, it will most likely continue for eternity.” Glenn E. Coven, *Corporate Tax Policy for the Twenty-First Century: Integration and Redeeming Social Value*, 50 WASH. & LEE L. REV. 495, 508 (1993). Professor Coven argues that because the distribution of the ownership of corporate stock is progressive, any reduction in the corporate income tax would be anti-progressive, and, in his view, undesirable. *Id.* For additional commentary on the desirability of a progressive structure, see Kornhauser, *supra* note 11; Marc Linder, *I Like Ike: Bringing Back Eisenhower-Era Progressive Taxation*, 67 TAX NOTES 833 (1995). Empirical work confirms the continuing appeal of progressivity as a matter of public policy. Michael L. Roberts & Peggy A. Hite, *Progressive Taxation, Fairness, and Compliance*, 16 LAW & POL’Y 27, 30-31 (1994). Indeed, the current debate over the merits of a flat tax underscore the continuing importance of progressivity in the formulation of tax policy. See *infra* note 174.

46. See GRAETZ & SCHENK, *supra* note 27, at 35-43. Simply because specific legislation makes the system more or less progressive, or is passed with more or less concern for the resulting distribution of the tax burden, does not diminish the importance of progressivity in evaluating a tax system as long as progressivity remains in the forefront of debate about the desirable objectives of tax policy. Thus, even those who might agree with Professor Graetz that the Tax Reform Act of 1986 “signal[ed] the demise of progressivity as the guiding principle for fairness in the distribution of federal tax burdens,” Michael J. Graetz, *Retirement Security and Tax Policy: A Reply*, 137 U. PA. L. REV. 1239, 1243 n.27 (1989), should also agree that, as long as scholars and policymakers continue to debate the appropriate level of progressivity, progressivity will remain an important concept in the formulation of tax policy. See Michael J. Graetz, *The Truth About Tax Reform*, 40 U. FLA. L. REV. 617, 626-28 (1988).

47. Empirical work confirms that the public has failed to understand the degree of progressivity that exists in the system. Roberts & Hite, *supra* note 45, at 44. The rate structure and the public’s equation of it with progressivity, obscures the structural factors that can serve to make the effective rate structure more, or less, progressive than the statutory rate structure. *Id.*; see also I.R.C. §§ 67, 68, 151(d) (West 1995).

has not gone unrecognized by scholars and thoughtful policymakers. Nevertheless, scholars and policymakers have not recognized the extent to which the degree of choice provided by the system affects the overall progressivity of the system. The need to present a complete picture of progressivity demands that this omission be corrected.

Adding an analysis of the distribution of the powers conferred by a tax system to the standard progressivity analysis, which focuses only on the distribution of burdens, can correct that omission. Such an analysis will yield a more complete picture of the progressivity of the system and thus better inform the debate on the optimum degree of progressivity.⁴⁸ My objective here is not to decide whether any given system ought to be more or less progressive.⁴⁹ My objective is much more modest. I want simply to point out that the distribution of power affects the overall progressivity of a tax system.

Of course, it is possible to conceptualize the positive aspects of a tax system—*i.e.*, the ways in which it can confer power—as separate and distinct from the concept of progressivity, as traditionally defined. Unlike the burden imposed by a tax system, most of which can be measured by the dollars of tax paid, the benefits conferred by a tax system cannot be measured in dollars. Indeed, it is difficult to conceive of numerical representation for the quantum of power bestowed by a tax system. Therefore, it would not be inappropriate to think of the empowering aspects of a tax system as separate from its progressivity, albeit equally important to an evaluation of its total impact. Nevertheless, the logical connection between the positive and the negative aspects of a tax system suggests that deciding whether to conceptualize

48. The progressivity of a system is determined by more than its rate structure. Indeed, the current federal income tax system achieves progressivity both through the rate structure and through expansion of the base as adjusted gross income increases. See I.R.C. §§ 67, 68, 151(d) (West 1995). Ultimately, the progressivity of the system must be judged by the distribution of the amount of taxes actually paid. Recent data suggests that the distribution of the tax burden remains progressive, so that the amount of taxes paid rises more steeply as income rises. Chris R. Edwards, *Who Pays Federal Income Taxes?*, 66 TAX NOTES 105 (1995). Analysis of the distribution of choice would complete this picture by suggesting the extent to which the distribution of burdens would be more progressive still if the distribution of choice were less progressive. In other words, in a system that distributes both benefits and burdens progressively, the distribution of the tax burden reflects choices to behave in ways that reduce tax liability as well as choices to behave in ways that do not. The existence of the choice is a benefit even to those who choose not to change their behavior. The removal of that choice would make the distribution of the burden more progressive still.

49. For an analysis of the important question of whether a progressive tax system, rather than substantive legal rules, should be used to accomplish redistribution of wealth, see Louis Kaplow & Steven Shavell, *Why the Legal System is Less Efficient than the Income Tax in Redistributing Income*, 23 J. LEGAL STUD. 667 (1994).

empowerment as being distinct from or a part of progressivity is less important than recognizing the importance of empowerment as a subject for tax policy analysis. Deciding whether progressivity should be redefined to include consideration of both positive and negative aspects or whether empowerment analysis should become a separate tool of tax policy is less important than acknowledging the importance of examining the ways in which tax systems empower. Either way, the concept of progressivity provides the anchor and the model for the analysis.

The first step toward developing a mechanism for analyzing the quantum of power bestowed by a given tax system is to recognize that tax systems can empower, and to dissect the ways in which they can do so. We must also develop a vocabulary for talking about the powers that tax systems can bestow. Only after that initial exploration should we try to develop a system for measuring the quantum of power that any given tax system can bestow and for determining the way in which that power is distributed. I seek here only to take the first step. Although the development of a measurement system must await another day, our current inability to measure the distribution of the powers should not detract from the insights to be gained from acknowledging and analyzing those powers.

IV. BURDEN POWER: CHOICE REGARDING THE DISTRIBUTION OF THE TAX BURDEN

A. The Nominal and Economic Burdens of a Tax

In addition to giving people the power to avoid the imposition of a tax by changing their behavior, tax systems can be designed in ways that make it possible for the nominal bearer of the tax burden to shift its economic burden to someone else. The nominal bearer of a tax bears the statutory responsibility for remitting the appropriate amount of money to the government.⁵⁰ For example, the nominal bearer of a

50. See RICHARD A. MUSGRAVE, *THE THEORY OF PUBLIC FINANCE* (1959); RICHARD A. MUSGRAVE & PEGGY B. MUSGRAVE, *PUBLIC FINANCE IN THEORY AND PRACTICE* 256-79 (1980); JOSEPH A. PECHMAN & BENJAMIN A. OKNER, *WHO BEARS THE TAX BURDEN?* 25-37 (1974); EDGAR K. BROWNING & WILLIAM R. JOHNSON, *THE DISTRIBUTION OF THE TAX BURDEN* 12-39 (1979); JCT PAMPHLET, *supra* note 2, at 20. The nominal burden is sometimes referred to as the statutory burden.

motor fuels excise tax is the seller of the fuel.⁵¹ Economists have long realized that the nominal bearer of a tax may not suffer any economic detriment as a result of the imposition of the tax. In the case of a motor fuels excise tax, the seller will not suffer as a result of the imposition of the tax if the tax causes the price of motor fuels to rise but does not reduce the demand for the fuels.⁵² In such a case, the seller can simply increase the price of the fuel by the amount of the tax. Although the seller would still bear the nominal burden of the tax, she will not bear its economic burden because imposition of the tax will not diminish her own economic well-being. The economic burden will be borne by the consumer.⁵³ Such an excise tax gives sellers the choice of either retaining the economic burden of the tax or passing it on to the consumer in the form of increased prices.⁵⁴ I will refer to that choice as the burden power.

51. JCT PAMPHLET, *supra* note 2, at 20.

52. *Id.* In reality, unless the supply of and demand for a product are completely inelastic, any rise in the price resulting from a producer's attempt to shift the economic burden of a tax to consumers will affect the demand for the product and therefore, to the extent demand for the product is reduced and the producer sells fewer units, the producer will bear some of the economic burden of the tax as well. The degree to which the economic burden of a tax will fall on producers or consumers depends on the relative elasticities of supply and demand for the product. As described by the Joint Committee:

The elasticity of demand is the percentage by which the quantity demanded falls if the price paid by consumers rises by one percent. The elasticity of supply is the percentage by which the quantity of supplies rises if producers' net receipts per unit rise by one percent. If the elasticity of demand for a good is high relative to its elasticity of supply, more of the incidence of a tax on the good falls upon producers. If the elasticity of supply of a good is high relative to its elasticity of demand, most of the incidence of a tax on the good falls upon consumers.

Id. at 25; see also PECHMAN & OKNER, *supra* note 50, at 27-37, 28 n.7.

53. PECHMAN & OKNER, *supra* note 50, at 27-37.

54. A seller who chooses to retain some or all of the economic burden of the tax would either not raise the price at all or raise it by something less than the full amount of the tax. I consider such a seller to have borne the economic burden of the tax, rather than simply bearing the burden of smaller profits, because, assuming equilibrium before the imposition of the tax, the seller should have been making a satisfactory level of profit before the tax was imposed. Any reduction in her profit after the introduction of the tax I would therefore attribute to the burden of the tax. Of course, the degree to which such a seller possesses burden power depends on the elasticity of demand for the product. Burden power is greatest when demand is inelastic, as it is in that case that the nominal bearer has the greatest ability to shift the economic burden of the tax. See *supra* note 52 and *infra* note 119. Indeed, it is the inelasticity of the labor supply that leads economists to conclude that workers bear the economic burden of the employer's half of the social security tax. See *infra* notes 96-98 and accompanying text. For a fuller explanation of the operation of burden power, see *infra* part IV.D.

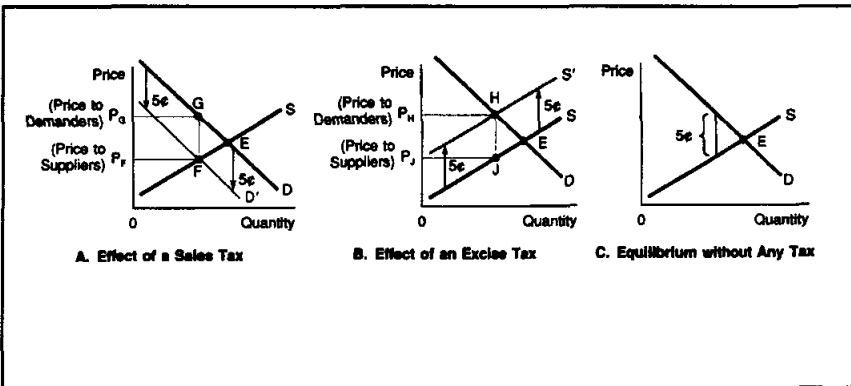
B. Traditional Economic Analysis

Traditional economic analysis posits that the nominal incidence of a tax does not affect its economic incidence.⁵⁵ Thus, whether a tax imposes its nominal burden on producers or consumers does not affect its economic incidence; rather, it is the shapes of the supply and demand curves for the good taxed that affect its economic incidence. Traditional economic analysis reaches that conclusion because the imposition of a tax on a particular item affects its equilibrium price in the same way regardless of whether the tax is nominally imposed on producers or consumers.⁵⁶ To illustrate, assume that a five-cent tax is nominally imposed on the purchasers of a widget.⁵⁷ That tax will have the effect

55. See, e.g., STEVEN E. LANDSBURG, PRICE THEORY AND APPLICATIONS 29 (2d ed. 1991); PECHMAN & OKNER, *supra* note 50, at 33 n.28 (addressing the incidence of the employment tax); JCT PAMPHLET, *supra* note 2, at 21-22. See generally OTTO VON MERING, THE SHIFTING AND INCIDENCE OF TAXATION (1942). See also *supra* note 10.

56. See, e.g., LANDSBURG, *supra* note 55, at 28-29.

57. This example, and the diagrammatic illustration that follows, as well as the explanatory text accompanying it, appears as Exhibit 1-10 in LANDSBURG, *supra* note 55, at 28. (Exhibits from PRICE THEORY AND APPLICATIONS, Second Edition by Steven E. Landsburg, copyright 1992 by the Dryden Press, reproduced by permission of the publisher.)



Panel A shows the market for lettuce before and after the imposition of a sales tax of 5 cents per head. The original demand curve (D) intersects the supply curve at E, which is the point of equilibrium before the tax. When the tax is instituted, the demand curve moves down vertically a distance 5 cents, to D'.

of shifting the demand curve for that widget down by a distance of five cents.⁵⁸ That shift will result in a new equilibrium price at a place five cents below where it was before the imposition of the tax, but that new equilibrium price will not represent the price consumers must pay for the widget because the new purchase price must include the five-cent tax they must pay. Thus, the price paid by consumers will be at a point five cents above the equilibrium point on the demand curve. If, instead, the tax were to be imposed on producers, the tax will shift the supply curve up by five cents and, again, there would be a new equilibrium point because the supply and demand curves would intersect at a point different from the point at which they intersected before the introduction of the tax.⁵⁹ That new equilibrium point would be at a position five cents above the point of pre-tax equilibrium, although the actual amount received by producers would have remained the same. Regardless of whether the supply or demand curve shifts, the post-tax price to consumers becomes the pre-tax price plus five cents and the post-tax price to producers is the same as the pre-tax price.⁶⁰ The tax therefore has the same effect whether nominally placed on producers or consumers.⁶¹

The new equilibrium point is F, and the new equilibrium price for lettuce is P_F . However, demanders must pay more than P_F for a head of lettuce—they must pay P_F plus 5 cents tax. Thus, the price to demanders is 5 cents higher than P_F . To find the corresponding point, begin at F and move up a distance 5 cents to G. Since F is on the curve D' , G must be on the curve D. The price to demanders is P_G .

Id. at 27, 29.

Panel B illustrates the effect of a 5 cent excise tax: The supply curve shifts upward a vertical distance of 5 cents, leading to a new market equilibrium at point H. The corresponding price, P_H , is what demanders must pay for a head of lettuce. But suppliers keep less than P_H when a head of lettuce is sold—they keep P_H minus 5 cents tax. Thus, the price to suppliers is 5 cents below P_H . To find the corresponding point, begin at H and move down a distance of 5 cents to J. Since H is on the curve S' , J must be on the curve S. The price to suppliers is P_J .

To compare the effects of the two taxes, we must compare the points G and F in panel A with the points H and J in panel B. In each case there is only one point on the curve D and one point on the curve S, and in each case the two points are a distance 5 cents apart. There is only one possible location for such points, as shown in panel C. It follows that points G and F are identical to points H and J. In other words, the sales tax and the excise tax have exactly the same effects on both suppliers and demanders.

Id. at 29.

58. See Panel A in the graph *supra* note 57.

59. See Panel B in the graph *supra* note 57.

60. Compare Panel A with Panel B in the graph *supra* note 57.

61. See Panel C in the graph *supra* note 57.

From the proposition that the tax will have the same effect regardless of whether its nominal burden is placed on producers or consumers it follows that the economic burden of a tax will remain the same regardless of whether its nominal burden is placed on producers or consumers. Since the distribution of the economic burden of a tax depends upon the shapes of the supply and demand curves, and those curves remain the same regardless of whether the nominal burden of the tax is placed on producers or consumers, it follows that the bearer of the economic burden of the tax will be the same regardless of who the nominal bearer is. Under this analysis, if suppliers bear the economic burden of a tax, they will do so regardless of whether the nominal burden of the tax is placed on them or on demanders.

Economists' focus on the two-dimensional world of supply and demand curves thus leads to the conclusion, unassailable from within the confines of that world, that placement of the nominal burden of the tax is irrelevant to the determination of its economic burden. That two-dimensional world, however helpful in explaining certain relationships, is inadequate to the task of describing the behavior of human beings, most of whom are not two-dimensional and many of whom make decisions on the basis of a multitude of factors.

C. *The Importance of Visibility*

Unlike economists, I believe that the placement of the nominal burden of a tax does matter. Placement of the nominal burden matters because it affects the visibility of the tax. The visibility of a tax matters because it determines the way people will react to it, not only in an economic sense but in an emotional and political sense as well.⁶² An individual who cannot differentiate between the effect of a tax and the effect of other market forces cannot change her behavior in response to the tax and can take no political action with respect to it. The visibility of the

62. Jerome Hellerstein, a noted teacher, scholar, and practitioner, well understood the importance of knowledge to the responsible exercise of the franchise, and he wrote an entire book designed to make the tax system accessible to people who were not tax professionals. HELLERSTEIN, *supra* note 41. As he stated in the introduction, "[u]nless laymen have before them nontechnical works which give them the key facts, pose the critical issues and present the alternatives, they are lost in acting as responsible citizens in a democracy." *Id.* at 5. More recently, Professor McCaffery has pointed out that the invisibility of certain taxes seems to account for their growth, precisely as cognitive theory would predict. McCaffery, *supra* note 6, at 1905.

tax thus affects the extent to which the political system becomes accountable for its actions.⁶³

Furthermore, the visibility of a tax can affect the economic response to it because humans are emotional beings who do not necessarily behave like the prototypical, wealth-maximizing economic paragon.⁶⁴ Accepting the economic precept that placement of the nominal burden of a tax is irrelevant to fixing its economic burden requires accepting the notion that all price changes produce the same effect. If people were simplistically motivated, perhaps that would be so, but I do not believe that the motivations for human behavior are so easily discernible. Consumers who know the reason for a price increase might respond differently to a five-cent increase in price that results from the imposition of a tax than to one that results from a supplier's decision to increase employee wages or from the supplier's attempt to increase its profit margin. Such knowledge might affect consumers' demand for a product, and thus change the post-increase equilibrium point.⁶⁵ For example, consumers might react to a price increase resulting from imposition of a tax by curtailing their consumption of a product out of a desire to rebel against the exaction, whereas they might react more benignly to a price increase occasioned by a producer's desire to appeal to a more affluent segment of the market; or vice versa. My point is not that knowledge will cause people to react in any particular way, but simply that knowledge will color their reaction. A visible tax provides that knowledge. As emotional beings for whom a dollar is not always just a dollar, people may alter their behavior based on that knowledge.

Visibility affects the ability to exercise burden power because one who knowingly bears the burden of a tax can decide whether to try to shift its economic burden. One who is unaware of the tax cannot even try. For example, producers who know that they are bearing the economic

63. Query: If voters knew and believed, as economists apparently do, that they, as providers of labor, bear the employer's half of the social security tax (which brings their employment tax burden to over 15 percent), would one see increased efforts to reform and reduce that tax? See *infra* note 96. Similarly, if employers knew and believed that employees actually bear the full economic burden of the social security and other employment taxes (including the half of the social security tax nominally imposed on employers), would the Internal Revenue Service have such trouble preventing employers from misclassifying workers as independent contractors? See *infra* note 100.

64. While economists often refer to maximizing utility, standard economic analysis equates utility with material wealth. While the focus on material wealth might reflect the relative ease of measuring material wealth and the relative impossibility of measuring other types of utility, it nevertheless presents an incomplete explanation and model for human behavior.

65. See *supra* note 57, for an explanation of the relationship between price changes and the equilibrium point.

burden of a tax in the form of higher prices will be able to use that information as leverage in price negotiations either with suppliers or consumers. In the end, a given producer may decide to retain some or all of the economic burden of the tax because shifting it would adversely affect her relationship with others. Whatever the producer's decision, it is the visibility of the tax (*i.e.*, the producer's knowledge of it) that gives her the power to make that choice.

Of course, merely possessing knowledge will not permit people to change their behavior. People must also be in an economic position to change.⁶⁶ In the short term, the empowerment that proceeds from visibility benefits only those in strong economic positions.⁶⁷ If the visibility of the burdens imposed by a tax system motivates those in weak economic positions to become politically active and to work to effect a change in the tax system, then visibility can, in the long run, redound to their benefit as well.

The visibility of a tax is tied to its nominal burden. Anyone other than the nominal bearer of the tax will find it difficult to react to the imposition of the tax because she will not be able to isolate the tax from

66. As discussed more fully in the text accompanying notes 144-50, *infra*, the ability to exercise choice is linked to economic position.

67. The ability of consumers to react to the effect of sales taxes illustrates this point. Retail sales taxes are visible. They are added to the price, noted on sales receipts and invoices, and even relied upon as a guide to the computation of the appropriate amount of tip. To borrow from the vernacular, sales taxes are "in your face." Despite their keen awareness of the tax's existence, most taxpayers can do little in the short term to avoid them other than refusing to purchase the taxed item. In the long term, however, they are not so powerless. The knowledge wrought by the "in your face" visibility of the tax can serve as a springboard for political action to change it. It is no accident that, of all of the tax increases enacted by former New Jersey Governor Florio, the increase in the sales tax was arguably the most unpopular. Nor was the unpopularity of that tax increase due simply to its regressivity. One of the factors that made the Florio tax increase so unpopular (contributing significantly to his failure to win re-election) was its high visibility. On a level of personal anecdote, I was impressed by the number of occasions on which sales people, and others waiting in line at stores in New Jersey during the time of the increase, remarked on the increase without any apparent prompting except the need to collect the tax. Indeed, I think that the sales tax increase probably hurt Governor Florio more than the income tax increase because the visibility of the sales tax, and the recurring nature of the need to pay it, served as a constant reminder of a politically unpopular act. See, e.g., Eugene Kiely, *Whitman Wins; Becomes State's First Woman Governor*, THE RECORD, Nov. 3, 1993, at A1 (noting that Florio "became the target of rallies across the state that drew thousands of people and wads of toilet paper, which came to symbolize the tax revolt after the state sales tax was extended to paper products, among other things."). But see McCaffery, *supra* note 6, at 1901-1905.

other factors that affect the price of an item. However clear it might be to economists that the nominal and economic burdens of a tax differ, the concept is not self-evident to non-economists. It is likely that few non-economists would recognize the difference absent the benefit of education on the point. Those who lack such education and who do not realize that the economic burden of a tax has been shifted to them cannot even begin to consider ways of changing their behavior in response to the imposition of the tax.

I recognize that what I am suggesting runs counter to accepted economic doctrine. As explained above, economic doctrine maintains that the economic burden of a tax is unaffected by the placement of its nominal burden because the economic burden of the tax is determined by the relative shapes of the supply and demand curves, which are, in turn, determined by the elasticity of supply or demand for the item in question.⁶⁸ Accepting this doctrinal position requires accepting the proposition that supply and demand curves accurately reflect all that is important about human behavior and that they follow laws that are, like the law of gravity, capable of being understood by humans but not capable of being altered. It also assumes that people possess complete knowledge. I neither accept the proposition nor make the assumption. While I might not disagree with economic doctrine in theory, I cannot accept it as either an explanation of, or a prescription for, human behavior.⁶⁹ Curves that depict patterns of supply and demand repre-

68. While economists do consider behavioral responses, they do so only in the context of considering the effect of price changes on the supply of, and demand for, a certain good. As the Joint Committee has explained,

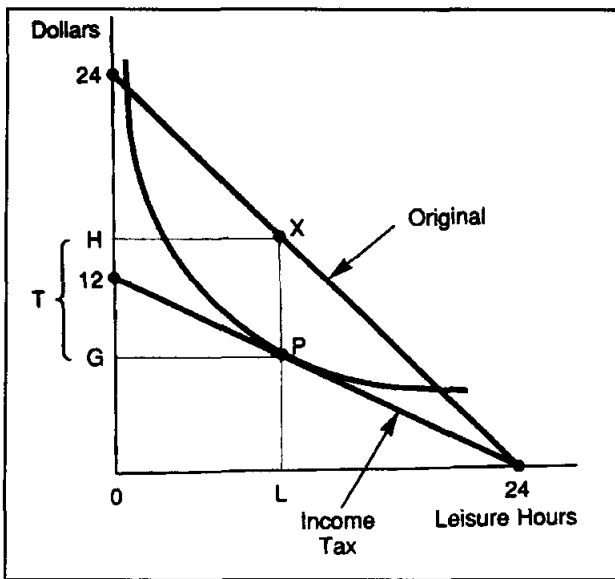
Economists measure the behavioral responses of consumers and producers by calculating the elasticity of demand and the elasticity of supply. The elasticity of demand is the percentage by which the quantity demanded falls if the price paid by consumers rises by one percent. The elasticity of supply is the percentage by which the quantity supplied rises if producers' net receipts per unit rise by one percent.

JCT PAMPHLET, *supra* note 2, at 25.

The shape of the supply and demand curves for particular goods will vary depending on the elasticity of supply and demand for them. The degree of elasticity depends on the relative shapes of the indifference curves of particular goods (or alternatively, on the relative cardinal utility of those goods) and the relationships between those shapes (or utilities) and each individual's budget line. For a good explanation of the role of indifference curves in the derivation of supply and demand curves and of the alternative theory of cardinal utility, see LANDSBURG, *supra* note 55, at 53-90. Although economists acknowledge the existence of choice, they focus on the result of the exercise of choice; that is, they assume information *ex post*. They do not separately value the existence of a choice.

69. The comparison of a head tax versus an income tax in the Landsburg text nicely illustrates the difference between the economists' classical treatment of choice and the new role which I seek for the concept. Professor Landsburg asks the question whether an individual would prefer to pay a head tax rather than an economically

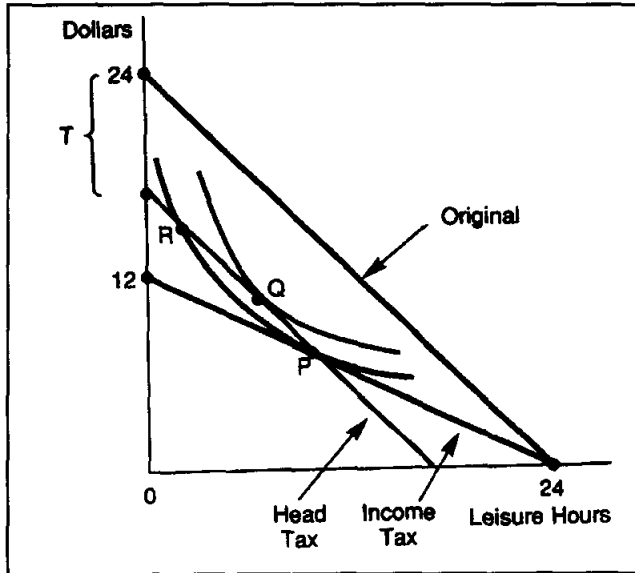
equivalent income tax—that is, an income tax that takes from the individual exactly the same amount of money as the head tax. He then analyzes the individual's budget constraint relative to the individual's indifference curve for leisure and concludes that since the head tax places the individual's optimum along a higher indifference curve than an income tax, a head tax is superior to an income tax. His analysis is graphically depicted as follows: These graphs, and the explanation that follows them appear as Exhibit 3-16 in LANDSBURG, *supra* note 55, at 79. (Exhibits from PRICE THEORY AND APPLICATIONS, Second Edition by Steven E. Landsburg, copyright 1992 by the Dryden Press, reproduced by permission of the publisher.)



PANEL A

Panel A shows your *original* (untaxed) budget line and your *income tax* budget line. The optimum on the *income tax* line is at P. Your after-tax income is \$G. Your before-tax income is equal to what you would earn if you were on your *original* budget line and working L hours, that is, \$H. Your tax bill is the difference, or \$T.

sent, at bottom, choices that individuals make. Choices made with complete knowledge will often differ from choices made with incomplete knowledge. If that is so, then a change in the quantum of knowledge provided might change the behavioral response observed.



PANEL B

Panel B shows the *head tax* budget line, which lies a vertical distance ST below the *original* budget line and consequently passes through point P . The optimum on the *head tax* line must be at a point like Q between P and R , and it is consequently on a higher indifference curve. The head tax is thus preferable to the income tax.

Id. at 79.

The foregoing analysis, while seductively precise, completely ignores the importance of taxpayer choice as an independent variable, an unsurprising outcome given its initial assumption that the head tax and the income tax would deprive the taxpayer of the same amount of money. But, the two systems of taxation are not absolutely equivalent precisely because of the importance of taxpayer choice. Under an income tax, taxpayers can choose whether to work more or consume more leisure and that choice will necessarily affect the size of their tax bill. Individuals should prefer a head tax to an income tax only if they do not value the ability to exercise that choice. The unpopularity of head taxes is testimony to the value individuals place on the exercise of choice. See GRAETZ & SCHENK, *supra* note 27, at 29; Peter Smith, *Lessons from the British Poll Tax Disaster*, 44 NAT'L TAX J. 421 (1991); John Turro, *The Second Battle of Britain: The Poll Tax*, 47 TAX NOTES 261 (1990). To compare the two systems without analyzing the importance of providing taxpayers with an opportunity to exercise choice is misguided.

D. Privatizing Taxation

If knowledge may affect behavior, including behavior in response to price changes, as posited, it should follow logically that acquiring knowledge can potentially change behavior. If the placement of the nominal burden affects the quantum of knowledge about a tax, then changing the placement of the nominal burden will change the quantum of knowledge available and thus change the behavior attributable to the imposition of the tax. In simpler terms, the more people know about a tax the more likely it is that they will change their behavior in response to it. Those who bear the nominal burden of the tax are in the best position to have that information and are thus most likely to be able to change their behavior in response to it. Indeed, one of the reasons the nominal bearer is often not the economic bearer might be that the nominal bearer has the knowledge, and often the power, to effect a shift.⁷⁰

70. Sometimes tax systems give the nominal bearer this power quite explicitly. The federal wealth transfer tax system serves as an example of such a system. Although dead people can't pay taxes, they can control whose share of their estate will be reduced by the payment of death taxes. (Whether testators bear the economic burden of death taxes is an open question the answer to which depends on the importance of the bequest motive and the extent to which the existence of the federal wealth transfer taxes alter it. See JCT PAMPHLET, *supra* note 2, at 10-11, 68.) To allow testators to exercise such control, most wills have "tax clauses." These are provisions that direct that the payment of death taxes be taken from particular, identifiable, portions of an estate. Thus, a will might provide that the federal estate tax shall be taken out of each beneficiaries' share proportionately. Alternatively, a will might provide that the federal estate tax shall be taken out of the share bequeathed to a specific beneficiary or even out of the residue. It is now well settled that if the will is silent, state law applies. Most states provide for an equitable apportionment of death taxes, whereby, in the absence of a direction to the contrary, death taxes are apportioned ratably. All of the state statutes operate only as default provisions, however. A testator may always direct the apportionment by will. Thus, testators retain the power to determine whose shares will be reduced by the payment of death taxes.

Perhaps an example will help to illustrate the effect of this analysis. Consider the situation of an unmarried testator, *D*, who has made no lifetime taxable gifts, who has one daughter, and who dies owning the following assets and no significant liabilities:

1. A bank account with \$25,000;
2. A house worth \$700,000;
3. A life insurance policy over which she has retained the incidents of ownership and which will pay \$1 million to her daughter;
4. Marketable securities worth \$700,000;
5. Household and personal effects of negligible value.

Assume also that in addition to her daughter, *D* has one sister and one companion with whom she is romantically involved. *D* wants her daughter to receive the proceeds of the

Awareness of a tax might affect not only the marketplace reaction to its imposition but the political reaction as well.⁷¹ Someone who does not know that she is bearing the economic burden of a tax cannot react politically to it. Such a person is, in a very real sense, disempowered and disenfranchised. That the study of economics could provide the missing knowledge is scant comfort because it is unlikely that enough individuals would engage in that study to allow reasoned discussion in a public forum. Taxation with representation can be no more than an illusion if the represented do not even realize that they are being taxed, or cannot appreciate the extent to which they are being taxed.

life insurance policy and any household and personal effects her daughter chooses. *D* wants her sister to receive the marketable securities. Finally, *D* wants her companion to receive the house, the bank account and any household and personal effects her daughter does not select. (My thanks to my friend and colleague, Jane Baron, whose story provided the seed for this example. Jane B. Baron, *Intention, Interpretation, and Stories*, 42 DUKE L. REV. 630 (1992)).

The federal estate tax bill for such an estate would amount to roughly \$643,000. If *D* does not alter her dispositive scheme to account for the need to pay the federal estate tax, state and federal law will do it for her by allocating the tax burden as provided by the applicable statutes. (In the case of the life insurance policy, the Code does it. See I.R.C. § 2206 (West 1995).) Similar provisions provide a right of recovery in the case of property subject to the marital deduction, I.R.C. § 2207A (West 1995), and property in which the decedent retained an interest, I.R.C. § 2207B (West 1995). Assuming that *D* chooses not to leave the allocation of the tax liability to state and federal law, *D* will then have to decide whose share of her property she will reduce. If *D* provides that the taxes will be paid out of the residue, only her companion's share will be reduced, but it will be reduced significantly. Most likely, the house will have to be sold and the companion will receive only the bank account and personal effects. If *D* provides that the tax will be paid out of her sister's share, her sister is likely to get nothing, unless the marketable securities increase in value significantly between the time of *D*'s death and the time of sale. If *D* provides that the taxes will be paid ratably out of the property, all beneficiaries will receive less.

A testator's ability to direct the source of payment of the federal estate tax has not generally been seen as an empowering feature, but merely as a matter of estate administration. See, e.g., Carolyn B. Featheringill, *Estate Tax Apportionment and Nonprobate Assets: Picking the Right Pocket*, 21 CUMB. L. REV. 1 (1990-91). Even those who have noted the importance of taking allocation of the tax burden into account in estate planning have done so in the context of trying to ensure that the various applicable rules are considered so that their operation does not disrupt the testator's dispositive scheme. *Id.* Indeed, these rules have been used to exhort estate planners to ensure that the desired beneficiaries bear the burden of the federal estate tax. *Id.* Yet, this scheme is empowering. It gives testators, not the government, the power to decide who will bear the economic burden of the tax.

71. That feelings about taxation, and political action in response to those feelings, run high is amply demonstrated by the passage of California's Proposition 13, which has had lasting effects in California, as well as elsewhere. See ARTHUR O'SULLIVAN ET AL., PROPERTY TAXES AND TAX REVOLTS—THE LEGACY OF PROPOSITION 13, at 5-7 (1995). Indeed, one of the reasons that property taxes spawn so much controversy is their extraordinarily high visibility. Property taxes are the among the most visible of taxes because they are not subject to withholding at the source. All taxpaying property owners must not only account for their property taxes, but must also write a check.

Acceptance of the proposition that the holder of the nominal burden can choose whether to shift or retain the economic burden of the tax has one additional, and somewhat more disturbing, consequence. It makes the holder of the nominal burden, rather than the government, proximately responsible for the imposition of the tax. It changes who decides who will pay the tax. It privatizes the decision. If an employer has a choice whether to shift or retain the economic burden of the employer's share of employment taxes, then any portion of those taxes that the employee bears as a result of the employer's decision to shift proceeds, at least proximately, from that decision. As long as holders of the nominal burden can choose to shift or to retain that burden, then it is not only possible, but probable, that similarly situated people will be taxed dissimilarly. Taxation will result, not from the imposition of a law equally applicable to all who are similarly situated, but from the exercise of many individual choices. The grant of burden power can therefore yield a system where unconnected individuals make decisions based on their own self-interest and ability to choose, and the possibility of uniformity and connectedness disappears.

E. Paternalism and Tax System Design

The foregoing dual consequences of the existence of burden power—the privatization of the decision regarding the identity of the bearer of the economic burden of the tax and the invisibility of the tax itself—reflect considerable paternalism.⁷² By hiding not only the

72. In his classic work on paternalism, Gerald Dworkin defined the term as “the interference with a person’s liberty of action justified by reasons referring exclusively to the welfare, good, happiness, needs, interests or values of the person being coerced.” Gerald Dworkin, *Paternalism*, in *MORALITY AND THE LAW* 107 (Richard A. Wasserstrom ed., 1971), reprinted in *PHILOSOPHY OF LAW*, *supra* note 35, at 230. Dworkin specifically regarded the social security system as paternalistic, classifying it as a system of laws that requires individuals to purchase retirement annuities, and, by imposing the requirement, interferes with liberty of action. *Id.* at 231. Dworkin referred to the type of paternalism represented by the social security system as “pure” paternalism, for it restricts the liberty of those whose good the restriction attempts to promote. *Id.* at 232. Dworkin’s subsequent broadening of his definition is consistent with this view of the social security system. See *infra* note 73. Dworkin’s view of the social security system as paternalistic is underscored by the relative lack of avoidance power for those who bear the economic burden of that system. Avoidance power is consistent with the existence of personal autonomy and is thus antithetical to paternalism. For an interesting twist on classic paternalism analysis, see McCaffery, *supra* note 6, at 1934-37. Although I find Professor McCaffery’s quasi-paternalism more attractive than

burden but also the identity of the person who inflicts it, a system high in burden power denies those who ultimately bear the economic burden of a tax the dignity of being able to control their destinies. Such a system restricts liberty by withholding the information necessary for informed judgments and fails to value the personal autonomy of those who bear the economic burden of its taxes.⁷³

That the system's designers might be able to estimate where the economic burden will ultimately reside and that they will seriously take those estimates into account in designing the system only underscores its paternalistic nature.⁷⁴ To all of those who have no burden power the designers of such a system are saying, in effect: We will ensure that the economic burden is distributed in an equitable manner. Therefore, you don't have to know that you are actually paying the tax or that someone other than the government is actually deciding to make you pay it. Trust us, even though we've denied you the information that would allow you to determine whether that trust is warranted. Like the song says, "Don't worry—Be happy!"⁷⁵

Even if the assumption that necessarily underlies such a statement were incontrovertible, that is, even if everyone could agree that burden tables accurately reflect economic reality,⁷⁶ such an attitude would be paternalistic in the extreme. That it is based on a debatable proposition—the accuracy of burden tables—makes it even more troublesome.⁷⁷ When the paternalistic attitude is directed toward those who

traditional paternalism, I aspire to a response that preserves personal autonomy to a degree greater than that afforded by quasi-paternalism.

73. Dworkin accepted Buchanan's definition of paternalism as "interference with a person's freedom of action or freedom of information, or the deliberate dissemination of misinformation." Gerald Dworkin, *Paternalism: Some Second Thoughts*, in *PATERNALISM* 105 (Rolf E. Sartorius ed., 1983), reprinted in *PHILOSOPHY OF LAW*, *supra* note 35, at 240 (quoting Allen Buchanan, *Medical Paternalism*, 7 *PHIL. & PUB. AFF.* 372 (1978)). Nevertheless, Dworkin would go further and define paternalism by reference to a denial of personal autonomy. Indeed, he believes that "it is because of the violation of the autonomy of others that normative questions about the justification of paternalism arise." *Id.* at 241.

74. For a thorough description of the ways in which distributional analysis is conducted and a critical appraisal of its uses and abuses, see *DISTRIBUTIONAL ANALYSIS OF TAX POLICY* (David F. Bradford ed., 1995) [hereinafter *DISTRIBUTIONAL ANALYSIS*].

75. Bobby McFerrin, *Don't Worry, Be Happy*, 73 Simple Pleasures (EMI-Manhattan Records 1988).

76. At least one influential commentator disagrees quite strongly. See Graetz, *supra* note 21.

77. The methodology employed by the different groups responsible for producing burden tables within the government alone makes reliance on these tables fraught with danger. As the papers presented at the December 1993 Invitational Conference on Distributional Analysis for Making Tax Policy sponsored by the American Enterprise Institute and published in *DISTRIBUTIONAL ANALYSIS OF TAX POLICY*, *supra* note 74, demonstrate, there is no one generally accepted methodology for conducting

lack capital, it reflects certain values as well: a high regard for the ownership of capital, a disregard for the personal autonomy of those who lack capital, and an endorsement of disconnectedness.⁷⁸ Those values are consistent with the values reflected by the grant of avoidance power to the holders of capital. For those who value personal autonomy independently of the ownership of capital, a tax system that provides a high degree of burden power should be judged undesirable for the same reason any other paternalistic system would be so judged: it violates the personal autonomy of at least some of those at whom it is directed. When that same system reserves the grant of avoidance power and the attendant opportunity for the exercise of personal autonomy for the owners of capital, the picture that emerges is one of a tax system that values the ownership of capital above all else. By reserving to the owners of capital not only the ability to choose the amount of their nominal burden but also the ability to shift the economic burden of the tax to someone else, while denying either ability to non-owners of capital, the system reflects the value of capital. That value is at odds with the values that have traditionally provided the philosophical underpinnings for progressive taxation—the value of fairness as manifested by the notion that tax liability should rise as ability to pay rises.⁷⁹

The effects of invisibility and privatization, and the denial of personal autonomy they beget, can be illustrated by considering the likely consequences of changing the social security tax system in a way that

distributional analysis and each of the three government agencies that perform distributional analysis employs different conventions and methodologies. The Office of Tax Analysis at the Department of the Treasury, the Joint Committee on Taxation, and the Congressional Budget Office each perform distributional analysis and produce burden tables. *Id.* at 111, 120, and 128. The extent to which any given burden table can be said to represent an accurate picture of the distribution of the tax burden is therefore quite problematical. R. Glenn Hubbard, *Distributional Tables and Taxes Policy*, in DISTRIBUTIONAL ANALYSIS, *supra* note 74, at 81; Thomas A. Barthold et al., *A Comparison of Distribution Methodologies*, in DISTRIBUTIONAL ANALYSIS, *supra* note 74, at 96. Michael J. Graetz, *Distributional Tables Tax Legislation and The Illusion of Precision*, in DISTRIBUTIONAL ANALYSIS, *supra* note 74, at 15. See also Graetz, *supra* note 21.

78. In observing that paternalism denies personal autonomy, Gerald Dworkin also observed that “[t]he denial of personal autonomy is inconsistent with having others share the ends of one’s actions—for if they would share the end, it would not be necessary to usurp their decision-making powers.” Dworkin, *supra* note 73, at 241.

79. Professor McCaffery uses cognitive theory, specifically the phenomenon of loss aversion, to explain this likely reaction. See McCaffery, *supra* note 6.

would place its nominal burden entirely on employees. Traditional economic doctrine would maintain that such a change is no change at all because the economic burden would remain unchanged in the long run. Yet, consider the likely taxpayer reaction to such a proposed change—it would almost certainly be adverse and vociferous. Indeed, it is difficult to imagine that any serious politician would even propose such a change because merely proposing it is likely to amount to political suicide. Even if economists could agree that the change would have no effect on the identity of the bearer of the economic burden of the tax, wage-earners, enlightened and empowered by the new visibility of the tax, would not be indifferent to the change.

Furthermore, even if such a change were made, the resulting system would quite likely be subject to more political scrutiny and controversy. Taxpayers would also be more likely to change their behavior in response to it, if only by choosing to consume more leisure. Under such a revised system, all employees would bear the full amount of the social security tax, both in the short term and in the long term. Changes in rates would be borne by employees in all industries immediately. Those employees who now benefit from their employer's inability to shift the economic burden of increased rates immediately upon enactment would lose that benefit under a revised system. All employees would, therefore, bear the full economic burden that government policy assumes them to bear,⁸⁰ and all employees would be able to identify the government as the entity responsible for the net amount of wages received.⁸¹

The federal income tax system receives so much more political and taxpayer attention than the social security system for at least two reasons. First, the annual obligation to file a return ensures that the

80. While it is theoretically possible for employers to choose to relieve employees of some of the economic burden of a social security tax that is nominally imposed entirely on employees, I don't think it is likely that employers would do so in many cases. First, shifting the economic burden of a tax away from oneself, as employers do under the current system, is different from shifting the economic burden onto oneself. Those employers who are in a position to shift the economic burden of the tax onto employees are hardly likely to assume the economic burden of any tax nominally imposed on employees. In addition, those employers who might choose to retain some or all of the economic burden of the tax under the current system might be less likely to do so under a system that imposed the nominal burden on employees.

81. Under the current system it is possible for employees to feel that their employer's greediness is responsible for their failure to receive a higher stated wage. An employer's failure to pay employees 7.65% more in wages (the prevailing employers' share of FICA under I.R.C. § 3111 (West 1995)) is likely ascribed to the employer's unwillingness to part with that additional amount, not to the fact that the government is taking that amount from the employer on the employee's behalf.

federal income tax system remains highly visible.⁸² Second, at least in the case of the individual income tax, the placement of the nominal and economic burdens on the same bearer makes application of the tax uniform, and its source—the government's decision to impose the tax—clear.⁸³ Further comparison of the federal income and employment tax systems will illustrate how an analysis of the extent to which tax systems empower can affect our views of those systems and the values they reflect.

V. CHOICES AND VALUES IN TWO PARALLEL SYSTEMS

The federal income tax system and the federal employment tax system⁸⁴ are the two most significant federal tax systems.⁸⁵ Together,

82. Placement of the obligation to file is relevant to the issue of visibility. There is no more direct way of making a tax visible than to require an individual to compute the amount due and remit a check therefor. Even a system of withholding at the source does not significantly detract from that effect as long as the taxpayer retains annual filing and remission obligations. However, when a system of withholding at the source does not obligate the taxpayer to perform an annual accounting and does not countenance refunds, as is typically the case with employment tax systems, the visibility of that system will be impaired. For an exception to the typical no-refund case, see Treas. Reg. § 31.6413(c)-1 (1993) (providing an exception to the "no refund" policy with respect to FICA taxes where an individual has had more than one employer during a taxable period). The impact of the obligation to file on the visibility of a tax explains, at least in part, why it was property taxes that spawned Proposition 13 and why it is the income and not the employment tax system that is the source of seemingly perennial debate and controversy.

83. This is certainly true for the portion of the individual income tax imposed on labor income, *see, e.g.*, JCT PAMPHLET, *supra* note 2, at 41-43 and sources cited *supra* note 44, just as it is true for an individual income tax on capital when the incidence of a tax on capital falls on the owners of capital. For a discussion of the difficulties of determining the incidence of a tax on capital imposed at the individual level, see JCT PAMPHLET, *supra* note 2, at 44-46. For purposes of this discussion, I have assumed, as has the JCT, that the incidence of the individual income tax on capital is on the owners of capital. *Id.* at 45. I have made this assumption because I am persuaded by the reasons the JCT stated for assuming likewise. *Id.*

84. I use the term "federal employment tax system" to refer only to the federal social security tax system created under the Federal Insurance Contributions Act (FICA), I.R.C. §§ 3101(a), 3111(a) (West 1995). The FICA tax is the largest and most broadly applicable of the federal employment taxes. Among the taxing provisions that fall outside that designation (which I do not consider for purposes of comparison to the income tax system) are the Federal Unemployment Tax (FUTA), the self-employment tax (SECA), and the Railroad Retirement Tax (RRTA). I exclude such provisions for varying reasons: In the case of FUTA, the effective tax rate applicable to any particular employer varies depending on the employer's experience as regards employee turnover. Consequently, the FUTA tax burden, economically borne by employees, is linked to

benefits paid out to past and present employees of that particular employer. Thus, FUTA operates more like an insurance premium than a tax (unlike the FICA tax which has been so far removed from its "social insurance" moorings that it may rightly be considered a tax). I.R.C. §§ 3301, 3302(a), 3302(b) (West 1995). The SECA tax is, by its very terms, a tax borne nominally by those taxpayers engaged in self-employment, *see* I.R.C. §§ 1401(a), 1401(b) (West 1995), and since that tax burden is directly attributable to the personal endeavors of the taxpayer, it is, like the federal individual income tax, difficult to shift economically. This characteristic, combined with the placement of its nominal burden on the individual, makes the SECA tax highly visible. For those inclined to self-employment, the SECA tax offers no avoidance power, no burden power, and little in the way of choice. It is precisely because the SECA tax system does not incorporate these features that I exclude it from my present discussion. Finally, I exclude the RRTA tax simply because it is a tax of relatively limited application. I.R.C. §§ 3201, 3231(a), 3231(b) (West 1995).

85. I regard the federal employment tax system as a true tax system. While the system was undoubtedly conceived as a funding mechanism for social insurance and, to a considerable extent, it still exists for that purpose, the use of the funds raised can be analyzed separately from the source of the funds, and the mechanism for the exaction of the funds is a tax. The Supreme Court analyzed the exaction as a tax and upheld its constitutionality as such. *Helvering v. Davis*, 301 U.S. 619 (1937); *Steward Mach. Co. v. Davis*, 301 U.S. 548 (1937). Indeed, the social security system has been widely criticized for its failure to operate as an insurance system, and has increasingly been analyzed under criteria applicable to an analysis of tax systems. *See* Graetz, *supra* note 28, at 852. While this approach to an analysis of the social security system has not been without its critics, *see* Altman, *supra* note 38, at 1427, I believe that it has gained sufficient currency to be treated as generally accepted.

Even economists treat the social security tax as a tax when drawing conclusions regarding the overall distribution of the tax burden. *See, e.g.*, Richard Musgrave, *A Reappraisal of Social Security Financing*, in *SOCIAL SECURITY FINANCING* 89, 110 (Felicity Skidmore ed., 1981) (concluding that the social security tax has reduced the overall progressivity of the system). Indeed, the important debate regarding whether the system is progressive or regressive and whether that question should be answered on the basis of the sources of funds alone or should combine an examination of both sources and uses, shows the extent to which viewing the system as one that imposes taxes (both positive and negative) has become an accepted part of the mainstream debate. *See* MYERS, *supra* note 38, at 455; *see also* JOSEPH A. PECHMAN ET AL., *SOCIAL SECURITY: PERSPECTIVES FOR REFORM* 178-80 (1968).

Moreover, there is a growing trend linking the social security and income taxes. One manifestation of this trend is the increased taxation of social security receipts. *See* Omnibus Budget Reconciliation Act of 1993, Pub. L. No. 103-66, §§ 13207, 13215, §§ 3121, 86(a), 107 Stat. 312, 467, 475 (1993) (increasing the maximum amount of social security benefits subject to the income tax). *See generally* COMMITTEE ON WAYS AND MEANS, 103D CONG., 2ND SESS., 1994 GREEN BOOK: OVERVIEW OF ENTITLEMENT PROGRAMS 30 (Comm. Print 1994); CONGRESSIONAL BUDGET OFFICE, *REDUCING ENTITLEMENT SPENDING* 31-34 (1994); James A. Fellows & J. Edison Haney II, *Taxing the Middle Class*, 71 *TAXES* 654 (1993); Jonathan B. Forman, *The Income Tax Treatment of Social Welfare Benefits*, 26 *U. MICH. J.L. REF.* 785 (1993); Philip J. Harmelink, *Taxation of Social Security Benefits: Analysis and Policy Recommendations*, 42 *TAX NOTES* 1363 (1989); Gene Steuerle, *Taxing Social Security Recipients*, 66 *TAX NOTES* 609 (1995). Another is the enactment and persistent expansion of the Earned Income Tax Credit (EITC), a mechanism designed in substantial part to alleviate the effects of the social security tax at the lower ends of the income scale. This conflation of the income and social security taxes underscores the similarities between the two exactions. For a thorough analysis of the EITC, *see* Anne L. Alstott, *The Earned Income Tax*

these tax systems provide over 70% of the total revenue collected by the U.S. Treasury.⁸⁶ The systems also share several features. In addition to raising approximately equivalent amounts of revenue, both systems are described by the Internal Revenue Code and both are generally familiar to working Americans. Yet, one of the systems takes nearly 2,000 pages to describe, while the other doesn't even manage to fill 100 pages.⁸⁷ Every law school offers at least one course on the 2,000 page system, while almost no law school offers even a seminar on the other.⁸⁸ Casebooks on one system fill the bookshelves of practically every tax professor in the country, while a law school casebook on the other has yet to be published. In short, one of the systems receives a phenomenal amount of scholarly and professional attention while the other gives rise to little controversy and is barely acknowledged.⁸⁹ Yet,

Credit and the Limitations of Tax-Based Welfare Reform, 108 HARV. L. REV. 533 (1995). For an excellent analysis of ways to improve the EITC, see George K. Yin et al., *Improving the Delivery of Benefits to the Working Poor: Proposals to Reform the Earned Income Tax Credit Program*, 11 AM. J. TAX POLICY 225 (1994). In sum, the absence of a direct correlation between the source of the funds and the uses to which they are put, which simultaneously infuriates the private insurance advocates and pleases those who would argue that the system is more progressive than a simple analysis of its tax structure would suggest, convinces me that the system imposes a tax and that it is appropriate to analyze it as such and to use its design to illustrate a concept germane to the design of tax systems generally. See generally SOCIAL SECURITY: BEYOND THE RHETORIC OF CRISIS (Theodore R. Marmor & Jerry L. Mashaw eds., 1988).

86. BUREAU OF THE CENSUS, U.S. DEPT OF COMMERCE, STATISTICAL ABSTRACT OF THE UNITED STATES 1994, 331 (table of federal receipts, by source, showing figures for 1993 (actual) and for 1994 (estimated)); *The Federal Government Dollar Fiscal Year 1996 Estimates*, 66 TAX NOTES 918, 919 (1995) (pie chart depicting estimated United States Government Fiscal Year 1996 Funding Sources); see also McCaffery, *supra* note 6, at 1876-82; Martin A. Sullivan, *Social Security Taxes: No Room to Grow?* 71 TAX NOTES 113 (1996).

87. As published by Commerce Clearinghouse, two volume set, 1995. INTERNAL REVENUE CODE (CCH 1995). This conclusion is based on a rough count of the pages in the two volume CCH set, which includes a restatement of prior versions of the provisions in very small print, and is subject to great understatement because of CCH's practice of having multiple pages that share a number (thus, there might be a page 6411-1, 6411-2, 6411-3 etc.) It is based on the rough number of pages occupied by Subtitle A of Title 26 minus the pages allocated to section 1402, the self-employment tax, and the number of pages allocated to Subtitle C of Title 26.

88. Indeed, most law schools offer at least 3 courses on the 2,000 page system but none on the other, and a number of law schools even offer graduate degrees in that system, while continuing to ignore the other.

89. This statement is, I believe, accurate as it pertains to legal scholarship, but is somewhat less accurate as it pertains to scholarship in the field of economics. With respect to legal scholarship, Jonathan Forman's recent work on the social security system

importance to the fisc cannot account for the disparity in attention paid by legislatures and the legal profession since both systems raise approximately the same amount of revenue.⁹⁰ Neither can the disparity be attributed to the extent to which they create burdens, at least insofar as the amount of burden is measured by the revenue generated. Something else must account for the difference. I believe that *something else* is the degree of choice, the quantum of avoidance and burden powers, that the systems provide.⁹¹ Comparing the two systems illustrates quite powerfully the benefits of broadening tax policy analysis to include the degrees of choice provided by particular systems of taxation.

Illuminating the existence of choice and the identity of its recipients in the federal income tax system in comparison to the employment tax system provides a stark and revealing contrast. Under the income tax system, the wealthier an individual is, the greater the choices she has. Not only do those with less wealth have fewer choices under that system, they also have a greater proportion of their wealth subject to tax under another system, one that provides virtually no opportunity for the exercise of choice—the employment tax (social security) system.⁹²

is a notable exception. Forman, *supra* note 85. So too is that of Michael Graetz, Nancy Altman, and W. Cohen. See WILBUR J. COHEN, RETIREMENT POLICIES UNDER SOCIAL SECURITY (1957); Graetz, *supra* note 28; Altman, *supra* note 38; Graetz, *supra* note 46. While the foregoing scholarship is excellent, its volume cannot even begin to approximate the volume of excellent scholarship devoted to the income tax, by scholars of such stature as Professor Graetz himself. For an excellent compendium of the economics literature on the social security tax system, see Graetz, *supra* note 28; Altman, *supra* note 38; Graetz, *supra* note 46.

90. See *supra* note 86. Professor McCaffery puts the figure at 85%. McCaffery, *supra* note 6, at 1877.

91. I do not believe that the difference is attributable to the ostensible design of one as a tax and the other as a program of social insurance because I do not regard the employment tax system as a system of social insurance. See *supra* note 85.

92. Chris Edwards has shown that “most lower- and middle-income Americans now pay more social insurance taxes than they pay in federal income taxes.” Chris R. Edwards, *Typical American Family Pays 40 Percent of Income in Taxes*, 66 TAX NOTES 735 (1995). In 1993, the median income family (defined according to the Bureau of Census as two employed, married adults), had total income of \$51,204 and paid \$7,834 in federal social insurance taxes compared to \$5,341 in federal income taxes. *Id.* at 736. For 1994, Edwards’ study estimates that the median income family will have total income of \$53,354 and will pay \$8,163 in social insurance taxes and \$5,581 in federal income taxes. *Id.* Edwards’ data is based on the assumption that both shares of the federal social security tax are economically borne by employees, as most economists believe them to be. See *infra* note 96.

A review of the data published by the Internal Revenue Service in its Summer 1995, STATISTICS OF INCOME BULLETIN tends to support Edwards’ conclusions. INTERNAL REVENUE SERVICE, STATISTICS OF INCOME BULLETIN (1995) [hereinafter SOI]. Thus, in 1990-91, when the social security tax rate on employees was 7.65%, SOI table 2 showed that individuals filing tax returns that showed adjusted gross income (AGI)

The employment tax system is nearly bereft of avoidance power for employees. The receipt of compensation for personal services generates the liability for the tax. Therefore, the choice reduces to one between working and not working (or, as economists like to put it, consuming leisure) or perhaps, working illegally.⁹³ Furthermore, because the rate structure of the tax is not progressive,⁹⁴ the existence of the tax does

between \$17,000 and \$19,000 paid federal income tax at the rate of 7.6% (1990) to 7.4% (1991) of AGI. *Id.* at 155. Such individuals were therefore remitting as many dollars to the federal government in social security tax as they were in federal income tax. Individuals with AGI of less than \$16,000, whose effective federal tax rate as a percentage of AGI was less than 7.65%, were remitting more dollars to the federal government in social security taxes than in federal income taxes. If both halves of the social security tax are taken into account, the disparity in remissions is, of course, even greater at the lower income levels since the federal income tax payment would stay the same. Indeed, the remissions attributable to both halves of the social security tax would not even out until taxpayers have over \$75,000 of AGI. While the SOI comparison is somewhat inexact (the tax figures include self-employment tax) they nevertheless provide some basis for corroborating Edwards' conclusion and illustrating the relative size of the disparity in tax remissions. Professor McCaffery has also provided a powerful and detailed illustration of this effect. McCaffery, *supra* note 6, at n.33.

93. Even outright evasion of the tax requires that the individual obtain the cooperation of her employer, thus depriving the individual of the ability to choose unilaterally to alter her behavior so as to remove the obligation to pay the tax. This issue received a great deal of publicity when it was revealed that President Clinton's nominee for Attorney General, Zoe Baird, had failed to pay employment taxes with respect to individuals she had hired to perform domestic services. Stephen Carter, *The Confirmation Mess, Cleaning Up the Federal Appointments Process*, § 7.25-28 (1994); McCaffery, *supra* note 6. Subsequent nominees for high appointive office underwent similar scrutiny, and the ensuing debate led to the enactment of significant changes to the threshold filing requirements. The Social Security Domestic Employment Reform Act of 1994, Pub. L. 103-387, § 2, 108 Stat. 4071 (creating I.R.C. § 3510); see also Scott E. Grimes & Marylyn K. Wiggam, *Nanny Tax Act Eases Rules for Employers of Domestic Workers*, 23 TAX'N LAW 212-16 (1995). Scholarly debate on the effect of the tax on the domestic workers' decision to work has become quite heated. See, e.g., Marc Linder, *What Hath Zoe Baird Wrought? The New FICA Amendments on Domestic Service Employees*, 66 TAX NOTES 113 (1995); Jonathan B. Forman, *Beyond the Nanny Tax: A Cut for All Low-Income Workers*, 66 TAX NOTES 741 (1995); Tom Silver, *The Zoe Baird Debate: A Member of the 'Oppressor' Class Responds*, 66 TAX NOTES 893 (1995); Marc Linder, *Marc Linder Responds to Silver and Forman*, 66 TAX NOTES 894 (1995).

94. Although the social security tax rate structure is not progressive, the distribution of social security benefits tends to offset the tax burden. Taken together, the social security tax and benefit structure is generally either proportional or mildly progressive, although this effect can vary tremendously between individual taxpayers. See Graetz, *supra* note 28, at 872-74; see also Camilla E. Watson, *Machiavelli and the Politics of Welfare, National Health, and Old Age: A Comparative Perspective of the Policies of the United States and Canada*, 1993 UTAH L. REV. 1337, 1362 n.123.

not affect the decision to work at the margin, except perhaps at the point where additional wages become free of the tax.⁹⁵

The employment tax system also gives little avoidance power to employers. If the business requires the performance of services, the employment tax will be paid by someone—either an employee or an independent contractor. The only question is who will bear the nominal burden of the tax.

By contrast, the employment tax system does create burden power, but bestows it almost exclusively on employers. For purposes of formulating tax policy, economists generally agree that when it comes to ability to shift the economic burden of taxes, the owner of the business has it all and the hired hand has none.⁹⁶ Economists reach the conclusion that employees bear the economic burden of employment taxes by noting that the labor supply is generally inelastic and that employers treat

95. While generating income above the level subject to the tax would remove the obligation to pay the tax on that additional income, individuals who lack the economic clout to set their level of compensation effectively do not have that option. Also, the existence of the option is really chimerical because the existence of the tax does not motivate individuals to generate given levels of income. Unless the level of a tax becomes confiscatory, earning more money will always be preferable to earning less, particularly if it can be done without forgoing the consumption of leisure.

96. Many economists acknowledge, however, that the incidence of the employer portion of the payroll tax is uncertain. See A. B. Atkinson, *The Distribution of the Tax Burden*, in John M. Quigley & Eugene Smolensky, MOD. PUB. FIN. 13, 20-36 (1994) (citing Richard A. Musgrave et al., *The Distribution of Fiscal Burdens and Benefits*, in 2 PUB. FIN. Q. 259, and JOSEPH A. PECHMAN, WHO PAID THE TAXES, 1966-85 (1985)). Theoretically, it can be shifted forward to consumers or backward to employees. *Id.* (quoting George F. Break, *Incidence and Economic Effects of Taxation*, in THE ECONOMICS OF PUBLIC FINANCE 168 (Alan S. Blinder et al. eds., 1974)). Some assert that it is borne by employees. See, e.g., Eugene Steuerle & Paul Wilson, *The Taxation of Poor and Lower-Income Workers*, 34 TAX NOTES 695, 700-01 (1987); Lawrence H. Thompson, *The Social Security Reform Debate*, 21 J. ECON. LITERATURE 1425, 1453 (1983). Significantly, the government economists in this country uniformly ascribe it to employees. Thus, the Joint Committee's burden tables assume that the entire burden of the tax on labor (employers' and employees' share) falls upon those supplying the labor, because most analyses of the incidence of taxes of labor in the United States so assume. JCT PAMPHLET, *supra* note 2, at 41 (citing JOSEPH A. PECHMAN & BENJAMIN A. OKNER, WHO BEARS THE TAX BURDEN? 25-37 (1974)); Pechman, *supra*; BROWNING & JOHNSON, *supra* note 50; James R. Nunns, *OTA's Methodology for Distributional Analysis 1* (Dec. 16-17, 1993) in DISTRIBUTIONAL ANALYSIS, *supra* note 74, at 111; Richard A. Kasten & Eric J. Toder, *CBO's Methodology for Distributional Analysis 2* (Dec. 16-17, 1993) in DISTRIBUTIONAL ANALYSIS, *supra* note 74, at 120. By contrast, government economists in the United Kingdom apparently assume that the burden is shifted forward to consumers in the form of higher prices. Atkinson, *supra* (citing Michael O'Higgins, *The Distributive Effects of Public Expenditure and Taxation: An Agnostic View of the CSO Analyses*, in TAX'N AND SOC. POL'Y 28 (Cedric T. Sandford et al. eds., 1980)). In this country, Browning has argued that the social security tax cannot fall exclusively on workers. Edgar K. Browning, *Tax Incidence, Indirect Taxes, and Transfers*, 38 NAT'L TAX J. 525, 532 (1985).

employment taxes as a cost of acquiring labor. By then further assuming that employers are willing to spend only a finite amount for labor, economists posit that the amount of any employment taxes attributable to a particular worker will reduce the amount of cash and other compensation that the employer will be willing to provide that worker. The inelasticity of the labor supply ensures employers that employees won't stop working simply because they are receiving smaller wages as a result of the imposition of the tax. Thus, the tax ends up burdening the employee.⁹⁷

Of course, over the short term, many employers must absorb the costs of increases in employment taxes because the market cannot react instantaneously to such changes.⁹⁸ Nevertheless, over the long term, many economists believe that employers shift the costs of employment taxes to employees. I believe that employers do so because they choose to do so. That shifting the economic burden of the tax is consistent with behaving as a rational, profit-maximizing economic actor, does not make it less of a choice. Furthermore, employers have that choice and employees do not. Employees have no burden power because there is no one to whom they can shift the economic burden of employment taxes.⁹⁹ Employers also have some power to shift not only the economic burden of employment taxes, but the nominal burden as well, by structuring their operations so as to retain independent contractors instead of employees. Employers' leeway in this regard is not great and

97. JCT PAMPHLET, *supra* note 2, at 42-43.

98. *Id.* at 43.

99. In theory, employees have several choices: they can choose to work less and consume more leisure, they can work illegally, or they can save so as to accumulate capital and then live off the income from capital. The first alternative is not practical for people living at the edge of subsistence. For those people, the choice between work and leisure is really a choice between working and receiving government transfer payments. Since many people abhor the 'dependency' that accompanies reliance on government transfer payments, that choice is, practically speaking, a non-choice. Even were it not illusory, we would still want to discourage, or even disallow, such a choice as a matter of public policy. The second alternative is equally impractical. Many people would find the idea of working in an illegal economy as unpalatable as not working at all. Thus, even for well-to-do individuals, the ability to choose to work illegally offers (practically speaking) no choice at all. And, from a policy standpoint, we should certainly discourage the migration of labor from legal to illegal economic activity. Finally, the third alternative—living off the income from capital—is, like the first, impractical for people living at the edge of subsistence. Such individuals must spend everything or nearly everything they make to survive. Even for individuals not on the edge of subsistence, this alternative is available only as a long-term strategy.

the Internal Revenue Service seems intent on making it ever smaller,¹⁰⁰ but whatever leeway does exist with respect to the classification of workers rests with employers, not with employees.¹⁰¹ Most of the factors that distinguish employees from independent contractors are within the province of those who receive the work, not those who provide it.¹⁰² Those who receive the work also have the greatest

100. In the early 1970s, the Internal Revenue Service initiated an aggressive enforcement campaign targeted at businesses that classified workers as independent contractors. John E. North, *The Employment Tax Morass*, 11 CREIGHTON L. REV. 775, 792-801 (1978). The Service had apparently come to believe: (1) that self-employed workers were less likely to comply with federal tax obligations than were wage earners, and (2) that many businesses exacerbated the problem by misclassifying their workers as "independent contractors" (i.e., "self-employed") rather than "employees." William H. Smith, "Independent Contractor" or "Employee"?—*That is the Question*, 1 N.Y.U. PROC. OF THE 33rd ANN. INST. ON FED. TAX'N 577, 589-90 (1975). See generally *Independent Contractor Status: Hearing Before the Comm. on Small Business, House of Representatives*, 104th Cong., 1st Sess. 58-89 (1995) (Coopers & Lybrand study citing IRS and GAO studies that confirm those beliefs) [hereinafter *Independent Contractor Status*]; Piroška Soos, *Self-Employed Evasion and Tax Withholding: A Comparative Study and Analysis of the Issues*, 24 U.C. DAVIS L. REV. 107, 113-20 (1990). For a good exposition of the problem and a description of the legislative and taxpayer responses, see Myron Hulen et al., *Independent Contractors: Compliance and Classification Issues*, 11 AM. J. TAX POL. 13 (1994). The problem has defied a solution but legislators continue their search.

At least three bills targeting the employee/independent contractor controversy were introduced during the 104th Congress alone. See H.R. 1972, 104th Cong., 1st Sess. (1995) (the "Independent Contractor Tax Simplification Act of 1995"); H.R. 510, 104th Cong., 1st Sess. (1995) (the "Misclassification of Employees Act"), and H.R. 582, 104th Cong., 1st Sess. (1995) (the "Independent Contractor Tax Fairness Act of 1995"). For examples of the current debate, and of IRS efforts to address industry concerns, see *IRS Overzealous in Enforcement of Independent Contractor Laws, Small-Business Representatives Say*, TAX NOTES TODAY, July 27, 1995, available in LEXIS, at 95 TNT 146 (summing up industry concerns voiced at July 26th hearing of the House Small Business Subcommittee on the classification of independent contractors); *IRS Reverses Field on Worker Classification*, 67 TAX NOTES 1381 (1995) (correspondence between Rep. Nancy L. Johnson and IRS Commissioner Margaret M. Richardson); Guy Vander Jagt et al., *The Significance of the IRS Shift On Worker Classification*, 67 TAX NOTES 1677 (1995); *IRS Targets Classification of Workers*, TAXES ON PARADE, Aug. 10, 1995, at 3 (noting current IRS initiatives designed to harmonize and clarify internal IRS procedures relating to worker classification).

101. It is ironic to note that this is also true in Russia, former bastion of the worker, and that American practitioner publications are explicitly advising employers to try to structure their operations in Russia through the use of independent contractors to avoid the need to comply with the provisions of the Labor Code of the Russian Federation and the need to withhold under the Russian individual income tax or make social benefit payments on behalf of the individual service provider. See Jean A. Brough & Yuri A. Timokhov, *Employment Through Independent Contractor and Consulting Agreements*, 5 EAST/WEST EXECUTIVE GUIDE 2, 22 (Feb. 1995). Capitalism seems truly to have arrived in Russia, warts and all.

102. See Treas. Reg. § 31.3121(d)-1 (as amended in 1980); Rev. Rul. 87-41, 1987-1 C.B. 296; Hulen et al., *supra* note 100, at 83; Walter H. Nunnallee, *Why Congress Needs to Fix the Employee/Independent Contractor Tax Rules: Principles, Perceptions,*

economic incentive to reclassify. By classifying workers as independent contractors the recipients of labor also free themselves from the nominal burden of employment taxes and, perhaps as significantly, from the attendant federal and state reporting requirements. Moreover, market imperfections may make it possible for labor recipients to reap the economic benefit of avoiding the payment of employment taxes. If workers do not realize that they bear the economic burden of employment taxes, they may judge the adequacy of their remuneration under an independent contract without taking into account the increase in nominal employment tax liability that will befall them as independent contractors. Any difference between what a labor recipient would pay on account of an employee and what it actually pays an independent contractor would inure to the benefit of the labor recipient and the detriment of the labor provider.¹⁰³

Problems, and Proposals, 20 N.C. CENT. L.J. 93 (1992).

103. For example, a labor recipient *R* who is willing to pay \$100 for services, inclusive of employment taxes, would offer a wage of \$92.89 (arrived at by solving the equation: $w + 7.65\%w = \$100$, where w is the nominal wage). If *R* can retain the services of an independent contractor for that same amount, *R* is ahead because she can pocket the entire \$7.11 that would otherwise have been remitted to the government (except that portion offset by the section 162 deduction) and the independent contractor is left holding the bag for the full employment tax liability. Even if the independent contractor were to demand more than \$92.89, as long as that demand was less than \$100, *R* would come out ahead. The independent contractor, on the other hand, should seek to secure remuneration sufficient to allow him to pay one-half of his self-employment tax and still be left with at least \$92.89, the nominal amount he could expect to be paid by *R* in an employment context (such amount being subject, in the latter case, to withholding of his one-half share of employment taxes). Thus, the independent contractor's remuneration x would need to satisfy the relationship: $x - \frac{1}{2}(s) \geq \92.89 , where s represents his SECA tax liability. Now, $\frac{1}{2}(s) = 7.65\%(x - 7.65\%[x])$. Thus, his remuneration, x , would need to satisfy the relationship: $x - 7.65\%x + 7.65\%(7.65\%)x \geq \92.89 or, equivalently, $x(1 - 7.65\% + 7.65\%[7.65\%]) \geq \92.89 , or $x(.9294) \geq \$92.89$, or $x \geq \$92.89 \div (.9294)$, or $x \geq \$99.95$. If the independent contractor accepts anything less than \$99.95, then, all other things being equal, he will be less well off than had he agreed to work as an employee for the \$92.89 wage. These computations are based on the current self-employment tax rate of 12.40% for OASDI and 2.90% for hospital insurance, hence, a total of 15.3% in SECA taxes. I.R.C. §§ 1401(a), (b) (West 1995). Employers and employees each pay 6.2% for OASDI. I.R.C. §§ 3101(a), 3111(a) (West 1995). They also pay 1.45% for hospital insurance. I.R.C. §§ 3101(b), 3111(b) (West 1995). The total burden for each is 7.65% (or 15.3% collectively) in FICA taxes. Note that bearing the nominal burden of the self-employment tax does not, as a rough matter, disadvantage a self-employed individual *vis a vis* an employee because I.R.C. §§ 164(f) and 1402(a)(12) allow the self-employed individual to make use of deductions that offer tax advantages comparable to those enjoyed by employees. I.R.C. §§ 164(f), 1402(a)(12) (West 1995). For further discussion of this and other

Classifying a worker as an independent contractor rather than as an employee means that the labor recipient will have to pay no employment taxes (either FICA or FUTA) with respect to the performance of the work, while the labor provider will bear the full responsibility for the self-employment tax.¹⁰⁴ For tax purposes, the labor recipient has everything to gain by structuring the performance of such labor so that it can be performed by an independent contractor rather than an employee.¹⁰⁵ The labor recipient, that is, the owner of capital, can therefore either shift the nominal burden of the tax or refrain from incurring it at all depending on how she structures the receipt of services. Of course, not all labor recipients can structure the manner in which the labor is provided so that the provider qualifies as an independent contractor. But the point is that if anybody has the power to avoid incurring a nominal or economic tax liability under the employment tax system, that person is the owner of capital, not the provider of labor. Whatever avoidance power the system does provide goes to the owners of capital, not the providers of labor.

Notably, the labor recipient who succeeds in retaining independent contractors rather than employees succeeds in transferring the entire nominal burden of the employment tax to the individual labor provider.¹⁰⁶ Labor providers who are classified as independent contractors end up paying a highly visible tax, and doing so at least in part because a labor recipient decided to have them pay it.¹⁰⁷

issues relating to the tax treatment of self-employed individuals, see *infra* note 107, and sources cited therein. Of course, notwithstanding the clinical analysis entered into above, other factors obviously enter into a labor recipient's calculus on whether to retain an independent contractor in lieu of hiring an employee. For example, if the labor recipient opts to use an independent contractor, she would no longer pay federal and state unemployment taxes. The government would thus lose the benefit of that FUTA. But, that loss of revenue should not put the government at a significant disadvantage since it does not assume unemployment liability with respect to the independent contractor as it would have for the same individual working as an employee.

104. I.R.C. § 1401 (West 1995); see also *supra* note 103.

105. See Nunnallee, *supra* note 102, at 95-96; see also *supra* note 103.

106. I.R.C. § 1401 (West 1995); see ALICIA H. MUNNELL, *THE FUTURE OF SOCIAL SECURITY* 85-89 (1977); John L. Brown, *A Comparison of Four Models of Taxation in Their Treatment of Social Security Contributions and Retirement Benefits*, 15 WM. MITCHELL L. REV. 991, 994, 1004 (1989); Graetz, *supra* note 28, at 867; cf. Derek C. Bok, *Emerging Issues in Social Legislation: Social Security*, 80 HARV. L. REV. 717, 729 (1967) (noting that economists disagree on the extent to which employers' contributions are shifted backward to employees as opposed to being shifted forward to consumers in the form of higher prices).

107. The self-employment tax is paid with the federal income tax, on Form 1040 (Schedule SE), and is subject to the requirement that quarterly estimated tax payments be made. I.R.C. § 6654(c)-(d) (West 1995). The Internal Revenue Code contains provisions designed to provide self-employed persons with tax treatment roughly equal to that provided to employees. For example, employees receive the benefit of reduced

Looking at the employment tax system through the lens of empowerment thus reveals that whatever quantum of avoidance or burden powers it provides goes to employers.¹⁰⁸ In addition, the system is low in

cost health insurance by virtue of the deductibility of health insurance plans by employers (the employees bear only the economic burden of the employer's net cost for that insurance). The Code attempts to provide self-employed persons with comparable treatment by allowing them to deduct 30% of their personal health insurance costs from self-employment gross earnings for income tax purposes. I.R.C. § 162(l) (West 1995). Employees also receive the benefit of an "exclusion" from income of that portion of employment taxes (7.65% of wage income under current law) attributable to employees but nominally borne by employers. That "exclusion" reduces the base upon which both income, and FICA, taxes are based.

The Code provides analogues for self-employed persons. Section 164(f) gives self-employed persons an income tax deduction equal to one-half of self-employment taxes (such amount being 7.65% under current law). I.R.C. §§ 164(f), 1401(a), 1401(b) (West 1995). Section 1402(a)(12) provides a similar deduction for purposes of computing SECA tax liability. Whether these allowances actually serve to place self-employed persons on an equal tax footing with employees is dependent on several variables, including the respective marginal tax rates of employer and employee. On the whole, however, most tax analysts agree that, notwithstanding these allowances, self-employed persons are less favorably treated than are wage earners. See, e.g., Alan D. Campbell, *Making the Self-Employment Tax More Equitable*, 68 TAX NOTES 625 (1995); Philip J. Harmelink & Janet F. Speyrer, *Social Security Tax Changes for the Self-Employed: Equity Concerns*, 46 TAX NOTES 1063 (1990); Robert J. Myers, *An Analysis of the Historical Changes in the Basis for Social Security Taxes of Self-Employment Income*, 65 TAXES 299, 300 (1987); Gene Steuerle, *Does the Social Security Tax Discriminate Against the Self-Employed?*, 63 TAX NOTES 1205 (1994).

108. As an example of the way in which separating the nominal from the economic burden of the tax empowers the recipient of the nominal burden, consider how much more difficult it would be for employers to shift the economic burden of the social security tax if that tax were raised through a different system. If those funds were raised by levying a tax on the transfer of business assets, or stock in business corporations, for example, employers would find it more difficult to shift the economic burden of the tax to employees. The added difficulty would be a result of the more episodic nature of the tax as well as the decreased linkage between the hiring of employees and an increase in the amount of tax nominally due. While the added difficulty would not prevent employers from shifting the burden to labor, it would probably make the shift less uniform. Indeed, determining the economic incidence of such a tax would pose the same difficulties as determining the incidence of the corporate income tax. See *supra* note 6. One could even argue that an attraction of the current system is that by making the linkage direct, it makes reliable identification of the economic bearer of the tax more likely, so that at least somebody knows who is paying the taxes.

My objective here is not to debate the relative merits of a business transfer tax system over an employment tax system or to suggest that a more episodic tax not tied to the hiring of workers is more desirable than a steady tax that depends directly on the hiring of workers as a mechanism for funding a system of social insurance. My objective is more fundamental: once we examine the ways in which the design of a tax system can confer power and we identify the recipients of that power, we can proceed to debate

visibility for employees, who bear most of the economic burden. Perhaps this is consistent with the system's function as a funding mechanism for compulsory social insurance. Perhaps this represents a decision that the full economic burden is appropriately borne by those who will receive its benefits.¹⁰⁹ Perhaps it also represents the paternalistic judgment that since the program is for labor's own good, its administration through a largely invisible system is expedient, or at least inoffensive. And perhaps all of that is precisely the way it should be. The problem is that whether that is the way it should be will not be debated in full unless the degree to which the system empowers, and the identity of those whom it empowers, are isolated as variables worthy of discussion in their own right.

VI. EMPOWERMENT AND VALUES

Discussion of the ways in which a tax system empowers and the identity of those whom it empowers must itself include consideration of the burdens of empowerment, as well as its benefits. Empowerment is not free. Empowerment is costly both individually and systemically.

A. Individual Costs

Individually, choice is the *sine qua non* of empowerment. Yet, the possession of choice is not always positive. Indeed, it can sometimes be quite burdensome. The relationship between choices and burdens is a curious one and depends on how one views the existence of choice. Choice, like a coin, has two sides. The good side posits that having

whether those who have the power ought to have it and whether alternative systems could raise revenue without conferring the same degree of power on the same individuals. Recognizing that the current system of employment taxation empowers the holders of capital but not the providers of labor proceeds from understanding the ways that tax systems can empower and serves as a springboard for a debate about who should be empowered. It has one additional salutary effect: it brings to the forefront of tax policy analysis the discussion of who bears the economic burden of a tax and of why they do so.

109. In a thoughtful analysis of the federal retirement security system, Professor Graetz concludes that the system is flawed because (1) its taxing structure is regressive, and (2) it does not allow those at the lower ends of the income scale to maintain their standard of living after retirement. Graetz, *supra* note 28. *But see* Altman, *supra* note 38. *See also* Graetz, *Retirement Security and Tax Policy: A Reply*, *supra* note 46. My analysis of the employment tax system corroborates Professor Graetz' conclusion, and I suspect that applying the choice analysis to the other two components of federal retirement policy—the income tax preferences for employer-sponsored pension plans and individual retirement savings—would underscore it. Regrettably (or perhaps, fortunately), such an application and discussion are beyond the scope of this Article.

choices makes people feel powerful and in control of their lives.¹¹⁰ The positive relationship between choice, empowerment, and psychological well-being currently dominates much thinking in psychology and child development.¹¹¹ Choices, we are told, are good. We want them for ourselves and should provide them for our children.¹¹² Choices provide personal autonomy, something we value as a culture and nation. Nevertheless, the power to choose has a dark side as well. The dark side is that the need to make a choice creates the correlative need to acquire information about the available choices and raises the possibility of experiencing feelings of regret that the wrong choice was made.¹¹³ The power to choose, in other words, brings with it responsibility for the choice made.¹¹⁴ Empirical work by psychologists suggests that while

110. See, e.g., JERRY M. BURGER, *DESIRE FOR CONTROL: PERSONALITY, SOCIAL AND CLINICAL PERSPECTIVES* 4-8 (1992); MYLES I. FRIEDMAN & GEORGE H. LACKEY, JR., *THE PSYCHOLOGY OF HUMAN CONTROL: A GENERAL THEORY OF PURPOSEFUL BEHAVIOR* 11 (1991); RALF SCHWARZER, *SELF-EFFICACY: THOUGHT CONTROL OF ACTION* ix (1984); Selma Wasserman, *Louis E. Raths: Theories of Empowerment*, 67 *CHILDHOOD EDUC.* 235 (1991); Shelley Martin & Ralph W. Smith, *OBRA Legislation and Recreational Activities: Enhancing Personal Control in Nursing Homes*, 17 *ACTIVITIES, ADOPTION AND AGING* 1 (1993); Michael D. West & Wendy S. Parent, *Consumer Choice and Empowerment in Supported Employment Services: Issues and Strategies*, 1 *ASS'N PERSONS WITH SEVERE HANDICAPS* 47, 48 (1992); Kenneth W. Thomas & Betty A. Velthouse, *Cognitive Elements of Empowerment: An "Interpretive" Model of Intrinsic Task Motivation*, 15 *ACAD. MGMT. REV.* 66, 67 (1990).

111. See, e.g., Cynthia M. Gibson, *Empowerment Theory and Practice with Adolescents of Color in the Child Welfare System*, 74 *FAM. IN SOC'Y* 387, 389 (1993); see *supra* note 110.

112. See ADELE FABER, *HOW TO TALK SO KIDS WILL LISTEN & LISTEN SO KIDS WILL TALK* 154-55 (1982); ADELE FABER & ELAINE MAZLISH, *LIBERATED PARENTS LIBERATED CHILDREN* 109-10, 183-84, 190-97 (1974).

113. See Meir Dan-Cohen, *Conceptions of Choice and Conceptions of Autonomy*, 102 *ETHICS* 221, 223 (1992); see also *infra* notes 114-16.

114. While it is possible to distinguish an action that reflects the making of a choice from one that reflects a response to a threat, I believe that within the category of propositions that can be classified as choices there are positive choices and negative choices. Nozick distinguishes between threats, which he views as producing coerced offers, and real offers which, in his view, produce free choices. Robert Nozick, *Coercion*, in *PHILOSOPHY, SCIENCE, AND METHOD* (Sidney Morgenbesser et al. eds., 1969). Based on Nozick's work, Mark Kelman has noted that "an offer is any proposition that the ultimate choosing party would choose to receive, whether he accepts it or not, while a threat is any proposition that the choosing party would rather never have heard." Mark Kelman, *Choice and Utility*, 1979 *WIS. L. REV.* 769, 789 (citing Robert Nozick, *Coercion*, in *PHILOSOPHY, SCIENCE, AND METHOD* (Sidney Morgenbesser et al. eds., 1969)). By this definition, the statement "your money or your life," when uttered by a mugger on a deserted street, would be a threat. Yet, the person who is told

people like having choices about relatively unimportant matters, they do not always welcome choices regarding very important, life or death, matters.¹¹⁵ Legal philosophers have also posited that not all choices are welcome.¹¹⁶ Some things we would rather not be responsible for.¹¹⁷

“your money or your life” has been given an option that the person who is killed outright does not have. As long as the option is real—that is, as long as the muggee really does have the option of turning over her wallet or getting shot—the muggee has what I would define as a choice, even though neither of the alternatives from which she can choose is desirable. Indeed, when English liveryman, Thomas Hobson, required his customers “to take the horse which stood nearest the door,” WEBSTER’S THIRD NEW INTERNATIONAL DICTIONARY 1076 (1986), he offered them a choice which they could exercise either by hiring the horse or walking away. However unpleasant the latter option may have been, the choice was there. In other words, I disagree with Nozick that the lack of desirability in the options presented belies the existence of a choice.

115. The importance of the underlying matter seems intuitively relevant to the question of whether a choice is welcome or not. After all, if we measure the “importance” of a matter by the severity of the repercussions that flow from the making of the choice, then the more important the matter under consideration, the greater the potential disparity between post-choice “reality [and] what might have been.” JANET LANDMAN, REGRET: THE PERSISTENCE OF THE POSSIBLE 4 (1993) (citations omitted). But the importance that attaches to a particular matter is not universally dispositive of whether or not a choice is welcome. A matter may be of the highest importance, yet the choice respecting that matter be sorely coveted. In fact, some philosophers have argued that the existence of choice, from a moral perspective, always creates a resolvable conflict. See WALTER SINNOTT-ARMSTRONG, MORAL DILEMMAS 2 (1988). Thus, for those not unduly prone to regret, even the most critical of decisions should be welcome insofar as the decisionmaker can decipher “the one right action.” *Id.* Nevertheless, in MORAL DILEMMAS, Armstrong posits that there are dilemmas which involve symmetrical moral requirements that are irreconcilable. In such cases (he proffers SOPHIE’S CHOICE—see *infra* note 117—as one example), the decisionmaker cannot decipher “the one right action,” nor does such a course exist. Whatever choice is made (including, in some cases, the decision not to make a choice), the decisionmaker necessarily violates a moral requirement because the choice opted for, being morally symmetrical to its counterpart, never was morally “correct.” *Id.* at 54-58. From this perspective, the “importance” of a matter is, as we intuited, relevant to the determination of whether choice is welcome. But, it is not the fact of importance that is dispositive of that question. Life and death matters tend to create unwelcome choices, not because they are important, but because they pose moral dilemmas. That most moral dilemmas involve important matters accounts for the correlation between the latter and the degree of “welcome” that attaches to the exercise of choice. For additional reading on the “moral” component of decisional theory, and on the price of choice generally, see ADAM MORTON, DISASTERS AND DILEMMAS (1991), and compare with GUIDO CALABRESI & PHILIP BOBBITT, TRAGIC CHOICES 88, 177-91 (1978) (using the societal dilemma of how best to allocate donated kidneys among dialysis patients to illustrate how the making of choices may involve collective determinations which are so “highly demoralizing and destructive of basic social values” that the choices themselves must be consciously abandoned).

116. GERALD DWORKIN, THE THEORY AND PRACTICE OF AUTONOMY 62 (1988). In a chapter provocatively entitled, “Is More Choice Better Than Less?” Dworkin argues that both psychic and economic costs are associated with making choices. The economic costs include the opportunity costs of foregoing the option rejected and the costs of acquiring the information necessary to make the choice. The psychic costs include the costs of worrying about the choice and the possibility of experiencing regret over the

choice made. Dworkin also points out that just because some degree of choice might be good, it does not follow that a greater degree of choice would be better. *Id.* at 80. (In the language of economics, choice is an inferior good, not a normal good). Gordon Tullock has also recognized that too much choice might be unwelcome. While he asserts that individuals generally prefer more choice to less choice, he points out that sometimes people will not prefer choice if the range of choices is too large or if the need to make a choice constrains them. He posits the example of college professors who might prefer not to have the option of teaching both summer sessions because if they had the option they might feel financially constrained to exercise it. GORDON TULLOCK, *THE LOGIC OF THE LAW* 15 (1987).

By distinguishing between willing and choosing, Meir Dan-Cohen has also recognized that not all choices are desirable. Dan-Cohen, *supra* note 113, at 223; *see also supra* note 114, *infra* note 117. Dan-Cohen maintains that there is a difference between choosing, which involves exercising a preference for one thing over others in a set, and willing, which involves exercising a preference because something just is. As an example of willing, he posits an individual who goes to a restaurant with the intention of having lobster and points out that such an individual would not look at the menu for the purpose of making a choice but for the purpose of confirming that lobster is on the menu. If that individual is then told that the squab is also good, she will now be made to choose, and in doing so she is likely to experience all of the negative psychic effects that Dworkin has identified. Dan-Cohen, *supra* note 113, at 229.

117. For example, the existence of a choice about what one is to have for dinner at a restaurant is likely to be seen as a benefit because the pleasure of having something one likes outweighs the costs of having to choose: the effort of reading the menu, acquiring information about the composition of particular dishes previously untried, and the possibility of experiencing possible feelings of disappointment at not being able to have more than one thing or at having chosen something that turns out to be less appealing than what a dinner companion chose. Dan-Cohen, *supra* note 113, at 229. (The restaurant menu analogy is based on an example in Meir Dan-Cohen, amplifying discussion *supra* notes 114-16).

By contrast, the choice that Sophie must make in *SOPHIE'S CHOICE*, William Styron, *SOPHIE'S CHOICE* (1979), is not only a choice no one would want because it is a choice between two unspeakably horrifying alternatives, but the mere existence of the choice creates a torment that would not exist if the same events occurred without the opportunity for the exercise of choice at all. The Nazis force Sophie, the principal character in the Styron novel, to relinquish one of her two children when she and the children, a boy and a girl, arrive in Auschwitz. Sophie must choose between her children and she must then attempt to live with that choice. Ultimately, what she cannot cope with is the choice.

This extraordinarily poignant and moving story makes an important point about the consequences of having a choice: even those who might cope with an appalling tragedy may fail to cope with the consequences of having had to make a choice associated with it. The book's central theme is indeed such a choice: the cruelty of forcing Sophie to choose exceeded the cruelty of separating her from her children, and it is the choice that she is eventually unable to live with. The unbearable mental anguish did not stem from the absence of choice, but from precisely the opposite situation—being required to make a choice that required assuming responsibility for its consequences. *See supra* notes 114-16. For a review of *SOPHIE'S CHOICE*, see Michael Kerman, *The Prophetic Outrage of William Styron*, WASH. POST, May 18, 1979, at C1. Styron, who won the 1968 Pulitzer prize for his 1967 novel, *THE CONFESSIONS OF NAT TURNER*, won the 1980

Given that choice is not always good, is the existence of choice regarding the size of one's federal income tax liability good? The answer to that question depends on the value placed on personal autonomy.¹¹⁸ If personal autonomy is valued highly, then the answer will likely be yes. A system that provides opportunities to choose reflects the value that personal autonomy is more important than the time, energy, and money that exercising the choice requires. A system that gives only some of its members the opportunity to choose reflects one of two views: either that those members are more deserving of personal autonomy than others, or that, for certain people, the benefits of personal autonomy do not exceed the costs (*i.e.*, the time, energy, and money expended in exercising choice). Deciding which of these competing views it reflects requires explicit discussion of the role of choice in the design of tax systems. Thus far, tax policy analysis has not embraced that discussion.

To say that tax policy analysis has ignored the role of choice is not to say that it has ignored the existence of taxpayer behavioral response to changes in the tax law. On the contrary, tax policy analysis is very cognizant of that response.¹¹⁹ The ongoing debate about the merits of

American Book Award for SOPHIE'S CHOICE. He has been widely acclaimed as an author.

118. Indeed, Gerald Dworkin cites the relationship between choice and personal autonomy as endowing the existence of choice with the value that it has. In Dworkin's words, "[w]hat does have intrinsic value is not having choices but being recognized as the kind of creature who is capable of making choices. That capacity grounds our idea of what it is to be a person and a moral agent equally worthy of respect by all." DWORKIN, *supra* note 116, at 80. Choices, according to Dworkin, have "constitutive" value, by which he means:

a value that resides neither in the causal effects of making choices nor in the value of choices for their own sake, but as definitive of a larger complex that is itself valued. If one wants to be the kind of person who makes decisions and accepts the responsibility for them, or who chooses and develops a life-plan, then choices are valued not for what they produce nor for what they are in themselves, but as constitutive of a certain ideal of a good life. What makes a life *ours* is that it is shaped by our choices, is selected from alternatives, and therefore choice is valued as a necessary part of a larger complex.

Id. at 80-81.

119. Economists also recognize the importance of behavioral responses and refer to them as elasticities. See JCT PAMPHLET, *supra* note 2, at 25. Thus,

Economists measure the behavioral responses of consumers and producers by calculating the elasticity of demand and the elasticity of supply. The elasticity of demand is the percentage by which the quantity demanded falls if the price paid by consumers rises by one percent. The elasticity of supply is the percentage by which the quantity supplied rises if producers' net receipts per unit rise by one percent. If the elasticity of demand for a good is high relative to its elasticity of supply, most of the incidence of a tax on the good falls upon producers. If the elasticity of supply of a good is high relative to its elasticity

a reduction in the rate of tax on long-term capital gains provides but one example of the importance of taxpayer behavioral response to the formulation of tax policy.¹²⁰ Debates regarding the merits of accelerated depreciation, investment tax credits, and charitable contributions provide a few more.¹²¹ That taxpayers react to the existence of taxes and to changes in the manner in which those taxes are imposed, is accepted as a universal truth. Indeed, it is so well accepted that the only

of demand, most of the incidence of a tax on the good falls upon consumers. *Id.* (Footnotes omitted).

When translated from economese, this means that if consumers respond to price increases by buying less of the good (high elasticity of demand), then producers have to absorb the cost of any tax on the good because, if they don't, they can't sell the good. If consumers don't respond to price increases by buying less of the good (demand is inelastic), then producers can afford to pass the tax on the good onto the consumers, so that consumers end up bearing the economic burden of it. In other words, if they can get away with it, producers will shift the economic burden of a tax to consumers.

120. The extent to which a rise or fall in the capital gains tax rate will alter taxpayer behavior (and incidentally benefit or harm low- and middle-income taxpayers) has been extensively debated. See, e.g., CONGRESSIONAL RESEARCH SERVICE, THE NEUTRAL TAXATION OF CAPITAL GAINS INCOME UNDER THE INDIVIDUAL INCOME TAX, available in Westlaw, 1994 WL 802580; *Colloquium on Capital Gains*, 48 TAX L. REV. 315 (1993); Walter J. Blum, *The Decline and Fall of Capital Gains: 1921-1957*, 28 TAXES 838 (1950), reprinted in Walter J. Blum, *A Handy Summary of the Capital Gains Arguments*, 44 TAX NOTES 1145 (1989); Walter J. Blum, *A Handy Summary of the Capital Gains Arguments*, 35 TAXES 247 (1957), reprinted in Walter J. Blum, *A Handy Summary of Capital Gains Arguments*, 44 TAX NOTES 1145 (1989); Marjorie E. Kornhauser, *The Morality of Money: American Attitudes Toward Wealth and the Income Tax*, 70 IND. L.J. 119, 164-65 (1994); Harold Pepperell, *Should Capital Gains Taxes be Raised?*, 62 TAX NOTES 379 (1994); Janet W. Tillinger & Martha L. Loudder, *Evidence of Taxpayer Behavioral Responses to Higher Tax Rates*, 65 TAX NOTES 361 (1994); Deborah M. Weiss, *Can Capital Tax Policy Be Fair? Stimulating Savings Through Differentiated Tax Rates*, 78 CORNELL L. REV. 206, 246-51 (1993).

121. See Mark A. Hall & John D. Colombo, *The Donative Theory of the Charitable Tax Exemption*, 52 OHIO ST. L.J. 1379 (1991); Zelinsky, *supra* note 8 (discussing the propriety and economic effects of accelerated depreciation and other tax incentives); Charles T. Clotfelter, *Tax-Induced Distortions in the Voluntary Sector*, 39 CASE W. RES. L. REV. 663 (1988-89). For commentary on the investment tax credit in particular, see Stephen R. Corrick & Martin A. Sullivan, *An Incremental Investment Tax Credit: Can It Deliver on its Promise?*, 58 TAX NOTES 209 (1993); Jane G. Gravelle, *What Can Private Investment Incentives Accomplish? The Case of the Investment Tax Credit*, 46 NAT'L TAX J. 275 (1993); Richard P. Roling, *Investment Tax Credits and the 'Human Experience': Why Not Fairness Rather than Pain?*, 58 TAX NOTES 789 (1993); Gene Steuerle, *The Failure of Investment Incentives*, 44 TAX NOTES 821 (1989). For an analysis of taxpayer behavioral response to the exclusion of imputed rent, and the deductibility of property taxes and home mortgage interest payments, see Harvey S. Rosen & Kenneth T. Rosen, *Federal Taxes and Homeownership: Evidence from Time Series*, 88 J. POL. ECON. 59 (1980).

controversial question that remains is the extent to which taxpayer behavioral responses ought to be quantified and taken into account in estimating both the distribution of the tax burden and the likely amount of revenue a given change will raise or lose.¹²² Even there, the debate is not about the existence of taxpayer behavioral response. Instead, it is about the likely form of that response and economists' ability to quantify it.¹²³

The traditional view of taxpayer behavioral response neglects to consider the benefits that accrue to taxpayers simply from the enactment of provisions that permit the exercise of choice. One positive aspect of choice is that it makes the system visible. Another is that it makes the individual who exercises the choice the arbiter of his or her own tax liability. The provision of choice, by making the system visible and empowering the individual to react to it, reinforces the value of personal autonomy.

Once the existence of a choice is identified, tax policy should determine if the choice is available on equal terms to all who are affected by the system. Although a focus on choice alone cannot answer the question whether the choice should be available to different people in different degrees, it can move the debate toward a discussion of values and away from a dependence on the seductive effect of tables and formulae. One of those values is personal autonomy; another is egalitarianism. If, for example, the analysis reveals that the ability to choose is reserved for those who hold material wealth, the value of ownership of capital is implicated. If that value is high, then increasing the benefits of such ownership is a good thing.¹²⁴

An explicit discussion of the role of choice, and the power it confers, will ensure that a discussion of values becomes an explicit part of the consideration of tax policy. It will ensure that considerations of visibility and privatization, and the values they reflect, receive deliberate attention from policymakers. A tax system, like any system of laws adopted by a society, reflects the values held by that society. Discussion of those values should be open and explicit, unobscured by a veil of numbers. Failure to engage in that discussion produces a situation in

122. See *supra* note 26 for additional discussion of the debate over dynamic scoring.

123. See *supra* note 26.

124. Perhaps some portions of this analysis might change if the income tax system treated human capital as it does other capital. That prospect, however, is unlikely. Despite a strong theoretical argument for equalizing the treatment of human and non-human capital, such equalization is, at present, only a pipe dream. For a recent and penetrating analysis of the ideal treatment of human capital under the income tax, see Louis Kaplow, *Human Capital Under an Ideal Income Tax*, 80 VA. L. REV. 1477 (1994).

which some, but not all, are empowered, and those who are not empowered are the victims of invisible taxes imposed by invisible actors, sanctioned by a paternalistic government.

B. Systemic Costs

On the systemic level, as on the individual level, empowerment is not free. On the contrary, empowerment costs the system in at least four ways. First, empowerment leads to complexity. If a system is going to empower by providing choices, it must provide for the consequences of exercising each possible choice. Such a system will necessarily be more complicated than one that only sets forth one set of rules.¹²⁵ In addition, a system that empowers only a subset of its members will be complicated because it will need to provide rules for determining who falls within the preferred subset. The emerging proliferation of anti-abuse rules¹²⁶ as well as the amount of discussion their very existence has generated, eloquently testifies to the complexity spawned by the need to determine who is entitled to what treatment.¹²⁷

125. If the employment tax system did not distinguish between employees and independent contractors, but instead imposed a tax on income derived from the provision of personal services, for instance, the need to distinguish between employees and independent contractors, and the attendant need for the Internal Revenue Service to provide standards for making the distinction and policing its application, would disappear, as would the need for two sets of compliance and penalty provisions. *See, e.g.*, I.R.C. §§ 3509, 6651(a)(1), 6653(a), 6672 (West 1995) (compliance and penalty provisions applicable in the employer/employee context); I.R.C. §§ 7202, 7204, 7215, 7205 (West 1995) (compliance and penalty provisions applicable in the independent contractor context). *Of course, I am not suggesting that there is no justification for the distinction; justifications exist, but making the distinction carries a price.*

126. *See, e.g.*, Treas. Reg. §§ 1.881-0, 1.881-3, 1.881-4, 1.7701(l)-1 (1994) (and amendments to Treas. Reg. §§ 1.871-1, 1.1441-3, 1.1441-7, and 1.6038A-3). The so-called conduit financing regulations were published in the Federal Register on October 14, 1994 pursuant to the authority granted in section 7701(l) to publish regulations "recharacterizing any multiple-party financing transaction as a transaction directly among any 2 or more parties where the Secretary determines that such recharacterization is appropriate to prevent avoidance of any tax imposed by this title." I.R.C. § 7701(l) (West 1995). These regulations can be expected to apply in the international arena to § 956 transactions as well as to foreign sales corporations. *See John Turro, Culbertson Briefs Florida Bar on International Developments*, January 20, 1995, available in LEXIS, 95 TNT 13-10. The partnership anti-abuse regulations provide yet another example. *See infra* note 128.

127. The tide toward complexity may have begun to turn. The Service's proposal to adopt a check-the-box classification system for unincorporated entities both suggests that and supports the notion that complexity is borne in large part, of the need to

Second, unless a system empowers all people equally, it will necessarily discriminate. Discrimination usually leads to dissatisfaction on the part of those discriminated against, at least to the extent that those discriminated against value personal autonomy and empowerment. That the distinctions are deliberate and justifiable does not mitigate the consequences of making them in the first place. For example, under the current federal income tax system, taxpayers who are contemplating alternative structures for a transaction motivated by bona fide business objectives have a range of choices that taxpayers who are not so motivated do not have. Even if discrimination between those two types of taxpayers is both deliberate and defensible, taxpayers who are denied the opportunity to exercise choice resent the denial and argue vociferously against it, as the recent debate over the partnership anti-abuse regulations has shown.¹²⁸

A system may also discriminate if it is designed to encourage certain types of behavior that are only possible for certain segments of the population. For example, a system that reduces the rate of tax on certain types of savings is often touted as providing an incentive for savings. Under such a system, people who do not need to consume all that they produce have a choice. They can choose to consume, and face a higher tax burden, or save, and face a lower tax burden. But such a system does not provide any choice for those who must consume all they make. Such a system discriminates in favor of those who produce more than they need to consume because it gives them the power to act in ways that will reduce their federal income tax liability. But it denies that

classify. See *infra* note 136.

128. The proposed adoption of the partnership anti-abuse regulations led to a lively exchange between proponents and opponents. See, e.g., Robert J. Wells et al., *Subchapter K Antiabuse Reg Sparks Heated Reactions*, 63 TAX NOTES 933 (1994); Lee A. Sheppard, *Partnerships, Consolidated Returns, and Cognitive Dissonance*, 63 TAX NOTES 936 (1994); *The Grass Roots Speak on Antiabuse Reg*, 63 TAX NOTES 1369 (1994) (letter to editor from Schuyler M. Moore); Kip Dellinger, *Further Reflections on Antiabuse Reg*, 63 TAX NOTES 1646 (1994); *Don't Prejudge ABA Comments on Antiabuse Reg, Urges Egerton*, 63 TAX NOTES 1645 (1994) (letter to editor from Charles H. Egerton); Kip Dellinger, *The Internal Revenue Service's Power Grab*, 63 TAX NOTES 1773 (1994); Sheldon I. Banoff, *Proposed Antiabuse Reg is 'Fatally Flawed'*, 64 TAX NOTES 125 (1994); Lawrence M. Stone, *Proposed Antiabuse Reg will Create Uncertainty But Accomplish Little Else*, 64 TAX NOTES 127 (1994); *Report on the Proposed Partnership Antiabuse Rule by the New York State Bar Association Tax Section*, 64 TAX NOTES 233 (1994); Joseph Bankman, *The Proposed Partnership Antiabuse Rule: Appropriate Response to Serious Problem*, 64 TAX NOTES 270 (1994); Daniel I. Halperin, *The Partnership Antiabuse Reg: A Reasonable Step in the Right Direction*, 64 TAX NOTES 823 (1994); *Eliminate the Proposed Partnership Antiabuse Rule's Tax Avoidance Test*, 64 TAX NOTES 969 (1994) (letter from Benjamin J. Cohen to the IRS); *It's Important to Pave the Way for Antiabuse Rules*, 64 TAX NOTES 1237 (1994) (letter from Peter L. Faber to the IRS).

power to those who must consume all that they produce. Such a system empowers. However, since the system empowers only some of those to whom it applies, those whom it does not empower may resent it, especially if the discrimination is visible. For those who value personal autonomy, the resentment flows from the absence of power.

Third, a system that empowers places on those subject to it the burden of obtaining the information necessary to permit the exercise of choice. Under such a system, not only must a person acquire information sufficient to ascertain whether she is a member of the class of people who have been given a choice, but, if she is, she must then acquire information about the nature of the choice, so that she can make it. The need to acquire this information will require individuals to allocate resources to the information-gathering process and will thus burden them.¹²⁹ To the extent that those resources would otherwise have been employed elsewhere, their allocation to information-gathering also distorts the economy and is therefore inefficient.

Fourth, a system that provides opportunities to exercise choice and that is therefore discriminatory and burdensome is necessarily more expensive to administer than one that makes few distinctions and provides little opportunity to choose.¹³⁰ Not only does a choice-laden system require more people to administer it because it has a greater number of provisions, spawned by the need to provide for the consequences of various alternatives, but the need to distinguish between those entitled to make choices and those not so entitled requires personnel to police and enforce those distinctions. A comparison of the federal income and employment tax systems again illustrates these points.

129. See Hal Gann & Roy Strowd, *Reducing the Mounting Tax Compliance Burden*, 66 TAX NOTES 427 (1995); Arthur P. Hall, *The Cost of Unstable Tax Laws*, 65 TAX NOTES 759 (1994) (examining a byproduct of taxpayer choice: the constant revision of federal tax laws in response to taxpayer abuse of choice); Arthur P. Hall, *The High Cost of Tax Compliance*, 63 TAX NOTES 887 (1994); Joel Slemrod & Nikki Sorum, *The Compliance Cost of the U.S. Individual Income Tax System*, 37 NAT'L TAX J. 461 (1984).

130. While the costs of administration could be seen as a subset of complexity, I have chosen to treat it separately because the burden of administration falls exclusively on the government and therefore seems qualitatively different from the burden of statutory complexity that falls on taxpayers as well as on the government. For a look at the administrative burden borne by government, see Hal Gann & Roy Strowd, *The Enormous Complexity of Being Fair*, 66 TAX NOTES 1711 (1995); Arthur P. Hall, *Growth of Federal Government Tax 'Industry' Parallels Growth of Tax Code*, 65 TAX NOTES 1133 (1994).

The federal income tax system, unlike the employment tax system, provides many opportunities for the exercise of choice. Some of those opportunities are explicit. The election to expense certain depreciable property,¹³¹ the election out of installment reporting,¹³² the election to recognize income upon receipt of restricted property,¹³³ the election to treat an acquisition of stock as an acquisition of assets,¹³⁴ and the many elections with respect to distributions from qualified retirement plans¹³⁵ provide but a few examples. Many more are implicit. Taxpayers may structure their business activities in a variety of different entities, each with differing tax consequences.¹³⁶ They can choose whether and when to realize gains and losses. They can also structure certain types of transactions so as to qualify for non-recognition treatment. This multiplicity of choices is not without significant costs. Unquestionably, the profusion of choices available under the federal income tax system carries a high price.

Much of the high price of choice stems from the resulting complexity. The federal income tax system is extraordinarily complex. The multitude of implicit and explicit choices that the system provides has spawned an entire industry composed of very highly educated people who spend their time mastering the choices available and who make their living advising taxpayers on the consequences and desirability of making one choice over another. I am not talking about compliance here—that is, about the difficulty of deciphering the requirements of the forms upon which the results of the year's activity must be reported. Rather, I am talking about planning. I am talking about the legion of lawyers, accountants and related secretaries, paraprofessionals, and other auxiliary personnel that help taxpayers exercise the powers that the system has given them. Most taxpayers would not even know the range

131. I.R.C. § 179(a) (West 1995).

132. I.R.C. § 453(d) (West 1995).

133. I.R.C. § 83(b) (West 1995).

134. I.R.C. § 338 (West 1995).

135. See I.R.C. § 402 (West 1995) (a mind-numbing range of choices for the taxation of distributions from qualified plans, the consequences of which depend on the taxpayer's choosing to elect to receive a lump-sum distribution or to effect a rollover of some of the distribution into an individual retirement account or similar plan).

136. Recently proposed regulations would allow unincorporated organizations to elect whether to be taxed as a partnership or as an organization taxable as a corporation. Prop. Reg. § 301.7701-1, PS-43-95, May 9, 1996, reprinted in 96 TNT 93-1 (May 10, 1996). See also I.R.S. Notice 95-14, 1995-14 I.R.B.; I.R.S. News Release IR-25-29 (Mar. 29, 1995). For commentary on the proposal to issue the regulations, see Daniel Shefter, *Check the Box Partnership Classification: A Legitimate Exercise in Tax Simplification*, 67 TAX NOTES 279 (1995). See also Sheryl Stratton, *IRS Imposes "Check the Box" Partnership Classification Procedures*, TAX NOTES TODAY (Mar. 30, 1995), available in Lexis, 95 TNT 62-3.

of available choices without these professionals, and many transactions require the services of not only one, but many of these individuals and their attendants. The reason so many individuals are required is that the system has become so complex that no one individual can possibly master the details of all of the alternative consequences that can flow from a given decision.¹³⁷ The number of if-then decision trees for any given transaction can boggle even the most remarkable of minds.¹³⁸ Eliminating choices would inexorably lead to an elimination of the if-then decision trees that somebody must draft and that somebody else must master and explain to a client. Eliminating choices would also render moot all of the rules that determine who can choose and that seek to prevent the abuse of choice. However, eliminating choices might also make the system much less visible, as individuals would not need to grapple with its existence in order to avail themselves of the choices it provides.

The existence of choices, the visibility they bring to the system, and the opportunity for the exercise of power that choices confer is largely responsible for the current complexity of the federal income tax system.

137. For a delightful and prescient account of the increasing complexity of the Code, see Robert Hellawell, *A Tax Fable*, 26 TAX L. REV. 659 (1971). Writing an allegorical account of the development of the tax law as it might look from the vantage point of the year 2020, Hellawell fancifully recounts how:

In 1995 the income tax provisions [of the Code] alone ran 100,000 pages, divided into almost 5,000 sections. While the sheer bulk of these provisions is impressive, it is the intricate, nearly impenetrable complications of the individual sections that were the hallmark of this Code. Practitioners took months or years to master the complexities of a single section. As a result most sections, a great many subsections, and not a few paragraphs had their corps of full-time practitioners, a nationwide organization and one or more monthly periodicals. There were still some generalists, however; many of you knew them and remember them fondly. Their knowledge of three or even four Code sections was remarkable.

Id. For another similarly witty commentary on the complexity of the tax law, see Walter J. Blum & James P. Johnson, *1913-2013: A Hundred Years of Income Taxation*, 33 TAXES 41 (1955).

138. Learned Hand once complained that:

In my own case the words of such an act as the Income Tax, for example, merely dance before my eyes in a meaningless procession: cross-reference to cross-reference, exception upon exception—couched in abstract terms that offer no handle to seize hold of—leave in my mind only a confused sense of some vitally important, but successfully concealed, purport, which it is my duty to extract, but which is within my power, if at all, only after the most inordinate expenditure of time.

LEARNED HAND, *THE SPIRIT OF LIBERTY* 213 (1952).

Talk of simplifying the system is cheap and in some quarters abundant, but a simple income tax system continues to elude us. Why? One reason, I believe, is the value we place on personal autonomy and the opportunity to exercise choice.¹³⁹ The price of simplicity is the abrogation of choice, and that is a price which we have thus far been unwilling to pay.¹⁴⁰

While some commentators have attributed the complexity of the current federal income tax system to the complexity of the present economy and the system's need to reflect the reality of complex economic transactions,¹⁴¹ I disagree. Complex economic transactions

139. The average American seems to be fully aware of this. A Wall Street Journal/NBC NEWS poll revealed a nearly even split between respondents' desire to have a tax system that touted lower rates but allowed for no deductions (translation: little opportunity for the exercise of taxpayer choice) over one that provided higher rates but retained the deductions most commonly used by individuals, the charitable contribution and home mortgage interest deductions (translation: more opportunity for the exercise of taxpayer choice). David Wessel, *What Should Be Taxed Will Be the Key Issue*, WALL ST. J., May 1, 1995, at A1.

140. At least some politicians acknowledge this. Robert Packwood, then Chairman of the Senate Finance Committee, acknowledged the difficulty of producing a tax system that applies a flat rate to a broad base devoid of many deductions and therefore devoid of much opportunity for the exercise of taxpayer choice, noting the psychic satisfaction that taxpayers receive from deductions. *Demise of Balanced Budget Amendment Will Lead to Tax Code 'Tinkering,' Packwood Predicts*, TAX NOTES TODAY (Mar. 3, 1995), available in Lexis, 95 TNT 43-3.

141. I do not, of course, attribute to all commentators the view that tax system complexity flows inexorably from the complexity of our current economic system. Many other reasons for the current complexity of the internal revenue code have been proffered. Among these are: (1) the desire of drafters to carry out Congressional substantive policy directives, (2) Congressional efforts to conform Code provisions to our evolving conception of economic income, (3) the desire of Congress to make the tax system fair by first, accounting for differences among taxpayers when designing Code provisions and, second, by constantly revising those provisions in response to evolving tax avoidance techniques, and even (4) the perpetuation of complexity by those players in the tax arena who benefit from it, namely the IRS (by virtue of enhanced revenue), the tax bar (by virtue of more clients and higher billing), and members of Congress (by virtue of increased patronage on the part of those taxpayers either fearful of, or seeking, changes in the prevailing legislative or judicial slant on existing law). For a closer look at these theories and at the issue of tax complexity generally, see DAVID F. BRADFORD, *UNTANGLING THE INCOME TAX* (1986); Michael A. Andrews, *Tax Simplification*, 47 SMU L. REV. 37 (1993); Edward J. McCaffery, *The Holy Grail of Tax Simplification*, 1990 WIS. L. REV. 1267; Charles E. McClure, Jr., *The Budget Process and Tax Simplification/Complication*, 45 TAX L. REV. 25 (1989); John A. Miller, *Indeterminacy, Complexity, and Fairness: Justifying Rule Simplification in the Law of Taxation*, 68 WASH. L. REV. 1 (1993); Malcolm L. Morris, *Determining Deductions Deserves Deductibility*, 21 FLA. ST. U. L. REV. 75 (1993); Sheldon D. Pollack, *Tax Complexity, Reform, and the Illusions of Tax Simplification*, 2 GEO. MASON INDEP. L. REV. 319 (1994); Lee A. Sheppard, *Is the Income Tax System Becoming Compliance Proof?*, 41 TAX NOTES 1010 (1988); Karla W. Simon, *Tax Simplification and Justice*, 36 TAX NOTES 93 (1987); Michelle J. White, *Why Are Taxes So Complex and Who Benefits?*, 47 TAX NOTES 341 (1990); Patricia D. White, *Realization, Recognition, Reconciliation*,

could be subject to a simple tax system if we were willing to deny those who engage in them the opportunity to alter their tax liability by changing the structure of the transaction.¹⁴² In short, complex economic transactions could be subject to a simpler tax if we were willing to accept that the tax system does not have to reflect precisely the choices available to people in the economy.¹⁴³ The more the system tries precisely to reflect economic reality and the choices that reality provides, the more it needs to differentiate between the treatment of various transactions. The more choices the system provides in its attempt to mirror the choices provided by the economy, the more complex it will necessarily become.¹⁴⁴

The enactment of a tax system that seeks to reflect economic reality is itself a choice and the product of our values. It reflects the value of personal autonomy and the triumph of individualism over communalism. It also reflects an acceptance of the prevailing economic order. Under that order, money (capital) is power and those with money have more power than those without. The federal income tax system reflects that order by giving those with capital the power to make choices that those

Rationality and the Structure of the Federal Income Tax System, 88 MICH. L. REV. 2034 (1990); Edward A. Zelinsky, *Another Look at Tax Law Simplicity*, 47 TAX NOTES 1225 (1990).

142. The check the box approach to entity classification proposed by the Internal Revenue Service provides an illustration of how this can occur. *See supra* note 136. By uncoupling substantive reality from tax treatment, the system becomes simpler because all of the provisions designed to make the tax classification follow the substantive classification can be eliminated, and with them, the need to master them, administer them, and prevent their opportunistic use. The social security tax system, which is imposed on a relationship that is quite economically complex—the employment relationship—provides another example of how simple taxes can apply to complex transactions.

143. *But see* Gann & Strowd, *supra* note 130 (complexity results from an attempt to achieve fairness through precision in the measurement of tax liability).

144. Senator Russell Long alluded to this relationship between complexity and the desire for the accurate reflection of taxpayer's actions when he quipped: "The complexity of our [C]ode in the main is not there because of some mischief. Most of it is there in the effort to do more perfect justice." *Tax Reform Proposals—III: Hearing Before The Senate Committee on Finance*, 99th Cong., 1st Sess. 53 (testimony by Senator Russell B. Long). For other explanations of the increasing complexity of the federal income tax system, see Pollack, *supra* note 141; McLure, Jr., *supra* note 141 at 25; Richard L. Doernberg & Fred S. McChesney, *On the Accelerating Rate and Decreasing Durability of Tax Reform*, 71 MINN. L. REV. 913 (1987); Roundtable Discussion, *The Uncertain Potential of Tax Simplification*, 79 CCH STANDARD FEDERAL TAX REPORTS No. 46, Pt. 2 (Sept. 23, 1992).

without capital simply do not have. For example, those with capital can choose whether or not to incur tax liability by choosing to realize gains. The choice does not diminish their wealth, except for the payment of taxes. By contrast, those without capital (or with mostly human capital) cannot make a choice that affects only their tax liability. To avoid the tax liability, they have to forgo the material wealth as well. In addition, a large percentage of their total tax burden is imposed by a tax system that provides little opportunity to exercise choice, is highly invisible, and whose burden is proximately imposed by extra-governmental actors.¹⁴⁵

That the ownership of capital carries with it the power to make choices that its absence denies reflects the existing economic order. That order discriminates. It makes distinctions that leave some people happy with it and others not. By having a tax system that reflects that order, we perpetuate and perhaps exacerbate those distinctions and resentments.¹⁴⁶ We do not redistribute, we reinforce.¹⁴⁷

C. Progressivity and Values

An individual's view of the appropriate distribution of tax burdens reflects her values. One who advocates steeply progressive taxation in the traditional sense probably values the egalitarian distribution of wealth more highly than its retention by those to whom the market distributes it.¹⁴⁸ Such a person probably thinks that market forces alone should

145. See *supra* part IV.D.

146. Redistributing income would, of course, create other distinctions and resentments, but those would be consistent with the objectives of progressive taxation. The problem is not that the system creates distinctions and resentments, but that it creates distinctions and resentments in the people for whose benefit it is at least apparently designed.

147. Joseph Pechman's work supports the foregoing analysis. Pechman analyzed income and tax data from 1952 to 1986, and concluded:

The market distribution of income in the United States has become more unequal over the past three decades, particularly since 1981. Thus, the share of society's product accruing to the top 15 percent of families has increased steadily over this period. [Also,] [t]he federal income tax of the United States is only mildly progressive and has not moderated income inequality to a significant degree.

JOSEPH A. PECHMAN, *The Rich, The Poor, and the Taxes They Pay*, in *TAX REFORM, THE RICH AND THE POOR* 26-27 (1989).

148. Professor Marjorie Kornhauser has argued persuasively that progressivity is consistent with feminist values because a progressive tax structure connects people by causing them to help one another, whether they like it or not. Professor Kornhauser sees progressivity as representing a world view that is in sharp contrast to the atomistic, individualistic view which is more typical of the way men think. Kornhauser, *supra* note 11. For a similar analysis in the context of contract law, see Jean Braucher, *Contract Versus Contractarianism: The Regulatory Role of Contract Law*, 47 *WASH. & LEE L. REV.* 697 (1990).

not determine the distribution of wealth and values the contribution to the common good more highly than the retention of privately generated wealth. Conversely, one who advocates proportional (or frankly regressive) taxation probably values the retention of wealth in accordance with market distribution more highly than the redistribution of some wealth to others in derogation of market forces. Such a person would likely value precisely what the market values and would see no reason for a distribution of burdens in accordance with anything other than market forces.

The debate over progressive versus proportional taxation, as traditionally framed, thus implicates views regarding the operation of the market and the distribution of privately-generated wealth. That values regarding wealth should be at the core of the traditional debate over progressivity follows logically from the way in which progressivity analysis has traditionally been framed. Since the analysis focuses on the burden of taxation, it follows that views about the object of that burden—wealth—should be at the core of the analysis.

Adding a discussion of benefits to the existing discussion of burdens would introduce additional values to the progressivity debate. Primary among these values would be that of personal autonomy. Conceptually, one may examine the value of personal autonomy separately from the value of wealth or income. The degree of personal autonomy enjoyed under a given tax system need not depend on the amount of wealth held. It can depend on the visibility of the system, the number of choices provided, and the ability to identify the source of the imposition of the tax burden. A tax system that correlates wealth with personal autonomy is the product of the value placed upon wealth, not of some unavoidable linkage.

The distribution of the powers conferred by a system of taxation thus provides a window into the relationship between wealth and personal autonomy and reveals much about the values of those who designed the system. In the case of the federal income tax system, such an examination reveals that, despite the claims to progressivity made by both its supporters and its detractors, progressivity in the distribution of burdens is offset by such progressivity in the distribution of powers, that the system as a whole amounts to a ringing endorsement of the value of wealth and the linkage of wealth to personal autonomy. In the case of the social security tax system, such an examination reveals the same

constellation of values, expressed in that context by the dual mechanisms of invisibility and privatization.

It is, of course, generally true that in a capitalist society wealth brings power and that one of those powers is the power to choose.¹⁴⁹ Analyzing the role of choice in the federal income tax system reveals that the very system that is both touted and reviled as the antithesis of the linkage between wealth and power (at least to the extent that it appears designed to distribute its burdens progressively, taking more from those who have more), actually serves to reinforce that link.¹⁵⁰

Not only does the extensive provision of choice in the federal income tax system reinforce the relationship between wealth and power and apparently contradict the redistributive objective of progressive taxation, but the existence of choice yields a system in which the identities of the specific bearers of the tax burden often remain hidden from common

149. Many social programs reflect this truism. Consider, for example, federal means-tested entitlement programs. The top five such programs (in terms of revenue outlays) are Medicaid, Aid for Families with Dependent Children (AFDC), Supplemental Security Income (SSI), the Food Stamp Program, and the Earned Income Tax Credit (EITC). CONGRESSIONAL BUDGET OFFICE, *REDUCING ENTITLEMENT SPENDING 2 & n.2* (1994). Federal government outlays on these programs totaled \$147 billion in 1993, but only \$46 billion was provided directly to recipients in the form of cash assistance. *Id.* at 3 (AFDC, SSI, and EITC being the sources of cash assistance). Medicaid and the Food Stamp Program (providing hospital services and food coupons, respectively) account for the most in-kind assistance. HOUSE COMMITTEE ON WAYS AND MEANS, *1994 GREEN BOOK: OVERVIEW OF ENTITLEMENT PROGRAMS*; BUREAU OF THE CENSUS, U.S. DEP'T OF COMMERCE, *1994 STATISTICAL ABSTRACT OF THE UNITED STATES* 373 (Medicaid outlays in 1992 came to \$68 billion, \$20 billion more than all federal cash outlays to the poor combined). By providing assistance primarily in the form of in-kind benefits, the federal government deprives recipients of the ability to exercise a wide range of choices. Thus, for example, a food stamp recipient cannot choose to redeem his coupons for cigarettes (rather than bread) even if he would have opted for cigarettes had he been given the choice. While the Food Stamp Program clearly provides recipients more opportunity for the exercise of choice than a program of direct distribution of food (such as that utilized to aid refugees), it provides significantly less opportunity for the exercise of choice than a system of direct cash grants.

150. This observation will come as no surprise to students of the critical legal studies movement, which has long maintained as one of its principal tenets that law reflects the hierarchies and values that inhere in the social organization in which it operates. Roberto M. Unger, *The Critical Legal Studies Movement*, 96 HARV. L. REV. 563, 563 n.1 (1983); see Duncan Kennedy, *The Structure of Blackstone's Commentaries*, 28 BUFF. L. REV. 205 (1979). Professor Unger acknowledges that others have criticized this thesis by pointing out that institutions often lack the cohesiveness that such a theory ascribes to them. See generally *THE POLITICS OF LAW* (David Kayries ed., rev. ed. 1990). For a fascinating account of how legal thinking has evolved to allow explicit linkage of the concepts of politics and law, see MORTON J. HORWITZ, *THE TRANSFORMATION OF AMERICAN LAW 1870-1960: THE CRISIS OF LEGAL ORTHODOXY* (1992).

view.¹⁵¹ Taxpayers behave, not as a body in pursuit of the shared objectives that are supposed to animate the system (tax policy), but as atomistic actors faced with myriad iterations of the prisoner's dilemma.¹⁵² The picture that emerges is not one in which the progressivity

151. See discussion of visibility, *supra* part IV.C. Invisibility undercuts the value of private property because it can allow the government to take more of an individual's property than might otherwise occur—if an individual cannot identify that the property is being taken, she cannot act to prevent the taking. Individuals at the bottom of the income scale are often subject to a greater burden and concomitant reduction in the value of their property because they have less choice and their taxes are less visible. See *supra* note 92 and accompanying text.

152. John Rawls has pointed out that a situation in which there are many choices is like a generalized prisoner's dilemma in that people acting in isolation and making choices that will affect what happens to them, as well as what happens to others, might make choices that, while rational on an individual basis, might not be good from the point of view of the whole. JOHN RAWLS, A THEORY OF JUSTICE 265-74 (1971). As Rawls has written,

The [problem of isolation] arises whenever the outcome of the many individuals' decisions made in isolation is worse for everyone than some other course of action, even though, taking the conduct of the others as given, each person's decision is perfectly rational. This is simply the general case of the prisoner's dilemma of which Hobbes' state of nature is the classical example.

The isolation problem is to identify these situations and to ascertain the binding collective undertaking that would be best from the standpoint of all.

Id. at 269-70. While I am not suggesting that individuals behave in a way that is as disconnected or unidimensional as that which Michael Sandel has alleged would be required to produce Rawlsian justice, I do nevertheless agree with Rawls' observation that when everyone must make choices in isolation, it is impossible for them to act for the common good. Cf. MICHAEL J. SANDEL, LIBERALISM AND THE LIMITS OF JUSTICE 122-32 (1982). The irony of the federal income tax system is that the very existence of the system represents an attempt to address the isolation problem since the system seeks to provide a mechanism for a "collective undertaking" that should redound to the benefit of society, and the provision of significant opportunity for the exercise of isolated choice undermines that objective. In Nozick's terms, the provision of significant choice means that the egalitarian objective of the system "is overturnable by the voluntary actions of individual persons over time." NOZICK, *supra* note 1, at 164.

Professor Roin has used public choice theory to reach a similar conclusion with respect to the effectiveness of the Congressional use of tax incentives. Julie Roin, *United They Stand, Divided They Fall: Public Choice Theory and the Tax Code*, 74 CORNELL L. REV. 62 (1988). Professor Roin argues persuasively that taxpayers' inability to work together over time operates as a curb on the abuse of the benefits provided by the Code. For a robust critique of public choice theory in general and of its use to explain tax legislation in particular, see Daniel Shaviro, *Beyond Public Choice and Public Interest: A Study of the Legislative Process as Illustrated by Tax Legislation in the 1980's*, 139 U. PA. L. REV. 1, 76-111 (1990).

of a system suggests communalism, but one in which the pursuit of individual objectives reigns supreme.¹⁵³

A progressive system suggests caring and connectedness. By asking for contributions in proportion to ability to pay, a progressive tax system treats taxpayers as members of a cooperative in which those who have skills that the market values highly contribute more to the common good for the benefit of those who have less highly valued skills.¹⁵⁴ A visible, progressive system that provides little opportunity for the exercise of individual choice regarding whether to make a contribution ensures that both the fact of the contribution and its amount result from a collective, collaborative process. The absence of choice ensures that the voluntary actions of individual persons do not overturn the egalitarian design of the system.¹⁵⁵

By contrast, an apparently progressive system that also gives those with more ability to pay more ability to choose whether or not to pay contains, in the provision of choice, the seeds of destruction of its egalitarian objective. Such a system places individual choice above the egalitarian objective of redistribution and by doing so plants the seeds

153. Perhaps it should not be surprising that a system designed principally by males reflects what Professor Kornhauser has classified as typically male values. Kornhauser, *supra* note 11; *see also supra* note 148. Interestingly, recent empirical work supports Professor Kornhauser's thesis. *See Roberts & Hite, supra* note 45, at 36-37. Professor Kornhauser's view of the values advanced by the progressive distribution of tax burdens echoes Robert Nozick. Nozick attacks the Rawlsian difference principle, whereby those who benefit from superior endowments can behave justly by using those endowments for the good of others less endowed, a view that supports the notion of the progressive distribution of tax burdens. Nozick asserts that adherence to the difference principle would lead to an imposition on society as a whole the type of "loving relationships" found within families, a result he pronounces inappropriate because the relationships within members of the broader society lack the voluntary nature of familial relationships. NOZICK, *supra* note 1, at 167-74. Indeed, Nozick disapproves of the redistributive implications of the difference principle even within the context of families. *Id.* at 167. Nozick's opposition to redistribution stems at least partly from what he views as the denial of even the opportunity to exercise choice by patterned systems of distributive justice. *Id.* Nozick's focus on disconnected, individualistic action is diametrically opposed to Rawls'. Whereas Rawls implores the state to solve the isolation problem, Nozick decries the state's efforts to establish patterns of redistribution. Ironically, Nozick disagrees with Rawls at least in part because he views Rawlsian theory as diminishing the role of individual choice, while Sandel disagrees with Rawls because he believes the Rawlsian model requires that individuals possess more opportunity for the atomistic exercise of choice than he thinks individuals actually have. SANDEL, *supra* note 152, at 122-32. Fortunately, accepting the thesis of this Article does not require a resolution of this debate. The thesis of this Article is only that the existence of choice is relevant to the degree of progressivity a system has. How much progressivity a system should have, and even whether it should have any at all, is the subject of the Rawls-Nozick-Sandel debate.

154. *See supra* note 148.

155. *See NOZICK, supra* note 1, at 164.

of destruction of the latter. In addition, by making the choice an individual matter, such a system makes the decision as to whether or not to contribute an individual, not a collective, one. As in the classic prisoner's dilemma, the exercise of choice by each person independently of the others can result in a situation in which the choosers are worse off by acting independently than they would have been if they had acted cooperatively.¹⁵⁶ Providing choice in proportion to wealth thus turns a seemingly progressive system into one in which the outward appearance of progressivity can be overturned by the voluntary actions of individual persons over time and in which the connectedness wrought by the objective of progressivity is undercut by the disconnected manner in which each choice is exercised.¹⁵⁷ Moreover, because bestowing the power to choose in proportion to wealth is itself anti-egalitarian, possession of the power can overturn the egalitarian objective even if the power is not used. A tax system that either removes the opportunity for the exercise of taxpayer choice or distributes that opportunity pursuant to some criterion other than economic wealth can reflect values in addition, or in opposition, to those of the market, thus resembling a cooperative rather than a feudal estate.¹⁵⁸

D. *The Value of Choice*

The federal income tax system requires taxpayers to pay the price of obtaining the information necessary to learn about that system, to exercise the choices it provides, and to maintain a complex administrative structure to enforce it. It thus requires taxpayers to pay the price of choice. It is now time to isolate and debate an important question: do we value choice highly enough to pay that price? Analysis of the employment tax system reveals that the government does not need to

156. For a good summary of literature on the prisoner's dilemma, see Ronald J. Gilson & Robert H. Mnookin, *Disputing Through Agents: Cooperation and Conflict Between Lawyers in Litigation*, 94 COLUM. L. REV. 509, 514 n.15 (1994). See generally ROBERT AXELROD, *THE EVOLUTION OF COOPERATION* (1984); MORTON D. DAVIS, *GAME THEORY* (1970); LANDSBURG, *supra* note 55, at 392-99; ROBERT D. LUCE, *GAMES AND DECISIONS* (1957).

157. See NOZICK, *supra* note 1, at 164.

158. Mortimer Lipsky analogized the existing economic order to a feudal state. LIPSKY, *supra* note 41, at 89-104. To the extent that the existing economic order reserves power for the wealthy, and pits the wealthy against those who are less so, it does indeed share some of the characteristics of the feudal state.

provide choice to raise revenue. Indeed, analysis of that system also shows that the government can raise revenue much more cheaply without providing choice. The absence of significant choice in the employment tax system is arguably consistent with the objectives of that system. Can the same be said about the abundance of choice in the income tax system? Perhaps so, perhaps not.

The answer to the foregoing question depends on the objectives of the system. If the objectives of the system are to raise revenue while reflecting and perpetuating the existing economic order, reserving the ability to exercise personal autonomy to those favored by that order, the answer should be yes. If the objectives of the system are to raise revenue while allowing the exercise of personal autonomy without regard to economic position, fostering connectedness and redistributing wealth, the answer should be no. The increase in the power to exercise personal autonomy that accompanies an increase in wealth undermines the redistributive function of the system by reducing its progressivity. It values wealth, not the personal autonomy of each individual.

Much is at stake in the perpetuation of the current system. Its development shows that, at least implicitly, we value both personal autonomy and the existing economic order and that we value those things more than we value simplicity, efficiency, and the ability of everyone to exercise the same degree of personal autonomy. A focus on the extent to which particular features of a system allow for the exercise of choice, and on the identity of those who will be the beneficiaries of that choice, will bring the debate about those values to the forefront.

E. Choice and Visibility

A focus on the existence of choice and on the identity of those who receive the opportunity to exercise it should also lead to greater questioning of the way in which the design of a tax system hides the identity of the economic bearer of the tax burden, and to an explicit debate of the merits of so hiding it. Policymakers might rationally, if paternalistically, decide that a system that hides the economic burden of a tax by placing the nominal burden on those with the power to shift it is preferable to a system that makes the identity of the bearer of the economic burden explicit. Such a decision would result in a system with hidden burdens, and would deny those affected by the system the ability to decide for themselves where the burden should be and to voice differing views regarding that placement.¹⁵⁹ Of course, such a system

159. See *supra* part IV.E.

might be expeditiously enacted because it would attract little opposition. It might also be simple and cheap to administer because it will not be concerned with tracking economic reality.¹⁶⁰ The question is whether such a system is desirable.

The segments of the population empowered by the ability to shift the economic incidence of taxation are, in very general terms, the same segments empowered by receiving the greatest number of choices under the individual income tax system. They are the owners of capital.¹⁶¹

160. For example, the employment tax system and the federal corporate income tax system are simpler and probably cheaper to administer than either the individual income tax system or a system that integrated the corporate and individual income taxes. If it were stripped of the rules designed to thwart the exercise of taxpayer choice, the corporate tax system would not be particularly complex. It is the anti-abuse rules in their various guises (not only the regulations under § 337(d) but the statutory provisions of §§ 302(b), 304, 318, 305(b)-(d), 306, and so forth) that make subchapter C complicated. Another example of this is in the realm of consumption taxes. Referring to European value-added tax provisions, Cliff Massa III, Vice Chair of the ABA Tax Section's Committee On Value-Added Tax, described them as "a set of laws about as complex as the U.S. income tax as to what is taxed, what isn't, and what is taxed at a particular rate. Companies spend a great deal of time trying to get their products into one rate or another like U.S. companies argue over the depreciation schedule." Claudia Maclachlan, *Consumption Taxes*, NAT'L L.J., July 24, 1995, at B1. To prevent this, European officials recommend eschewing exemptions in favor of refunds or rebates. *Id.*; see also Sijbren Cnossen, *Administrative and Compliance Costs of the VAT: A Review of the Evidence*, 63 TAX NOTES 1609 (1994); J. Clifton Fleming, Jr., *Scoping Out the Uncertain Simplification (Complication) Effects of VAT's, BAT's, and Consumed Income Taxes*, 2 FLA. TAX REV. 390 (1995); George K. Yin, *Accommodating the "Low-Income" in a Cash-Flow or Consumed Income Tax World*, 2 FLA. TAX REV. 445 (1995).

The problem with simpler and cheaper tax systems is that they primarily empower segments of the population who would be less empowered under a system that placed its nominal burden upon the recipient of its economic burden. (I treat the concepts of power and empowerment as positive, not as power over someone but as "ability or capacity, the power to do something." Angela Harris, *Foreword: A Jurisprudence of Reconstruction*, 82 CAL. L. REV. 741, 781 (1994) (citing THOMAS E. WARTENBERG, *THE FORMS OF POWER: FROM DOMINATION TO TRANSFORMATION* 17-19 (1990)). As Professor Harris points out, "In post-structuralist theory . . . 'power' is not only negative or repressive—an infringement on prior liberty—but also productive and creative." Harris, *supra*, at 773.) They also allow individuals, acting in isolation for their own benefit only and not in concert in pursuit of the common good, to be the arbiters of the final placement of the economic burden of taxation. They are the antithesis of connectedness.

161. Professor Kornhauser has suggested that the design of the income tax system reflects not a preference for the ownership of capital, but rather an ambivalence toward it. Kornhauser, *supra* note 120. She reaches that conclusion by tracing the apparently cyclical nature of changes in the tax law, and showing how they reveal more or less deference toward the ownership of wealth. Her argument is persuasive, and not necessarily at odds with the claim I make here, since whether the system shows more

Perhaps that is precisely as it should be. Much economic theory is built around the value of capital, the need to preserve it, and the desirability of enhancing it. But if a tax system is to be designed so as to preserve and enhance the value of owning capital, those who design it for that purpose ought to be candid about it. Lip service to notions of progressivity and ability to pay only serves to confound the issues and prevents a frank discussion of the values the system perpetuates. A discussion of the ways in which tax systems empower could go a long way toward illuminating what is at stake. It could also lead the formulators of tax policy to consider the value of empowerment as an end in itself, a goal that scholars in other fields have often urged.¹⁶²

VII. CONCLUSION

In his recent book, *Dimensions of Law in the Service of Order—Origins of the Federal Income Tax 1861-1913*, Robert Stanley, a lawyer and historian, advances an intriguing thesis: The enactment of a system of federal income taxation resulted from centrism, which he defines as including “an inertial commitment to statist capitalism—to the use of law in support of privately held enterprise.”¹⁶³ Stanley posits

or less deference to wealth at one time or another or in one respect or another, I believe it is still the case that even at its low points, it shows more deference to the ownership of capital than other possible alternatives.

162. For a thoughtful reflection on the importance of empowerment as an end in itself, see Harris, *supra* note 160, at 781. For an illustration of how empowerment can proceed from connectedness, see Barbara Christian, *The Race for Theory, in MAKING FACE, MAKING SOUL, HACIENDO CARAS: CREATIVE AND CRITICAL PERSPECTIVES BY WOMEN OF COLOR* 335, 343 (Gloria Anzaldua ed., 1990).

163. ROBERT STANLEY, *DIMENSIONS OF LAW IN THE SERVICE OF ORDER—ORIGINS OF THE FEDERAL INCOME TAX 1861-1913*, 12 (1993). Stanley’s thesis is in sharp contrast to the traditional view that sees the nominally progressive income tax as the embodiment of the principle of redistribution and thus as a system to be abhorred by defenders of the interests of private property. For example, in his excellent recent history of the American legal system, Morton Horwitz recounts a speech given by Judge John F. Dillon as *Pollock v. Farmer’s Loan & Trust Co.*, 157 U.S. 429 (1895), was being heard, and quotes him as noting that while proportional taxation might be legitimate, when taxes are levied

[F]or the real purpose of reaching the accumulated fruits of industry, and are not equal and reasonable, but designed as a forced contribution from the rich for the benefit of the poor, and as a means of distributing the rich man’s property among the rest of the community—this is class legislation of the most pronounced and vicious type; [it] is, in [a] word, confiscation and not taxation. Such schemes of pillage [are] violative of the constitutional rights of the property owner, subversive of the existing social polity, and essentially revolutionary.

HORWITZ, *supra* note 150, at 26 (quoting John F. Dillon, *Property—Its Rights and Duties in Our Legal and Social Systems*, 29 AM. L. REV. 161, 162-63 (1895)). Horwitz himself seems to view the Court’s decision holding the federal income tax unconstitutional in

that in enacting the first generally applicable system of income taxation, the legislators of the late nineteenth and early twentieth century were motivated more by what they shared—wealth, power, and the desire to retain them—than by the differences in the rhetoric that separated them.¹⁶⁴ Stanley refers to this shared perspective as centrist and uses it to

[E]xplain the apparent contradiction between the reformist promise of income taxation and its fitful history by demonstrating that it is the vision of law in society held by the dominant tradition which has led to our perception that a contradiction exists at all. Proceeding from changed assumptions about the nature of society, the state, law, and history, [Stanley's analysis] contends that there was no contradiction. [It] reveals that income taxation was not created as a vehicle for the authentic expansion of wealth and opportunity through a redirection of the continuous flow of legally channeled largesse. Rather, as a product of the center's efforts to protect itself against dissent, income taxation served as an important element in the maintenance of the traditional order.¹⁶⁵

It is my thesis that the federal income tax system still serves that purpose, and that a more complete analysis of tax system design would so reveal.¹⁶⁶

Pollock as evidence that "the anti-distribution principle had come to be thought of as part of the very essence of the constitutional law of a neutral state." *Id.* Unlike Stanley, however, Horwitz sees that view as changing, and identifies the Court's decision in *Lochner v. New York*, 198 U.S. 45 (1905) as the catalyst for change. Horwitz observes that the ratification of the 16th Amendment eliminated the "clean distinction between a tax and a taking. Not only had the constitutional legitimacy of the progressive income tax muddied that distinction but, even more important, it had discredited the Classical notion that a neutral state entailed opposition to redistribution." *Id.* at 165.

164. In 1977, Mortimer Lipsky made a similar argument with respect to the actual effects of the income tax, and charged that "The functioning of the tax law upholds the wisdom of the Biblical aphorism that 'from him who has not shall be taken away and to him who has shall be given.'" LIPSKY, *supra* note 41, at 139. While Mr. Lipsky may have been overstating his case a bit, at least as regards the burdens which served as the focus of his analysis, his charge applies with a bit more force to the distribution of power under the current system.

165. STANLEY, *supra* note 163, at 14. John Witte made a similar claim in 1985, when he argued that the ostensibly opposing sides in the tax reform debate were linked by what they shared and separated only slightly by their differences. WITTE, *supra* note 28, at 20-21, 244-68. Witte's attack on the incremental nature of changes in the tax law and his prediction that the system had undergone about as much incremental change as it could endure, though boosted by the rhetoric of the changes effected in 1986, have, in the nearly 10 years since then, been proven premature.

166. In so concluding, I part with Stanley, who concludes that the modern income tax does not reflect centrism because it now affects everyone, and is no longer reserved for a very few taxpayers at the top of the income scale, as was the 1913 tax. See WITTE, *supra* note 28, at 255-56.

A complete analysis of a tax system design should consider both how the system burdens and how it benefits—how it gives as well as how it takes away. Traditional tax policy has only considered burdens. Existing data tells us a lot about what various systems of taxation remove from people, but, predictably, not much about what such systems give them. The data generally supports the view of the income tax as progressive and thus redistributive; it shows that a higher percentage of revenue comes from the people at the top of the income scale than from the people at the bottom.¹⁶⁷ The data thus corroborates the traditional view of the income tax as the darling of liberals and progressives.¹⁶⁸

167. Chris R. Edwards, an economist at the Tax Foundation in Washington, D.C., has studied the relationship between the level of income received and the proportion of the tax burden borne, and has shown that individuals at the highest income levels supplied the greatest proportion of federal tax revenues, and that the proportion of tax revenues paid by those at the top of the income distribution rose in the decade between 1982 and 1992 notwithstanding the reduction in marginal rates during that time. Chris R. Edwards, *Who Pays Federal Income Taxes?*, 66 TAX NOTES 105 (1995). Edwards has shown that the effective “federal income tax rate rises steadily with income from 2 percent for those earning under \$10,000 per year to over 27 percent for those earning over \$1 million per year.” *Id.* Edwards also noted that while the millionaire group earned 4.6 percent of the total adjusted gross income, it paid nearly 10 percent of the total federal income taxes. *Id.* (see in particular Table 2 at 108.) Edwards’ data also shows that whereas individuals in income groups below the \$50,000 to \$100,000 group paid a share of the total taxes that was smaller than the share of total adjusted gross income they received, and individuals in the \$50,000 to \$100,000 group itself paid a share of the total taxes that was nearly the same as the share of total adjusted gross income they received (28.7 percent of AGI versus 29.5 percent of taxes), individuals in groups above the \$50,000 to \$100,000 group paid a much higher share of taxes than the share of income they received. *Id.* This distributional pattern obtained notwithstanding that the rates applicable in 1992 were lower than in 1982, a phenomenon that Edwards attributes to the increase in the share of adjusted gross income received by high income recipients. In other words, the rich are paying more in taxes because they are getting richer. While Edwards’ study indicates that the system has retained its fundamental progressive structure, the data does not permit any conclusions regarding the relative degree of progressivity.

In testimony before the Senate Finance Committee on May 18, 1995, Michael Graetz drew similar conclusions regarding the progressivity of the existing system, based on preliminary IRS data for 1993. Michael J. Graetz, *Current Flat Tax Proposals*, 67 TAX NOTES 1256, 1260 (1995). Although he was able to perform only “back of the envelope calculations,” he concluded that in 1993, tax returns with adjusted gross income above \$75,000 paid 50% of all the income taxes for that year although they accounted for only 7 percent of the total number of returns filed. *See id.* at 9.

168. Jerome Hellerstein provides a particularly concise and pithy account of the development of the first income tax. *See HELLERSTEIN, supra* note 41. Hellerstein describes how that tax, which the Socialist and Populist Parties demanded, was enacted in response to the feeling that urban investors and professionals were bearing little of the tax burden under state and local tax systems in place during the last quarter of the nineteenth century, while farmers and others in rural areas bore substantial real and personal property taxes. The income tax was enacted by a Democratic administration against the charge that to enact such a tax amounted to “socialism, communism and devilism.” *Id.* at 9. After being declared unconstitutional, the tax was ensconced in the

Traditional tax policy has not considered the ways in which tax systems can empower. No data on empowerment exists. An examination of the ways in which tax systems can empower reveals that the federal income and employment tax systems, which contribute the bulk of the revenue that feeds the federal budget, empower roughly the same group: the owners of capital. Under those systems, owners of capital enjoy maximum ability to exercise choice in determining the ultimate size of their nominal tax bill and to shift the economic burden of that bill to someone else. Empowerment analysis reveals, perhaps not coincidentally, that centrism is alive and well even today. The federal income tax system may look progressive in its distribution of burdens, but to the extent that those burdens are affected by the progressive distribution of avoidance and burden powers, the system is much less progressive than it appears. Analysis of the way in which the system distributes its benefits reveals that the centrist alliance that produced the system has succeeded in its goal of preserving centrism.

The analysis of benefits also reveals an even more insidious effect. Not only does the benefit that flows from possession of avoidance power serve to reduce the overall progressivity of the system, but the benefit that flows to the holder of burden power allows the system as a whole to hide its burden from those on whose shoulders it eventually falls. The failure to discuss the existence and distribution of these powers openly and explicitly thus compounds the disenfranchisement of those who are denied those powers. The very design of the federal tax system supports Professor Stanley's hypothesis that, notwithstanding its claims of redistribution, the system serves to perpetuate a centrist agenda. Perhaps more insidiously, it also serves to hide its effect and thus to prevent debate by those who are affected by it. In short, an analysis of the powers conferred by the federal income tax system (as well as by the employment tax system) suggests that Nozick was right—to the extent that people are permitted individually to exert their will, a seemingly

Constitution by the 16th Amendment. Professor Hellerstein also recounts that Republican party leaders regarded President Taft's submission to Congress of the 16th Amendment as a brilliant move designed to respond to the wide popular demand for an income tax at little real cost, for they expected that the amendment would fail to garner sufficient votes among the states for ratification. They were, of course, wrong. *Id.* at 7-15.

egalitarian distributional pattern can, over time, be destroyed, or at least be precluded from reaching its full egalitarian promise.¹⁶⁹

Whether centrism should continue to thrive is, of course, an important question with which taxpayers should grapple. Empowerment analysis should help them to do so. It should help to unmask the ways in which tax systems fail to deliver all that they promise and to encourage a fuller discussion of the ways in which tax systems affect our lives. The language of empowerment is easy to understand. Its costs and benefits are readily apparent. As we embark on a serious consideration of dramatic alternatives to the federal income tax system, whether they be flat taxes,¹⁷⁰ consumption taxes,¹⁷¹ a radically altered income

169. See *supra* note 1. I take a progressive tax to be egalitarian in the sense that progressivity is conceptually designed to ameliorate inequalities. See MICHAEL J. GRAETZ, *FEDERAL INCOME TAXATION*, 23-27 (1988); Charles R. O'Kelley, Jr., *Tax Policy for Post-Liberal Society: A Flat-Tax-Inspired Redefinition of the Purpose and Ideal Structure of a Progressive Income Tax*, 58 S. CAL. L. REV. 727 (1985) (examining entitlement-based arguments for progressivity in the context of a "degressive" dual-rate flat tax); Salzyn, *supra* note 38, at 584-90; see also *supra* Part VI.C. That the income tax continues to operate progressively, see *supra* note 167, is testimony to the power of a progressive rate structure and frequent change, even when coupled with significant amounts of avoidance power.

170. Senator Arlen Specter (R-Pa.) has sponsored a bill—S. 488, 104th Cong., 1st Sess. (1995)—which would impose a 20% flat tax on the earned income of individual taxpayers and would provide standard deductions ranging from \$9,500 for individuals to \$16,500 for married persons filing jointly. An alternative flat tax proposal, co-sponsored by Rep. Richard Armey (R-Tex.) and Senator Richard Shelby (R-Ala.) would also impose a flat tax on individuals' earned income, but would allow more generous standard deductions ranging from \$13,100 for individuals to \$26,200 for married couples. See H.R. 2060, 104th Cong., 1st Sess. (1995); S. 1050, 104th Cong., 1st Sess. (1995). For a closer look at the Armey/Shelby proposal, see ROBERT E. HALL & ALVIN RABUSHKA, *THE FLAT TAX* (2d ed. 1995) (setting forth the flat tax plan upon which both the Armey/Shelby, and the Specter, proposals are based); Vernon Hoven, *Flat Tax as Seen by a Tax Preparer*, TAX NOTES TODAY (Aug. 10, 1995), available in LEXIS, 95 TNT 156-62; Barbara Kirchheimer, *Armey Flat Tax Plan Panned by Treasury*, 65 TAX NOTES 655 (1994). For a closer look at the Specter proposal, see JOINT COMMITTEE ON TAXATION, *DISCUSSION OF ISSUES RELATING TO "FLAT" TAX RATE PROPOSALS* (1995). For an overview of the merits of flat taxation generally, see Curtis J. Berger, *In Behalf of a Single-Rate Flat Tax*, 29 ST. LOUIS U. L.J. 993 (1985).

171. Two consumption tax proposals are currently in the drafting stage. Senator Richard Lugar (R-Ind.) has proposed a 17% retail sales tax and Senator Sam Gibbons (D-Fla.) has proposed a value added tax (VAT), the rate of which has not been determined. Neither proposal has yet been fully fleshed out. Although these two proposals are explicitly labeled consumption taxes, it is significant to note that both the Armey/Shelby and the Specter flat tax proposals are also consumption taxes in that they do not tax individual savings. For a look at merits and demerits of consumption taxes generally, see CONGRESSIONAL RESEARCH SERVICE, *VALUE-ADDED TAX AS A NEW REVENUE SOURCE*, available in Westlaw, 1994 WL 546916; James M. Bickley, *The Value-Added Tax: Concepts, Issues, and Experience*, 47 TAX NOTES 447 (1990); David F. Bradford, *What are Consumption Taxes and Who Pays Them?*, 39 TAX NOTES 383 (1988); Barbara H. Fried, *Fairness and the Consumption Tax*, 44 STAN. L. REV. 961 (1992); Michael J. Graetz, *Revisiting the Income Tax vs. Consumption Tax Debate*, 57

tax,¹⁷² or some combination of the above,¹⁷³ we should add questions of empowerment to the debate.¹⁷⁴ Only by discussing fully the changes in benefits as well as the changes in burdens that would flow from any other system of taxation can we purport to engage in a thorough analysis of the consequences of change.

TAX NOTES 1437 (1992); Maclachlan, *supra* note 160, at B1; Eric Toder, *Comments on Proposals for Fundamental Tax Reform*, 66 TAX NOTES 2003 (1995); *see also* William H. Morris, *A National Debate on VAT: The Gibbons Proposal*, 60 TAX NOTES 1259 (1993).

172. For example, as part of the Contract with America, Rep. Bill Archer (R-Tex.) has introduced H.R. 56, a reformation, but not replacement, of the current income tax system. *See* H.R. 56, 104th Cong., 1st Sess. (1995). H.R. 56 would, among other things, "amend the Internal Revenue Code of 1986 to provide all [non-corporate] taxpayers with a 50 percent deduction for capital gains." *Id.* at 1 (synopsis). The Archer proposal has taken its share of criticism. *See, e.g.*, Michael Kinsley, *The GOP's Tax Scam*, NEW REPUBLIC, Dec. 12, 1994, reprinted in 66 TAX NOTES 611 (1995); Harold Pepperell, *'Rush' Exposes the Capital Gains Tax Cut Hoax*, 66 TAX NOTES 1200 (1995). For a look at the distributional effects of Archer's proposal, *see* Gene Steuerle, *The Distributional Effects of Tax Changes*, 66 TAX NOTES 2027 (1995). Other reforms of the current Code have been proposed. For example, H.R. 980, sponsored by Rep. Richard Gephardt (D-Mo.), provides credits and deductions to promote education, child care, and retirement savings. H.R. 980, 104th Cong., 1st Sess. (1995).

173. Michael Graetz has proposed a series of particularly intriguing combinations that would retain a progressive structure at the top of the income scale, while reducing the compliance burden for lower income and some middle class taxpayers. *See* Graetz, *supra* note 167, at 1260.

174. Consider the opportunities for taxpayer choice presented by the two most seriously proposed alternatives to the current federal income tax, the flat tax accompanied by an expanded base as in the Armey/Shelby proposal, *supra* note 170 (eliminating all itemized deductions and special exemptions), and the cash flow consumption tax. *See, e.g.*, S. 722, 104th Cong., 1st Sess. (1995) (sponsored by Sen. Sam Nunn (R-Ga.) and Sen. Pete Domenici (R-N.M.)). The Nunn/Domenici proposal would retain numerous exemptions, deductions, and credits. For a critique of both alternatives, *see* Sheldon D. Pollack, *Consumption Taxes, Flat Taxes, Capital Gains, and Other Tax Fantasies*, 66 TAX NOTES 577 (1995). For a closer look at the principles underlying the Nunn/Domenici proposal, *see* Pete V. Domenici, *The UnAmerican Spirit of the Federal Income Tax*, 31 HARV. J. ON LEGIS. 273 (1994). While little in the flatness of rates affects the ability of taxpayers to exercise choice, much in the definition of the tax base does. Thus, what at least some taxpayers would lose with the expansion of the base is the ability to choose to alter their tax liability by engaging in particular kinds of behavior. In effect, they would lose some degree of personal autonomy in the determination of tax liability. Would they be willing to pay that price, if asked the question directly? Perhaps not. Because personal autonomy is an important value and because the degree to which it exists can affect the ability of a tax system to accomplish any redistributive objective, truth in taxation requires that we begin to employ this more comprehensive analysis now.