

# News and Views from the Dismal Science

Dr. Econ's commentary on global economic and other affairs

April 2008

## April 15 - Tax Day

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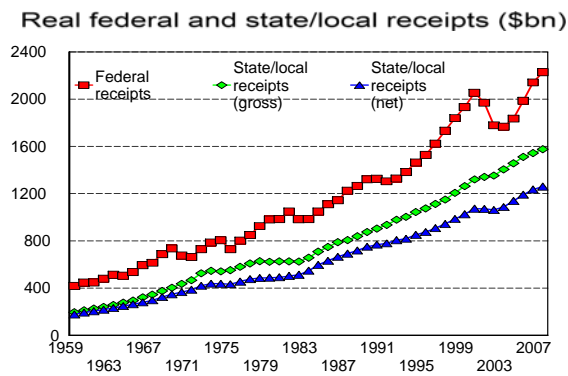


Figure 1

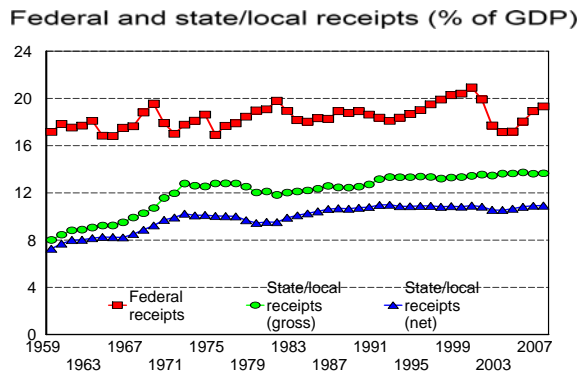


Figure 2

In the United States, April 15 is the day by which people need to have declared to the tax authorities their income for the prior year. Taxes must be paid up, or reimbursement claimed. A good opportunity, then, to use this month's column to write about taxes or, more generally, government receipts.

Each society must think about the *level* of taxes to be imposed and also about the *distribution* of the tax burden across different groups of taxpayers. Figure 1 displays federal and state receipts (adjusted for inflation) from 1959 to 2007. Because the economy grew, so did the government receipts. But whereas Gross Domestic Product, a measure of national income, grew by a factor of 4.7, federal receipts grew by a multiple of 5.3. Because state and local authorities receive transfers from the federal government, these must be subtracted to arrive at state/local *net* receipts raised from within the states. This take has risen by a factor of 7.1. Indeed, as Figure 2 shows, the overall growth of government receipts is due primarily to increases in state and local receipts in the

1960s. This despite heavy spending at the federal level during the 1960s when the Vietnam War, the Apollo moonshot program, Interstate highway building, and the introduction of income and social security programs vastly expanded the role of the federal government in society. The real "culprit," if there is one, is not the federal government, but municipalities and states.

Since the early 1970s, however, state/local net receipts have been a remarkable stable at between 10 to 11% of GDP. In contrast, federal receipts are somewhat more volatile at between 17 to nearly 21% of GDP. Adding the numbers reveals that total receipts are between one-quarter to nearly one-third of national income. But given the stability in the

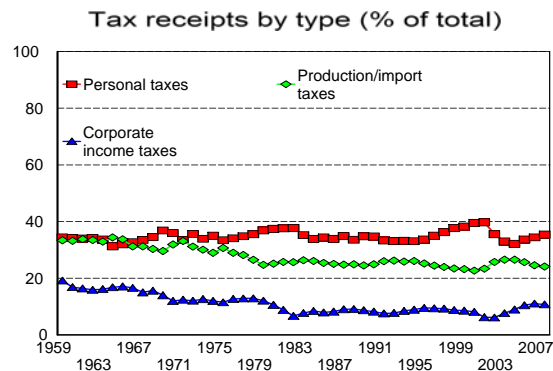


Figure 3

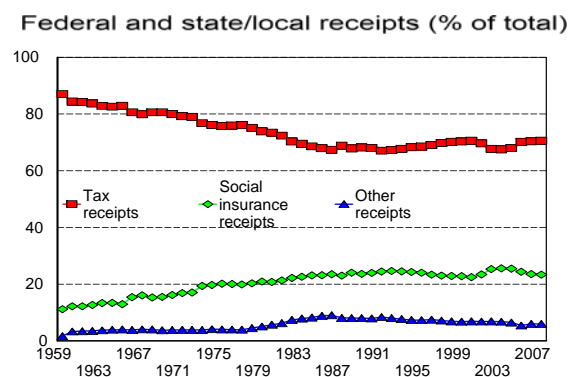


Figure 4

politically contentious issues of taxation are, the nearly 50 year record displayed in Figures 1 to 4 shows a remarkable consistency in the level and distribution of taxation, at least between personal and corporate taxation. Within this stability, however, three major trends are visible: (a) the very gradual rise in state and local taxation; (b) the more pronounced rise in social insurance taxation; and (c) since social insurance is split between employer and employee, the slow, but noticeable, decline in corporate income taxation alongside a slight overall increase in personal taxation. All-in-all, then, reason enough not to complain so much about levels of taxation per se as to more diligently examine how efficiently or inefficiently taxpayers funds are spent.

Note: All computations are based on the *Economic Report of the President 2008* (released February 2008).

**Jurgen Brauer's latest book, co-authored with Hubert van Tuyl is *Castles, Battles & Bombs: How Economics Explains Military History* (Chicago, IL: The University of Chicago Press, 2008).**

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numbers since the early 1970s, it would appear that society-at-large somehow has decided on the appropriate *level* of taxation.

What about the *distribution* of the tax burden? Who pays? Figure 3 shows the percentage of personal taxes in all government receipts (federal, state, and local) to have stayed between 30% and 40% over the entire time period, with no trend visible. Again, this is a remarkable stability. In contrast, corporate tax contributions have steadily fallen from about 20% in 1959 to about 10% in 2007, and production/import taxes have fallen as well. Thus, the percentage of the total tax take in all government receipts must have fallen as well. And indeed, Figure 4 shows a drop in tax receipts from about 90% in 1959 to 70% in 2007, made up by a corresponding rise in social insurance taxes and other receipts.

Social insurance contributions of course are split between employers and employees so that in Figure 3 the corporate tax drop from 20% to 10% is overstated and the personal tax stability around 35% is understated. Still, given how