PROGRESSIVE TAXATION REVISITED

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In 1953, two professors wrote that progressive taxation was then "widely accepted as a secure policy commitment which [did] not require serious examination."[1] Nevertheless, even forty years ago the topic seemed newsworthy enough to merit attention in light of a proposal to amend the Constitution to impose a tax ceiling that effectively would have curtailed progressivity.[2] Now, in the mid-1990s, progressivity is no longer clearly "widely accepted as a secure policy commitment." Rather, members of both parties in Congress have produced proposals for a flat (proportionate) rate income tax, and there has also been serious discussion of eliminating the income tax as we know it in favor of a consumption tax.

While progressivity has enjoyed broad approval over the years, efforts to justify that approval theoretically have been mostly inconclusive. Tax policy has not managed to clarify just what theoretical fibers make up the cloak of approval that has surrounded progressivity.[3] Thus in 1953, Professors Blum and Kalven concluded that "the case for progression, after a long critical look, thus turns out to be stubborn but uneasy."[4]

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1. Walter J. Blum & Harry Kalven, Jr., *The Uneasy Case for Progressive Taxation*, 19 U. CHI. L. REV. 417 (1952) *reprinted in* WALTER J. BLUM & HARRY KALVEN, JR., THE UNEASY CASE FOR PROGRESSIVE TAXATION 2 (1953). In the early days there was more debate over whether income was the appropriate tax base than over the progressivity of the rate structure. *Id. But see* Joseph Bankman & Thomas Griffith, *Social Welfare and the Rate Structure: A New Look at Progressive Taxation*, 75 CAL. L. REV. 1905, 1906 (1987) (progressive rates have always been controversial).

2. Blum & Kalven, *supra* note 1, at 1–2.

3. *See* Marjorie Kornhauser, *The Rhetoric of the Anti-Progressive Income Tax Movement: A Typical Male Reaction*, 86 MICH. L. REV. 465, 466 (1987) (consensus about progressivity began to crumble in the 1970s). Several surveys conducted in the 1970s and early 1980s showed that popular opinion was no longer uniformly in favor of progressivity. *Id.* Specifically, pollsters in the early 1980s found that 39% to 60% of the taxpayers polled preferred a flat tax. *See* Karlyn Keene, *What Do We Know About the Public's Attitude on Progressivity?*, 36 NAT'L TAX. J. 371, 374–75 (1983) (cited in Kornhauser).

A more recent study produced results somewhat more in favor of progressivity. Michael Roberts and Peggy Hite found that 60% to 66% of households surveyed preferred progressive rates. Michael L. Roberts & Peggy A. Hite, *Progressive Taxation, Fairness, and Compliance*, 16 L. & POL'Y 27, 44 (1994). Public opinion has supported both proportionate and progressive income tax structures because of their perceived fairness. Robert V. Beaudry, *The Flat Rate Tax: Is It a Viable Solution to the Crisis Facing the Internal Revenue Code?*, 9 OKLA. CITY U. L. REV. 219, 221 n.9 (1984).

4. Blum & Kalven, *supra* note 1, at 103.

In this article I argue that the case for progression is uneasy even for its proponents because of largely unexamined philosophical assumptions underlying the theoretical frameworks within which tax theorists have presented their arguments. By examining some theories of distributive justice developed by philosophers, I hope to begin to identify the "magic" that has cloaked progressivity and to explain why the case for progressivity is "uneasy" although the notion of progressivity, itself, may be intuitively appealing.[5]

The bulk of the arguments against progressive taxation (and in favor of a flat rate or proportionate tax) are based on some version of economic efficiency.[6] Scholars in favor of progressivity have generally accepted economic theory as an appropriate forum for debating the merits of different rate structures and have made valiant efforts to justify progressivity purely on economic grounds.[7]

Yet the economic arguments in favor of progressivity have not been strongly persuasive, and a review of only the traditional literature may well leave even the pro-progressivity reader with the conclusion that the case for progressivity does seem to be uneasy.[8] Nevertheless, progressivity has persisted in the income tax, even through moves to flatten the income tax in the mid-1980s.[9] The new Republican Congress has shown great interest in the issue of

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5. *See* Blum & Kalven, *supra* note 1, at 103–04.

6. *See, e.g.*, Beaudry, *supra* note 3, at 230 (citing legislators who blame high progressive rates for reducing work incentives); Martin Feldstein & Daniel Feenberg, *Higher Tax Rates with Little Revenue Gain: An Empirical Analysis of the Clinton Tax Plan*, 58 TAX NOTES 1653 (1993) (arguing that higher marginal rates on high-income taxpayers would result in little or no additional revenue because of intentional reductions in the amount of income produced).

7. I consider the benefit theory to be part of this framework because it can be thought of as applied Pareto efficiency. Sacrifice, or ability-to-pay, theory is a close cousin, based on income utility. The theory seeks to minimize utility loss rather than to maximize utility gain. But this anticipates the discussion in Part II.

The burden of proof in this discussion has generally been placed on those who favor progressive taxation. CHARLES O. GALVIN & BORIS I. BITTKER, THE INCOME TAX: HOW PROGRESSIVE SHOULD IT BE? (1969); Bankman & Griffith, *supra* note 1, at 1907.

8. The conclusion that the case for progressive taxation is uneasy was elegantly presented in a 1952 article by Walter J. Blum and Harry Kalven, Jr. *See generally*, Blum & Kalven, *supra* note 1. Their conclusion of uneasiness has appeared in more recent work, as well. *See also* RICHARD A. EPSTEIN, TAKINGS: PRIVATE PROPERTY AND THE POWER OF EMINENT DOMAIN 303 (1985) ("The case for the progressive tax is not 'uneasy.' It is wrong."); GALVIN & BITTKER, *supra* note 7, at 35 (Bittker: why should burden be on progressivity?). *Cf.* Bankman & Griffith, *supra* note 1, at 1967 (concluding that the case for progressivity is less uneasy than formerly supposed); Mark S. Stein, *Diminishing Marginal Utility of Income and Progressive Taxation: A Critique of The Uneasy Case*, 12 N. ILL. U. L. REV. 373, 374 (1992) (conclusion of uneasiness by modern scholars has been influenced by improper conclusions of Blum and Kalven). *But see* Nancy E. Shurtz, *A Critical View of Traditional Tax Policy Theory: A Pragmatic Alternative*, 31 VILL. L. REV. 1665, 1673 (1986) (no tax policy analysis could be compelling because possible conflicts between underlying tenets and other tenets remains unclear).

9. *See* Tax Reform Act of 1986, PUB. L. NO. 99–514. Under the 1954 Code, the maximum rate was 91%. I.R.C. § 1 (1954). The maximum nominal rate for 1994 is 39.6%. Phaseouts of personal exemptions and some deductions make the actual highest rate slightly higher at some income levels. Differences in how progressivity is measured affect the comparability of cited rates. Kornhauser, *supra* note 3, at 466 n.7.

But see Alice G. Abreu, *Choices, Burdens, and Systems of Taxation* (1995) (unpublished manuscript, on file with Donna M. Byrne) (arguing that overall the tax system may be less progressive than it appears because it has the effect of endowing upper income taxpayers with the power to affect the imposition and incidence of the tax).

progressivity, and the debate that is sure to follow will most likely take place within the same economic framework.

Some advocates of progressivity have dared to abandon the economic arena and have presented their views in terms of equity or fairness as a justification for a redistributive role for the income tax.[10] The most frequent response is that fairness is a matter of personal preference and, therefore, not an appropriate subject for debate.[11]

And there the debate usually rests, with a nod to the need for redistribution but with little analysis of the case for progressive taxation on grounds of fairness.[12] But tax is one of the basic institutions that shape society,[13] and tax policy cannot be stranded without societal goals. Thus, tax theorists are also social theorists, since the choice of tax structure has significant effects on the distribution of wealth in society.[14] The justice of that resulting distribution merits discussion in the same forum that decides to implement the rate structure.

Legal philosophers, undeterred by the notion that fairness or equity is a matter of personal preference, have long engaged in analysis of the case for one or another scheme of distributive justice. Indeed, the earliest economists (and in a sense, all economists) were the same philosophers on whom the philosophical analysis of issues of distributive justice often rests today.[15]

This article considers the traditional arguments for or against progressive taxation alongside some theories of distributive justice in favor of and opposed to income redistribution in an attempt to integrate the economic analyses of the case for progressive taxation with the philosophical bases for an unequal tax burden.

Part I defines the concept of progressivity and places the rate structure discussion within the larger context of tax policy.

Part II is an overview of the main arguments regarding progressive taxation organized according to the tax policy criteria of equity, efficiency, and simplicity. In addition to describing these arguments, I highlight the unstated philosophical choices implicit in these arguments.

10. Norman B. Ture, *Commentary*, *in* INCOME REDISTRIBUTION 159 (Colin D. Campbell ed., 1976) (criticizing another scholar [James Tobin] for examining tax progressivity other than "on the basis of the economist's specialized expertise" and rejecting arguments about redistribution). *But see* Kaplow & Shavell, *Why the Legal System is Less Efficient than the Income Tax in Redistributing Income*, 23 J. LEGAL STUD. 667 (1994) (assuming that the redistributive role needs no defense and comparing methods of accomplishing it).

11. GALVIN & BITTKER, *supra* note 7, at 28 (Bittker: choice of rate structure depends on "faith, personal preference, or fiat"); Ljubomir Nacev, *A Commentary on the Literature on Tax Policy*, 86 TAX NOTES TODAY 53-186 (Mar. 17, 1986) *reprinted in* 1 TAX POL'Y NOTES (Tax Analysts) 8 (1993). *But see* HENRY C. SIMONS, PERSONAL INCOME TAXATION: THE DEFINITION OF INCOME AS A PROBLEM OF FISCAL POLICY 17 (1938) (one should begin by saying what one thinks about inequality).

12. *See* Edward J. McCaffery, *The Holy Grail of Tax Simplification*, 1990 WIS. L. REV. 1267, 1280 (1990) (few authors have discussed normative grounds for tax equity).

13. *See* JOHN RAWLS, A THEORY OF JUSTICE 277 (1971) (including taxation as one of the basic social institutions).

14. *See* Shurtz, *supra* note 8, at 1673 (tax policy criteria represent social, as well as economic, objectives).

15. *See, e.g.*, ROBERT NOZICK, ANARCHY, STATE, AND UTOPIA 18 (1974) (citing Adam Smith's "invisible hand"); *Id.* at 40 (citing Bentham); RAWLS, *supra* note 13, at 22 n.9 (citing Adam Smith and Jeremy Bentham).

Part III describes three philosophical approaches to the issues of fairness that seem to give progressive taxation its instinctive appeal. In this section I explore the possible contributions of John Rawls, Ronald Dworkin, and Robert Nozick to the tax policy arena.

Part IV reconsiders the wealth maximization principle and considers the extent to which the philosopher's contributions can change the focus of the rate structure debate. I attempt to reconcile the gut feeling that progressivity is a good thing with progressive taxation's relatively poor showing in the economics arena. The article asks why legal philosophy is not a regular part of this discussion.

Finally, the article concludes that unstated assumptions about entitlement to wealth create the uneasiness that generally characterizes the case for progressive taxation. Theories based on incompatible assumptions appear compatible until their assumptions are expressed. This false compatibility, I conclude, is at the root of the uneasy case. I do not end with thumbs up or thumbs down for progressivity; rather, I suggest a broader way of approaching tax policy issues, inviting the input of legal philosophers into a debate long dominated by economists. I conclude by arguing that the philosophical assumptions underlying economic decision making should be made explicit, rather than left to gut-level instinctive feelings.

I. ARGUMENTS ABOUT PROGRESSIVE TAXATION

A. Types of Progressivity

In very general terms, progressivity means that tax rates increase as one moves up on some scale. Usually, progressivity is understood to mean progressive with respect to income. Thus, high income taxpayers pay a higher percentage of their income in taxes than do low income taxpayers. Similarly, sales taxes and wage taxes are said to be regressive. Even though these taxes are not imposed with respect to income, low-income people pay a higher percentage of their incomes as sales and wage taxes than do high-income people.[16] In some contexts, however, progressivity is measured against some scale other than income. The federal estate and gift taxes, for example, are imposed at higher and higher rates as the amount of wealth transferred increases.[17] Similarly, a consumption tax could be "progressive" if tax is imposed at increasing rates as consumption increases.[18] While there may be a direct correlation between consumption level or amount of wealth transferred and income, income is not the starting point, per se, in these systems. For

16. GALVIN & BITTKER, *supra* note 7, at 69 (Bittker rebuttal: state sales and property taxes are regressive only with respect to income).

17. *See* I.R.C. § 2001 (Supp. 1993) (estate tax rates); *id.* § 2502(a)(1) (1988) (gift tax rate computed under § 2001).

18. *See* William D. Andrews, *Fairness and the Personal Income Tax: A Reply to Professor Warren,* 88 HARV. L. REV. 947, 956 (1975) (noting that a consumption tax can have graduated rates); Michael J. Graetz, *Implementing a Progressive Consumption Tax,* 92 HARV. L. REV. 1575, 1579 (1979); Edward J. McCaffery, *Tax Policy Under a Hybrid Income-Consumption Tax,* 70 TEX. L. REV. 1145, 1168 (1992) [hereinafter McCaffery, *Hybrid*] (describing arguments for a progressive tax on consumption as a measure of ability to pay).

purposes of this discussion, however, progressivity should be understood to mean progressivity with respect to income.[19]

A second distinction should be made. There is more than one way to achieve progressivity through an income tax. The first is through the familiar tax-bracket system by which additional increments of income are taxed at ever higher rates. Tax brackets cause the effective rate (the percentage of total income paid as tax) to increase by increasing the marginal rate (the rate of tax on·the last dollar received) as income increases. Brackets have always been a characteristic of the income tax and are a feature of the current system, which now uses five marginal rate brackets ranging from 15% to 39.6%.[20]

A second way of achieving progressivity is through a zero tax bracket or exemption. Exempting the first X dollars makes even a flat-rate tax somewhat progressive because the percentage of total income paid as tax increases as income increases.[21] For example, assume a ten percent flat rate (proportionate) tax, and let us exempt the first $10,000 of income altogether. Now imagine several individuals with incomes of $10,000, $15,000, $50,000, and $200,000. The taxpayer with $10,000 of income pays no tax and has a tax rate of zero percent. The taxpayer with $15,000 on income also pays no tax on the first $10,000 because of the exemption, but pays ten percent of the remaining $5000 for a total tax of $500. This works out to 3.3 percent of the taxpayer's $15,000 income. The taxpayer who has $50,000 in income pays $4000 in tax, which is eight percent of the taxpayer's income. Finally, the $200,000 taxpayer pays $19,000 in tax, which is 9.5 percent of this taxpayer's income. This example is summarized and expanded in Table I.

19. Why income should be the baseline is another interesting issue. Presumably, income offers an easily measured way of comparing taxpayers' ability to pay. *See* RICHARD A. MUSGRAVE, THE THEORY OF PUBLIC FINANCE 91 (1959) (notion that just taxation is taxation according to ability to pay goes back to at least the 16th century). Wealth might be a better measure of ability to pay, but it presents tremendous measurement challenges. *Id.* at 94 (early notions of ability to pay were based on property rather than income; the proper index is still subject to debate).

20. I.R.C. § 1 (Supp. 1993). For the sake of simplicity, I am ignoring the effect of phasing out personal exemptions and limiting deductions for certain taxpayers. *See* I.R.C. § 68 (Supp. 1993) (overall limitation on itemized deductions); *id.* § 151(d)(3) (Supp. 1993) (phaseout of personal exemptions).

21. *See* Bankman & Griffith, *supra* note 1, at 1945 (optimal tax would be a flat rate with a demogrant and would be effectively progressive); Curtis J. Berger, *In Behalf of a Single-Rate Flat Tax*, 29 ST. LOUIS U. L.J. 993, 1003 (1985) (flat tax with exemption is effectively progressive).

TABLE I.

Income	Tax($)	Tax (% of income)
$ 10,000	0	0%
$ 15,000	500	3.33%
$ 30,000	2,000	6.67%
$ 50,000	4,000	8.00%
$ 200,000	19,000	9.50%
$2,000,000	199,000	9.95%
Exemption Amount $10,000; Flat Tax Rate of 10%		

A proportionate or flat-rate tax with an exemption, as in the above example, is sometimes called a degressive tax. The total effect is somewhat progressive in that the effective rate of tax increases as income increases, even though the marginal rate remains constant. Most of the increase occurs at the lower income levels, however, and the rate does flatten out considerably as it approaches the nominal rate of ten percent, which it will never quite reach.[22] The current tax system utilizes this "degressive" feature as well as the familiar marginal rate brackets in order to achieve overall progressivity.[23] A third source of progressivity is the elimination of deductions or other tax breaks as income rises beyond some threshold level. This additional progressivity is hidden from many (if not most) taxpayers.[24] Examples of this "back door" progressivity are the 2-percent floor on miscellaneous itemized deductions,[25] the phaseout of personal exemptions,[26] and the overall limitation on itemized deductions.[27] For purposes of this discussion, however, progressivity will mean

22. It is thus possible for one theorist to write about a "progressive flat rate tax." *See* 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) [hereinafter O'Kelley, *Post-Liberal*].

This phenomenon of merely approaching the nominal rate may evoke unpleasant associations for anyone who struggled to understand limits in first semester calculus.

23. *See* I.R.C. § 151 (Supp. 1993). A variant of the "degressive" tax is a combination of a flat rate on all income with a "demogrant," a lump-sum payment to every taxpayer. *See* Bankman & Griffith, *supra* note 1, at 1953. At low incomes the grant would exceed the amount of tax resulting in a negative income tax. At high incomes, the effective rate of tax would approach the nominal rate, resulting in a smoothly progressive tax similar to the degressive tax. At some point the amount of tax paid would exactly equal the demogrant resulting in a tax of zero. At incomes above this point, the tax would be effectively the same as a proportionate tax. *Id.* A tax accompanying a demogrant could be progressive even if marginal tax rates decline as income rises. If the progressivity achieved with the grant outweighs the regressivity of declining marginal rates, the overall tax would still be progressive.

24. Abreu, *supra* note 9 (recent tax legislation uses the "back door" to introduce progressivity into the system). Professor Abreu argues that a fourth source of progressivity (or limitation on progressivity is the extent to which the tax system allocates choice. The ability to choose whether or how to enter into transactions is a benefit available mostly to higher income taxpayers and should be considered in discussions of progressivity. *Id.*

25. I.R.C. § 67 (Supp. 1993).

26. I.R.C. § 151(d)(3) (Supp. 1993).

27. I.R.C. § 68 (Supp. 1993).

a system that includes increasing marginal tax rates and which probably, but not necessarily, includes an exemption amount.

B. Broader Context

Actually, the discussion of progressivity should be viewed as part of a larger debate about the nature of the tax system. First, the federal income tax is only part of the overall tax system. The effects of excise taxes, wealth taxes, and consumption taxes at the national, state, and local levels are all part of this picture. From the perspective of an individual taxpayer, the income tax rate structure may be insignificant compared to the impact of employment taxes and property taxes.[28] Indeed, some analysts support progressivity in the income tax only insofar as it counteracts regressivity in the rest of the tax system.[29] In addition, the discussion about progressivity is often really part of a broader discussion about the extent to which we should tax labor relative to capital. High income taxpayers often receive a greater portion of the income as returns from investment or as capital appreciation.[30] Thus, higher rates on high incomes may affect savings disproportionately.[31]

Finally, the tax system cannot really be viewed separately from the expenditure system.[32] For any individual taxpayer, what really matters is the net flow of benefits to or from the government.[33] Some of these benefits may be built into the tax system in the form of reduced tax expenditures, adding further confusion to the issue of who really pays more or less tax.[34] Thus, even

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28. *See* Blum & Kalven, *supra* note 1, at 6 (discussion of merits of progressivity can apply to progressivity in the system as a whole even though the focus is on the income tax). For an interesting argument that the original role of the income tax was to provide an appearance of justice and progressivity in comparison with the extensive excise taxes in place at the time, see R. Stanley, *Dimensions of Law in the Service of Order* 21–22 (1993) (noting that to one 19th Century proponent of the income tax, the income tax prevented a "clamor" that would otherwise come from the masses "who will complain of injustice and wrong"). Professor Stanley argues that wealthy industrialist elites were willing to vote for a progressive tax on the very rich in order to keep in place a regressive tax system that would have been politically unacceptable in isolation. *Id.*

29. *See* Blum & Kalven, *supra* note 1, at 6 (the income tax is the best vehicle for making the whole system progressive); Beaudry, *supra* note 3, at 244 (a flat rate tax might result in a system that is regressive overall).

But see GALVIN & BITTKER, *supra* note 7, at 79 (Galvin rebuttal: the argument that progressive income tax makes overall system proportionate undermines all other arguments for general progressivity).

30. Blum & Kalven, *supra* note 1, at 26 (the higher the income, the higher the likelihood of savings).

31. *But see* GALVIN & BITTKER, *supra* note 7, at 80 (Galvin rebuttal: investment income should be regarded as the stable, baseline income and services income as the income subject to the highest rates).

32. GALVIN & BITTKER, *supra* note 7, at 139–40 (comments of Gerard Brannon: ultimate judgment should consider not only taxes and expenditures, but also "the whole government operation with regard to property rights").

33. George K. Yin et al., *Improving Participation and Compliance in the Earned Income Tax Credit Program*, 94 TAX NOTES TODAY 40–56. Charles Galvin, therefore, argues for a combination of a broad base, a proportionate tax with a negative income tax at the bottom, plus direct expenditures. GALVIN & BITTKER, *supra* note 7, at 95–96.

34. Criticism of the Internal Revenue Code as it existed in the early 1980s is often particularly muddled because of the many exclusions, exemptions, and deductions available to upper income taxpayers. Tax scholars found it nearly impossible to focus only on the tax base or only on the rate structure. *See, e.g.*, Beaudry, *supra* note 3, at 227 (analyzing proposals for a comprehensive broad-based flat tax); O'Kelley, *Post-Liberal*, *supra* note 22, at 734 (question of tax burden obscured by policy issues and complexity).

a flat tax may not be proportionate in effect if some groups of taxpayers receive benefits that exceed the amount of tax they pay (or even if one group of taxpayers receives greater benefits proportionately than another). Notwithstanding the claims of the multitude of interesting policy issues that intersect and compete with the choice of rate structure in determining the shape of the tax system, this article will focus only on the issue of progressivity and the philosophical underpinnings of arguments for and against progressive taxation. The philosophical issues that inform the choice of rate structure are also significant in all of the other policy debates and should be expressed in those discussions as well.[35]

C. Burden of Proof

Many scholars have asked why proponents of progressive taxation must bear the burden of proof of justifying a rate structure. Opponents of progressivity take proportionate taxation to be presumptively fair and better for the economy.[36] Thus, their efforts are generally focused on attacking progressivity, and those in favor of progressivity find they must rise to its defense. The arguments in favor of progressivity have not been overwhelmingly persuasive, at least partly because they are based on theoretical frameworks that rest on sometimes conflicting philosophical starting points.[37] Proponents of progressivity point out, however, that no airtight case can be presented for proportionate taxation either. Why then is proportionate taxation granted a presumption of fairness and efficiency?[38]

Two responses to the burden-of-proof question present themselves. First, progressive marginal rates are the status quo. Since 1913, the federal income tax has always had progressive rates and has always included an exemption.[39] Legal scholarship is most interesting when it challenges that which is taken for

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35. *See* Elliott M. Abramson, *Philosophization Against Taxation: Why Nozick's Challenge Fails*, 23 ARIZ. L. REV. 753 (1981); Abreu, *supra* note 9 (benefits should be considered explicitly in tax policy discussions); O'Kelley, *Post-Liberal, supra* note 22, at 734 (structural complexity and policy rationales behind individual Code provisions obscure rate structure discussions); Charles R. O'Kelley, Jr., *Rawls, Justice, and the Income Tax*, 16 GA. L. REV. 1, 5–6 (1981) [hereinafter, O'Kelley, *Rawls*] (focusing only on inner workings of system insulates it from criticism; questions of social justice must also be addressed).

36. Blum & Kalven, *supra* note 1, at 3; Bankman & Griffith, *supra* note 1, at 1907. Blum and Kalven point out that no case need be made that progressive taxation is preferable to a regressive tax. The only comparison possible, then, is progressive taxation as opposed to proportionate taxation. Blum & Kalven, *supra* note 1, at 3. *See also* Shurtz, *supra* note 8, at 1689 (choice of rate structure is between proportionate and progressive rates).

37. *See* Shurtz, *supra* note 8, at 1673 (tax policy criteria bound to conflict because based on different underlying tenets).

38. *See* GALVIN & BITTKER, *supra* note 7, at 22 (Galvin, first lecture: some progressivity is acceptable to compensate for regressivity of state taxes); *Id.* at 32 (Bittker, second lecture: earlier commentators have accepted the fairness of proportionality as self-evident).

A proportionate tax seems generally to be the minimum acceptable structure for an income tax. While no one would seriously argue for the fairness of a regressive income tax, many non-income taxes are regressive with respect to income.

Most consumption taxes would be regressive, for example, although this is not generally considered a defect. In addition, the current social security tax is a flat percentage up to an income cap level, above which it is not imposed at all. I.R.C. §§ 3101–26 (1988). Across the range of all incomes, then, the social security tax is regressive with respect to income, yet this is acceptable regressivity.

39. Blum & Kalven, *supra* note 1, at 12.

granted.[40] It is thus more interesting to attack progressivity, which we have, than to attack a flat-rate tax, which we do not.

The second response, and the one with which we are concerned here, is that the case for *or against* progressivity ultimately rests on philosophical considerations. To the extent that the debate about progressivity has rested on benefit theory and efficiency arguments, the whole debate has reflected a choice of analytical starting point that supports proportionate taxation better than progressive taxation.[41] Because this starting point is usually not identified, progressivity is always on the defensive. Arguments based on a philosophy that does not justify progressive taxation themselves cannot justify progressive taxation. Accordingly, the philosophical considerations underlying the discussion must be made explicit, not just because progressivity can be justified through philosophical arguments,[42] but because it makes little sense to discuss the rate structure without examining the rules of the debate itself.

II. SIMPLICITY, EFFICIENCY, AND EQUITY

While the hallmarks of a good tax system have included as many as seven different criteria,[43] the many criteria are often reduced to the three broad categories of equity, efficiency, and simplicity.[44] Progressivity has been subject to scrutiny through these lenses as well. Opponents of progressivity claim that it makes the tax system unduly complex and economically inefficient. In addition, progressivity presents equity issues that do not have easy answers and is, therefore, both criticized and supported on equity grounds. Finally, many theorists reject progressivity as economically inefficient. In this section I review the tax policy arguments that are usually made in these three categories, highlighting their inconclusiveness. While common sense would seem to suggest that arguments of equity require debate in philosophical terms, it may be less obvious that arguments based on economic efficiency also have philosophical underpinnings. In both cases, however, the philosophical aspects of these issues are invisible in most traditional tax scholarship.[45]

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40. Harold S. Lewis, Jr., *Integrity in Research*, 42 J. LEGAL EDUC. 607, 609 (1992) (challenges to received wisdom are afforded great tolerance). *See also* Blum & Kalven, *supra* note 1, at 14 ("rigorous analysis of progression came only after the idea had become a political reality").

41. *See* Kornhauser, *supra* note 3, at 469 (assumptions underlying analytical framework are usually not made explicit).

42. It can just as easily be rejected through such arguments, depending on the starting assumptions.

43. Joseph T. Sneed, *The Criteria of Federal Income Tax Policy*, 17 STAN. L. REV. 567, 568 (1965) (describing seven purposes of the income tax: (1) revenue raising; (2) a practicality and workability; (3) horizontal equity; (4) economic stability; (5) reduction of economic inequality; (6) economic efficiency; (7) harmony between tax and political order). Shurtz, *supra* note 8, at 1667–68 (commenting on Sneed's seven criteria).

44. *See, e.g.*, Robert J. Peroni, *A Policy Critique of the Section 469 Passive Loss Rules*, 62 S. CAL. L. REV. 1, 62 (1988) (tax system should be fair, economically efficient, and simple).

45. Professor Sneed attributes this invisibility to the preference of tax theorists for discussing "implementation of their premises rather than the premises themselves." Sneed, *supra* note 43, at 584. *See also* Shurtz, *supra* note 8, at 1673–75. Professor Shurtz argues that because traditional tax policy criteria have different theoretical underpinnings, they inevitably conflict with each other and, therefore, provide no basis on which to make policy decisions. *Id.*

A. *Simplicity*

Progressive marginal rates, according to their detractors, introduce unwelcome and unnecessary complexity into the tax system.[46] Any bracket structure entails more complexity than a flat tax and provides incentives for taxpayers to find loopholes and shift income.[47] If increasing taxable income brings a disproportionately higher tax burden, there is more incentive to find creative ways to keep taxable income low. In addition, the "back door" sources of progressivity—phaseouts and limitations on deductions—also increase the complexity of the system. While this type of complexity creates interesting work for tax practitioners, some proponents of a flat tax have identified a misuse of resources in this "work."[48] This particular source of complexity is deemed unnecessary and undesirable because it is avoidable through a flat tax.

But progressive rates are not the only source of tax planning possibilities.[49] Even a flat tax would not eliminate the great loophole hunt, as long as the Code allows any potential for timing of deductions.[50] With or without brackets, taxpayers generally would prefer to pay later rather than sooner. In addition, when losses are assigned to a particular tax year, the effect of brackets is present even without brackets. If possible, taxpayers would rather have income in a "low-bracket" year in which losses or deductions are available to soak it up. Similarly, the at-risk rules and passive activity loss rules would function to create "brackets" even in the presence of an underlying flat tax.[51]

In addition to the timing effects and anti-tax-shelter provisions, the attempt merely to create a statutory definition of economic net income

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46. Blum & Kalven, *supra* note 1, at 15 (progression has high costs in terms of complexity). *See also* McCaffery, *supra* note 12, at 1274 (progressive marginal rates add structural complexity to income tax).

47. EPSTEIN, *supra* note 8, at 299. In other words, a flat tax would simplify private planning and reduce lawful and unlawful tax avoidance. *Id. See also* GALVIN & BITTKER, *supra* note 7, at 16. *Cf.* Blum & Kalven, *supra* note 1, at 15 (progression makes it advantageous to split income between taxpayers).

48. *See, e.g.*, Dan T. Smith, *High Progressive Tax Rates: Inequity and Immorality?*, 20 U. FLA. L. REV. 451, 459 (1968) (contribution of tax practitioners to the general welfare is ambiguous). *But see* Bankman & Griffith, *supra* note 1, at 1932–33 (citing studies showing that the rate structure adds little complexity to return preparation).

49. Bankman & Griffith, *supra* note 1, at 1935 (intuition and experience indicate only a small amount of tax practice is related to progressivity).

50. *See* GALVIN & BITTKER, *supra* note 7, at 33–34 (Bittker, second lecture). This is another example of how the rate structure debate cannot really be separated from other major issues, such as the comprehensiveness of the tax base. See O'Kelley, *Post-Liberal*, *supra* note 22, at 730–35, for an integrated discussion of the tax base and the rate structure.

51. *See* I.R.C. §§ 465 and 469 (1988). Section 465 provides, generally, that a taxpayer may deduct expenses attributable to an activity only to the extent that the taxpayer's own assets (as opposed to proceeds from debt secured by the activity itself) have been invested in the activity; in other words, to the extent that the taxpayer is personally "at risk." I.R.C. § 465 (1988).

Section 469 provides, generally, that a taxpayer who does not "materially participate" in an activity may deduct expenses from that activity only against proceeds from that activity or from other "passive" activities. Accordingly, taxpayers have an incentive to realize "passive activity losses" when they have passive activity income. I.R.C. § 469 (1988). *See generally*, Peroni, *supra* note 44.

See also Bankman & Griffith, *supra* note 1, at 1935–37 (discussing sources of Code complexity other than progressivity); David Sachs, *Variations on a Theme by Dick Armey—A Framework for Real Tax Simplification*, 66 TAX NOTES 863, 864 (1995).

contributes complexity to the income tax.[52] Given the tremendous complexity involved in trying to achieve a fair measure of net income, the complexity attributable to progressivity seems minor. Add to this the many tax expenditures accomplished through deductions,[53] and the complexity from brackets is barely visible.

B. Efficiency

Arguments based on the extent to which progressive taxation distorts economic decision-making and creates a "drag" on the economy are perhaps the most vigorously asserted[54] and come in the most formidable and technical packages. In short, progressive rates are criticized because they create economic inefficiency.[55] "Efficiency," however, can have several different meanings in this context and it is not always clear which meaning is intended.[56]

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52. *See* William J. Turnier, *Personal Deductions and Tax Reform: The High Road and The Low Road,* 31 VILL. L. REV. 1703, 1705 (1986) (deductions useful in taxing net income rather than gross receipts). While there is general agreement that an income tax should tax net income rather than gross receipts, there is less agreement on how to define net income. *See* Gerard M. Brannon, *Tax Loopholes as Original Sin: Lessons from Tax History,* 31 VILL. L. REV. 1763, 1765 (1986); Shurtz, *supra* note 8, at 1669–71 ("reality gap" between economic income and taxable income; no good definition of income).

Most traditional tax theoreticians begin with the widely cited "Haig–Simons" definition: "the algebraic sum of (1) the market value of rights exercised in consumption and (2) the change in the value of the store of property rights between the beginning and end of the period in question." Brannon, *supra* at 1765 nn.10–11 (citing SIMONS, *supra* note 11, at 50). *See generally* BORIS I. BITTKER & LAWRENCE LOKKEN, FEDERAL TAXATION OF INCOME, ESTATES AND GIFTS ¶ 3.1.1 (2d ed. 1989).

For an interesting debate on income and what constitutes an appropriate tax base, *see generally* Boris I. Bittker, *Comprehensive Income Taxation: A Response,* 81 HARV. L. REV. 1032 (1968); Boris I. Bittker, *A "Comprehensive Tax Base" as a Goal of Income Tax Reform,* 80 HARV. L. REV. 925 (1967) (implications of a "no-preference" tax base); Charles O. Galvin, *More on Boris Bittker and the Comprehensive Tax Base: The Practicalities of Tax Reform and the ABA's CSTR,* 81 HARV. L. REV. 1016, 1017 (1968) (plain language illumination of Haig–Simons definition); Richard A. Musgrave, *In Defense of an Income Concept,* 81 HARV. L. REV. 44, 47 (1967) (historical development of tax system has chosen income rather than consumption as basic measure for assessing tax); Joseph A. Pechman, *Comprehensive Income Taxation: A Comment,* 81 HARV. L. REV. 63, 64 (1967) (Haig–Simons definition is basic concept used in discussing comprehensive income taxation).

53. *See generally,* Stanley S. Surrey, *Tax Incentives as a Device for Implementing Government Policy: A Comparison with Direct Government Expenditures,* 83 HARV. L. REV. 705 (1970) (discussing logic of accomplishing policy objectives through the tax laws).

54. *See* Beaudry, *supra* note 3, at 229–30 (quoting Senator Helms, quoting George Gilder: highly progressive rates "redistribute taxpayers...from offices and factories to golf courses, foxhunts, and tropical beaches,...from productive professions to excess financial intermediation and finagling"). *See also,* Bankman & Griffith, *supra* note 1, at 1918 (the prima facie case against progressive taxes is drag on labor efficiency).

55. This claim is sometimes extended to income taxes in general. *See* Louis Kaplow & Steven Shavell, *Why the Legal System Is Less Efficient than the Income Tax in Redistributing Income,* 23 J. LEGAL STUD. 667, 667 (1994) ("income taxes and transfer payments distort incentives to work").

56. Jules L. Coleman, *Efficiency, Exchange, and Auction: Philosophic Aspects of the Economic Approach to Law,* 68 CAL. L. REV. 221, 222 (1980) [hereinafter Coleman, *Exchange*] (describing four notions of efficiency—allocative efficiency, Pareto optimality, Pareto superiority, and Kaldor–Hicks efficiency); Jules L. Coleman, *Efficiency, Utility, and Wealth Maximization,* 8 HOFSTRA L. REV. 509, 512 (1980) [hereinafter Coleman, *Utility*] (Posner's wealth maximization increases the total to five); Lewis A. Kornhauser, *A Guide to the Perplexed Claims of Efficiency in the Law,* 8 HOFSTRA L. REV. 591, 592 (1980) (economists distinguish between productive and allocative efficiency); Uwe E. Reinhardt, *Reflections on the*

In addition, criticism based on efficiency, however defined, is persuasive only to the extent that we agree on the level of importance that efficiency should occupy. The choice of efficiency as the most important criterion, however, requires choices that can only be based on more fundamental philosophical beliefs.

Finally, the degree of efficiency is always measured against a theoretical world without taxes. Thoughtful scholars may disagree, however, on whether such a world is any more or less efficient than one with tax.[57]

The following is a brief explanation of some of the usual meanings of efficiency.[58] The next section will discuss some of the specific inefficiency claims leveled against progressive taxation. Finally, we will consider the unstated but necessary value judgments that underlie the choice of efficiency as a criterion, as well as the usefulness of making efficiency comparisons in the first place.

1. Definitions of Efficiency

A standard desk dictionary defines efficiency as "effective operation as measured by a comparison of production with cost (as in energy, time, and money)."[59] This type of production-maximizing efficiency is probably what most people mean by the word. This is fine, as far as it goes, but is more relevant to engineering problems than to social welfare economics. Economists who confront the problem of determining an allocation of scarce resources that maximizes the value of a mix of outputs, not all of which are tangible or have monetary equivalents, often employ the concept of *Pareto efficiency* or *Pareto optimality*.[60] An allocation is Pareto optimal if there is no other allocation that would make one person better off without making someone else worse off.[61]

Meaning of Efficiency: Can Efficiency Be Separated from Equity?, 10 L. & POL. REV. 302, 315 (1992) (the term "efficiency" is widely misunderstood and misused).

57. *See generally* Duncan Kennedy & Frank Michelman, *Are Property and Contract Efficient?*, 8 HOFSTRA L. REV. 711 (1980) (arguing that a system of private property rights is not presumptively more or less efficient than the "state of nature" or a system of forced sharing). Professors Kennedy and Michelman point out that efficiency comparisons are often made between types of taxation, rather than between a tax and a non-tax world. Because any social structure "distorts" incentives relative to a Robinson Crusoe-like world, efficiency comparisons of different kinds of distortions may be meaningless. *Id.*

58. More comprehensive explanations are available in RICHARD A. MUSGRAVE & PEGGY B. MUSGRAVE, PUBLIC FINANCE IN THEORY AND IN PRACTICE 59–65 (1989); Reinhardt, *supra* note 56; Jules L. Coleman, *The Economic Analysis of Law*, *in* ETHICS, ECONOMICS & LAW 83 (J. Roland et al. eds., 1982).

59. WEBSTER'S NINTH NEW COLLEGIATE DICTIONARY 397 (1989).

60. Reinhardt, *supra* note 56, at 306 (Pareto efficiency is the most popular notion of efficiency); L. Kornhauser, *supra* note 56, at 592 (allocative efficiency is Pareto efficiency).

61. Coleman, *Utility*, *supra* note 56, at 513; Reinhardt, *supra* note 56, at 307. For a more elaborate presentation of Pareto efficiency, *see* MUSGRAVE & MUSGRAVE, *supra* note 58, at 63:

> [In] an economy with two consumers, A & B, and two products, X & Y...these conditions must...be met:
>
> 1. Efficiency requires that any given amount of X should be produced in such a way as to permit the largest possible amount of Y to be produced at the same time, and vice versa. The best available technology should be used. If one technique permits production of 100 units of X and 80 units of Y and another permits 100 units of X combined with only 50 units of Y, the former method is obviously to be preferred.

Related to Pareto optimality is Pareto superiority. A change from one situation to another is a Pareto superior move if at least one person is made better off and no one ends up worse off.[62]

Three points should be made about the Pareto concept. First, in Pareto efficiency, people are better off or worse off in terms of their utility or welfare.[63] Utility is the satisfaction one derives from various goods and attributes.[64] Although utility is difficult to measure, it is a variable that recognizes that life is about more than simply money.[65] So money is valued because of the utility it brings, usually indirectly through acquisition of goods and services. An allocation is Pareto efficient if there are no voluntary trades that anyone would be willing to make. A voluntary trade always leads to an allocation that is Pareto superior to the starting allocation, at least with respect to the parties involved, because as a theoretical matter, no one would enter into a voluntary trade if the thing or position received were not more attractive than that given up. Thus, it is possible to rank individual preferences when trades are voluntary.

Although voluntary trades result in theoretical improvements in utility for the parties involved,[66] they could also result in diminished utility for nonparties.[67] Because of the possibilities of such externalities, it is almost impossible to tell whether or not a change really is Pareto superior.

> 2. The "marginal rate of substitution" in consumption between goods X and Y must be the same for consumers A and B. By this we mean that the rate at which A and B will be willing to trade the last unit of X for additional units of Y should be the same. If A is willing to give 1 unit of X for 3 units of Y, and B will give 4 units of Y for 1 unit of X, it will be to the advantage of both to exchange, with A increasing consumption of Y, and B consuming more of X until equality of the marginal rates of substitution is restored.
>
> 3. The marginal rate of substitution of X for Y in consumption should be the same as their marginal rate of transformation in production. The latter is defined as the additional units of X that can be produced if production of Y is reduced by 1 unit. Thus, if the marginal rate of substitution in consumption is 3X for 2Y. While the marginal rate of transformation in production is 3X for 1Y, it will be desirable to increase the output of Y and to reduce that of X until the two ratios are equalized.

Id.

62. Reinhardt, *supra* note 56, at 307.

63. Or happiness or satisfaction. All of these are more or less synonymous with "utility" for this purpose.

64. RICHARD A. POSNER, THE ECONOMIC ANALYSIS OF LAW 11 (3d ed. 1986). Judge Posner gives an example of the utility of a growth hormone to someone who will be stunted without it relative to the utility to someone who will be normal height without and will only gain a couple inches with. *Id.*

65. *See* Richard A. Posner, *Utilitarianism, Economics, and Legal Theory*, 8 J. LEGAL STUD. 103, 122 (1979) [hereinafter Posner, *Utilitarianism*] (wealth cannot be equated with happiness and people are not purely wealth maximizers although wealth is important to most).

The difficulty of measurement does not make utility a worthless concept. *Cf.* Coleman, *Utility, supra* note 56, at 515 (although the Pareto standard does involve comparisons of individual utility, it can be justified on other grounds as well).

66. The improvements are only theoretical because some voluntary trades could result in disutility if, for example, the package received turns out to be not so great after all.

67. *Cf.* POSNER *supra* note 64, at 12–13 (transactions that affect nonparties would not be Pareto optimal unless all affected parties were compensated).

Second, unlike the dictionary definition, Pareto efficiency does not require maximization of any measure.[68] In the case of productive (dictionary) efficiency, the ratio of output to input is maximized. In the case of Pareto efficiency, however, there is no maximization of output or even welfare because of the significant veto effect of the second half of the definition.[69] Thus even if a reallocation would double the total "output" of welfare, the status quo would still be Pareto efficient if the increase could be achieved only at a utility cost to one person, however slight. In other words, any allocation is Pareto efficient unless only costless improvements are possible.

Finally, along these same lines, some intuitively unappealing allocations of scarce resources, once in place, are Pareto efficient because any reallocation that would make someone better off would make someone else worse off. For example, assume there are only two people, Rich and Poor, and Rich owns all the productive resources while Poor owns none. In other words, Poor has nothing for which Rich would be willing to trade. The allocation of resources is Pareto efficient if the only way to make Poor better off is to make Rich worse off.[70]

Because Pareto efficiency tends to validate the existing allocation, whatever it is, and says nothing of maximum output of any sort, economists often use a different kind of efficiency to evaluate alternative allocations. An allocation is more efficient than another under the Kaldor–Hicks definition of efficiency if some people are made better off and it would be possible, at least in theory, for the winners to compensate the losers, even if no compensation actually takes place.[71] Thus, Kaldor–Hicks efficiency is a maximizing concept.

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68. *See* Coleman, *Utility*, *supra* note 56, at 516 ("Pareto judgments are expressed in terms of individual-preference orderings rather than in terms of total utility.").

69. Pareto improvements do increase total utility, however, since by definition, there are no losses of utility but there are gains in any move from a state that is not Pareto efficient to one that is (or from one inefficient state to another one that is Pareto superior). *See* Coleman, *Utility*, *supra* note 56, at 515.

70. Of course, if Rich would actually feel better off after giving some of the resources to Poor, the situation would not be Pareto efficient, since it would be possible to make Poor better off without making Rich worse off. This is an example of a Pareto optimal distribution that did not necessarily result from a Pareto superior move. Professor Coleman points out that Pareto optimal distributions can result from a variety of moves and that they are not necessarily Pareto comparable. Coleman, *Utility*, *supra* note 56, at 518.

71. Reinhardt, *supra* note 56, at 312. Professor Reinhardt calls this the "unrequited-punch-in-the-nose criterion of social welfare."

> Suppose, for example, that I feel very aggressive today and therefore would like to punch you in the nose. An honest referee (an economist) asks me what I would be willing to pay for that privilege. Suppose the maximum I'd be willing to pay were $1,000. Next, the honest referee asks you how much you would have to be paid to receive that punch in the nose without hitting me back. Because you are strapped for cash, you might accept the punch for $600. The referee (our economist) is ecstatic, for (s)he perceives here the opportunity to enhance *social welfare*. Consequently, the deal is struck, you kindly present your precious nose, I punch, you bleed and hold out your hand in anticipation of my payment of $1,000. Alas, I walk away happily, along with my $1,000, which I refuse to surrender. Not to worry. The honest referee (our economist) will soothe you with the expert assurance that, according to Nicholas Kaldor, and in principle, we just have witnessed a major enhancement in *social welfare*, to the tune of $400, even though the expected $1,000 bribe is not actually paid. It is to be hoped that you have enough respect for the referee to accept this verdict gracefully, and you probably will, if you accept the benefit-cost analyses typically sold by economists to policymakers.

If total utility increases, efficiency has improved.[72] Kaldor–Hicks efficiency says nothing whatsoever about the distribution of this bounty, however. Finally, Kaldor–Hicks efficiency in the economics sense refers to increases in utility (as opposed to wealth). Net increases in utility may be difficult to identify, however, because comparisons of utility across persons are close to impossible in the absence of voluntary exchanges.

A variation of Kaldor–Hicks efficiency that avoids the problem of utility comparisons is wealth maximization as a measure of efficiency. Judge Richard Posner is probably the best known and most outspoken proponent of wealth maximization as an efficiency criterion.[73] Wealth maximization is similar to Kaldor–Hicks efficiency in that compensation need only be theoretically possible and need not actually occur in order for one state of affairs to be deemed more efficient than the next.[74] Under wealth maximization, however, the most efficient allocation of resources is the one that produces the most wealth overall. Wealth in this sense is the value of goods and services determined by the price that someone is willing and able to pay for those goods.[75] The main difference between wealth maximization and Kaldor–Hicks efficiency is that wealth maximization is based on actual prices, whereas Kaldor–Hicks efficiency is based on preferences without the requirement of willingness or ability to pay.[76]

As noted above, it is difficult to measure overall increases in utility because we have no reliable way of comparing utility between the two individuals.[77] Thus it is difficult to evaluate relative gains and losses in aggregate utility. As long as trades take place voluntarily, there is no need for interpersonal comparisons, but if we wish to compare two different sets of circumstances, somehow we must be able to assign utility values to such intangible goods as leisure time and absence of stress, as well as to money.[78]

Focusing on wealth eliminates some of the problems presented by utility-based notions of efficiency. Market exchanges, by definition, produce increases

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Id. at 312–13.

72. Paradoxically, it is not always possible to determine whether a Kaldor–Hicks efficient move has produced an increase in utility. If the winners could compensate the losers only in such a way that the winners are no longer winners and the losers become winners, two states can be Kaldor–Hicks efficient to each other. It could never be said, however, that two states each provide more total utility than the other. *See* Coleman, *Utility*, *supra* note 56, at 519 n.14, for an explanation of this paradox.

73. *See generally* POSNER, *supra* note 64, at 11–12; Posner, *Utilitarianism*, *supra* note 65, at 119–35; Richard A. Posner, *The Value of Wealth: A Comment on Dworkin and Kronman*, 9 J. Legal Stud. 243 (1980) [hereinafter Posner, *Wealth*].

74. If compensation were required, wealth maximizing reallocations would be Pareto superior moves because someone would be better off by virtue of the additional wealth and no one would be worse off, since losers would receive compensation. Anthony T. Kronman, *Wealth Maximization as a Normative Principle*, 9 J. Legal Stud. 227, 238 (1980) [hereinafter Kronman, *Wealth*]. The converse is not true, however; a move could be Pareto superior but not be wealth maximizing if, for example, someone was better off in some way that no one would be willing to pay for.

75. POSNER, *supra* note 64, at 11–12; Posner, *Wealth*, *supra* note 73, at 243.

76. One might counter that prices are merely reflections of preferences. While it is true that prices are reflections of preferences, not all preferences are reflected in prices.

77. Bankman & Griffith, *supra* note 1, at 1917–18 (many consider interpersonal comparisons of utility to be meaningless).

78. For a more complete discussion of interpersonal comparisons of utility in the context of the Pareto criterion, see Coleman, *Utility*, *supra* note 56, at 515–17.

in wealth if wealth is defined in terms of prices.[79] Such exchanges may not always be Pareto superior, however, if they negatively affect non-parties without compensating them.[80] Transactions could actually cause losses in utility, yet be wealth maximizing.

2. Efficiency Objections to Progressivity

The main efficiency objection to progressivity is that high tax rates on marginal income create a disincentive to earn additional income.[81] In the case of labor, for example, a worker theoretically is faced with the choice between an additional hour of leisure or the after-tax wages of an additional hour of work. The after-tax reward for working can be thought of as a cost of the leisure.[82] As the cost of leisure goes down, demand theory says that the worker should demand or choose more leisure. Thus as the tax rate increases so that the net reward for working decreases, the worker has an incentive to work less.

A similar argument operates on other resources, such as investment funds. Here the choice is between saving and consuming.[83] The cost of present consumption is not only the dollar price of the goods consumed, but in addition includes the present value of the income stream that could have been generated with that amount. If the future after-tax return is reduced (because investment returns are subject to increasing levels of taxation), the cost of current consumption is similarly reduced.[84] At some point the potential investor may choose to take a more expensive vacation rather than making the further investment.

It is not entirely clear which type of inefficiency theorists mean when they criticize progressivity on efficiency grounds. The disincentive effects described here seem to be "inefficient," if at all, primarily in a wealth-maximizing sense.[85] Disincentives are undesirable because they result in a

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79. *See* Posner, *Utilitarianism, supra* note 65, at 120–22 (distinguishing wealth from happiness).

80. *Cf.* POSNER, *supra* note 64, at 12–13 (transactions that affect nonparties would not be Pareto optimal unless all affected nonparties were compensated).

81. *See* Blum & Kalven, *supra* note 1, at 20–21 (progressive taxation reduces incentive to produce or work); Kaplow & Shavell, *supra* note 55, at 667 ("income taxes and transfer payments distort incentives to work"). *See also* Kennedy & Michelman, *supra* note 57, at 735 n.26 (arguing that *any* tax system other than a lump-sum head tax creates distortions relative to a non-tax world). High marginal rates do not necessarily mean progressive rates, although very high marginal rates generally would be impossible under a flat rate tax. *See* Bankman & Griffith, *supra* note 1, at 1920–21 (high marginal rates produce inefficiency); Kornhauser, *supra* note 3, at 477–78 (need to distinguish between arguments about progressivity and arguments about high taxes).

82. This is, in fact, the opportunity cost of the leisure—the foregone return from the alternative use of the worker's resource (time).

83. There is a whole slough of arguments here in favor of a consumption tax instead of an income tax, or alternatively, an exemption for investment income. *But see* Barbara H. Fried, *Fairness and the Consumption Tax*, 44 STAN. L. REV. 961, 970–90 (1992) (discussing the nature of investment income).

84. Blum & Kalven, *supra* note 1, at 24–26. Higher taxes reduce the return on risky investments. The overall effect on savings and investment is difficult to estimate, however, because the motivations for saving are so complex. Blum and Kalven note that some people may actually save more at lower rates in order to reach specific savings goals. For an interesting discussion of reasons for saving and appropriate taxation of different types of savings, see McCaffery, *Hybrid, supra* note 18.

85. *See* Bankman & Griffith, *supra* note 1, at 1925 (describing efficiency costs as a percentage of tax revenue).

smaller economic pie; with less to go around, presumably everyone gets a smaller slice. At some point, the theory goes, higher taxes result in *less* tax revenue because there will be less income on which to impose the income tax.[86]

Increasing tax rates thus result in increasing government revenues to a point beyond which the tax burden becomes such a disincentive to further production that tax revenues actually fall off.[87] Regardless of the type of efficiency intended, there are two objections to this general disincentive argument on its own terms. First, it is not really an argument against progressivity, but rather against high marginal tax rates.[88] Thus, a very high flat rate (perhaps accompanied by a large exemption) would also be a disincentive and if pushed high enough would theoretically not increase revenue.

Second, the disincentive effect may not actually occur over much of the income range.[89] Upper income workers may find their motivation to work in nonmonetary considerations such as prestige and a sense of responsibility. Thus, the disincentive theory depends on the assumption that individuals generally prefer work over leisure if the pay is high enough. The validity of this assumption, however, depends on individual preferences for leisure and wealth, which may depend on how much wealth (as opposed to income) one already has.[90] Thus, to a certain extent, the predicted inefficiency of any tax system is influenced by the existing distribution of resources, at least insofar as we are concerned with the work/leisure tradeoff.[91]

In addition, lower and middle income taxpayers may not have the option of reflecting the tax rate in their work efforts because of the fixed nature of most jobs.[92] At the lower end and middle of the taxpaying income scale an opposite effect, the "income effect," may actually describe worker behavior. The income effect is the tendency of some workers to work more hours as the tax rate goes up in order to maintain a constant standard of living.[93] Similarly, savings may actually increase for some taxpayers as the after-tax return on investment decreases. Savers who are saving for a certain purpose may have

86. *See, e.g.*, Feldstein & Feenberg, *supra* note 6, at 1653 (1993) (asserting that if taxpayers reduce taxable income in response to higher rates, no additional revenue would result for the fisc). *But see* Jane G. Gravelle, *Behavioral Responses to Proposed High-Income Tax Rate Increases: An Evaluation of the Feldstein-Feenberg Study*, 59 TAX NOTES 1097, 1100 (May 24, 1993) (challenging behavioral assumptions of Feldstein & Feenberg study).

87. This is known as the "Laffer" effect and is often presented graphically as an upside-down U-shaped curve with total tax revenue on the vertical axis and tax rate on the horizontal axis. *See* DAVID G. DAVIES, UNITED STATES TAXES AND TAX POLICY 61 (1986). Many of the poorest developing countries have high tax rates and low total revenue. *Id.* at 66 (citing JUDE WANNISKI, THE WAY THE WORLD WORKS (1978)).

88. *See* Kornhauser, *supra* note 3, at 478.

89. Gravelle, *supra* note 86, at 1100 (results for labor force at large may not apply to high-income wage earners).

90. Bankman & Griffith, *supra* note 1, at 1924 (work helps determine social standing and self-esteem) (citing Gramm, *Labor, Work, and Leisure: Human Well-Being and the Optimal Allocation of Time*, 21 J. ECON. ISSUES 167, 175 (1987)); Gravelle, *supra* note 86, at 1100 (most studies find labor supply elasticity for males is negative and small).

91. Kennedy & Michelman, *supra* note 57, at 717–20.

92. DAVIES, *supra* note 87, at 68. *See* Bankman & Griffith, *supra* note 1, at 1922–23, 1926 (reviewing studies of compensated elasticity of labor; elasticity of labor generally found to be low, but higher for married women); Stein, *supra* note 8, at 388–89 n.42 (1992) (table showing hours worked at different income levels).

93. DAVIES, *supra* note 87, at 69.

specific savings goals that require consumption sacrifices when returns are lower. For example, a family saving for college tuition may find it necessary to scale back consumption if tax rates rise in order to attain a target level of savings.

The extent to which either of these phenomena actually occurs is not clear. Economists cannot really prove the extent to which an effect actually occurs since it is impossible to conduct a controlled experiment that can be replicated.[94] Anecdotal evidence, however, suggests that high tax rates do have enough of a disincentive effect to cause reductions in government revenue.[95] The exact mechanism by which this occurs is not quite clear, however. For example, one study suggested that a tax cut may lead to confidence, which, in turn, would have a positive effect on the volume of business transactions and thus incomes and tax revenue.[96]

Assuming, however that progressive taxation does discourage production, it is still not immediately clear in which sense progressive rates are inefficient. Perhaps progressive taxation is inefficient in the sense that resources are not allocated as a tax-free unregulated market would allocate them. Market allocations, as described above, are generally thought to be Pareto efficient moves. Because market transactions are voluntary, the parties presumably consider themselves better off as a result. But this does not mean that the overall allocation is absolutely efficient. The best the allocation can be is efficient *given* the initial distribution of resources and *given* the particular set of legal rules in place.[97]

Any tax is likely to be inefficient in a Pareto sense, unless the benefits each individual receives from government at least equal the taxes the individual pays. This exception is described below as the "Benefit Theory."[98] Even though taxation is involuntary, people could still be better off as a result if benefits are high enough.[99] The benefit principle is usually presented as a separate argument, however, so this is probably not the efficiency argument intended to expose progressivity as undesirable.[100] In addition, market allocations resulting under different tax regimes cannot be compared with respect to the Pareto criterion, because under any given tax regime, players will only enter into

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94. DAVIES, *supra* note 87, at 68.

95. DAVIES, *supra* note 87, at 68.

96. DAVIES, *supra* note 87, at 67–68 (citing G. Koretz, *Economic Diary*, BUS. WK. 16 (May 4, 1981)).

97. *See* Kennedy & Michelman, *supra* note 57, at 730–35. Professors Kennedy and Michelman describe a "Robinson Crusoe" economy in which each individual inhabits a desert island; once social structure is imposed, the choices each makes are different from those made in a one-person economy. Thus any society results in "distortion." In addition, what the choices are depends on the resources available on each island. *Id.*

98. *See infra* notes 166–81 and accompanying text.

99. *See* Kennedy & Michelman, *supra* note 57, at 735 n.26 (whether a tax regime is more Kaldor–Hicks efficient than another depends on interpersonal comparisons of utility) (citing RICHARD A. MUSGRAVE & PEGGY B. MUSGRAVE, PUBLIC FINANCE IN THEORY AND PRACTICE 461–77 (2d ed. 1976)).

100. *See* Kornhauser, *supra* note 3, at 484–85 & n.79 (limited government may be the actual goal of limited tax proponents). Kornhauser quotes Ronald Reagan: "individuals...must be free to control their own resources, to enjoy the fruits of their labor, and to keep what they earn, free from excessive government taxation and spending" *Id.* (citing *Exerpts from President's 1988 Legislative and Administrative Message to Congress*, 38 TAX NOTES 499 (1988)). For a philosopher's explanation of why this should be, see NOZICK, *supra* note 15, at 149–231 (discussing why only a minimal state is morally justifiable).

transactions that they believe will improve their well-being. While the tradeoffs involved may be different under varying tax schedules, it cannot be said that the tradeoffs are more "natural" under proportionate than under progressive taxation; rather, the tradeoffs are different.[101]

Another possible efficiency argument is that progressive taxation is inefficient in a Kaldor–Hicks sense of maximizing overall welfare. The claim is that progressive taxes create more disincentive to work and save than do flat taxes and that they channel resources into tax avoidance efforts. The resulting allocation of resources supposedly diverges more sharply from the non-tax free market allocation of resources than would the allocation resulting under a proportionate tax. Since the market allocation is assumed to be nearly welfare maximizing if there are no transaction costs or deficiencies of information, this changed allocation should result in less total welfare. It is possible, and even likely, however, that progressive taxation does not result in less total welfare than a flat tax, if the calculation includes the utility people derive from knowing the tax is progressive. A recent study showed that about two-thirds of taxpayers prefer a progressive rate structure.[102] Moreover, to the extent that progressive taxation allows greater reduction of income inequality there may be welfare increases even over a non-tax world.[103] The effect of a tax on total welfare, however, requires some way to compare welfare changes across individuals. Accordingly, although tax theorists may mean cost-benefit or Kaldor–Hicks efficiency when they say that progressivity is inefficient, the case for Kaldor–Hicks inefficiency is not quite convincing and may not be what is intended after all.

Finally, one could argue that progressivity is inefficient because it results in a smaller economic "pie," in other words, that it is inefficient in a wealth-maximizing sense. If, as economic theory suggests, a non-tax market results in the greatest wealth for society, any tax will be inefficient, and because progressive taxation has relatively more effect on those in a position to maximize wealth, it is probably more inefficient than proportionate taxation. If progressive taxes result in a smaller economic pie, however, this is a bad result only if a smaller pie is necessarily a bad thing.[104] Some scholars have argued that other benefits may outweigh the cost of a reduced pie. For example, if a smaller pie is the necessary cost of assuring some minimum standard of living, a smaller pie may be acceptable.[105] Introducing other values is in itself a rejection of the wealth maximization criterion, however. Thus the choice of criterion becomes a philosophical discussion rather than an economics discussion.

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101. Professors Kennedy and Michelman make this point strongly in their article of the presumptive efficiency of property and contract. *See generally* Kennedy & Michelman, *supra* note 57.

102. Roberts & Hite, *supra* note 3, at 44.

103. John Rawls, for example, believes inequality is an inherently evil state of affairs. *See generally* RAWLS, *supra* note 13.

104. Many philosophers as well as some tax scholars have questioned the benefit of a larger pie. *See, e.g.*, Kornhauser, *supra* note 3, at 482. See*infra* notes 194–281 and accompanying, text for a discussion of some philosophers' views on this question.

105. *See* Ronald Dworkin, *Is Wealth a Value?*, 9 J. LEGAL STUD. 191 (1981); Kornhauser, *supra* note 3, at 482 (quality of distribution of wealth includes non-economic values such as fairness).

3. *Values Underlying Efficiency*

What are the implications of choosing efficiency as a goal? As noted above, tax theorists who refer to efficiency seem generally to mean wealth maximization rather than utility maximization. Choosing wealth as a goal, however, implies choices about fundamental values. First, it shows a preference for exclusive private property rights[106] and for an individual's moral entitlement to whatever level of wealth, intelligence, and talent with which the individual may have been born. The wealth maximization principle seems to be strongly rooted in notions of individual liberty to do as one pleases, provided that doing so doesn't impair someone else's rights to do the same. Wealth maximization as a goal assumes that those who have wealth deserve it as a result of application of virtues such as honesty, diligence, and self-denial in combination with talent and intelligence.[107]

The implicit corollary to this deservedness assumption, however, is that those who do not manage to accumulate wealth must be deficient in these virtues.[108] Whether all opponents of progressive taxation who rely on efficiency claims embrace these beliefs is not the point. The point is that *some* beliefs about principles of right and good must support the efficiency goal, and it would be useful to know what these beliefs are.

Finally, the specific "efficient" allocation that results in a voluntary market system depends on the specific original distribution.[109] Embracing a wealth-maximizing allocation implies acceptance of this original distribution as just or right, or at least acceptable. Economics purports to make no explicit claims about whether an original distribution is to be considered just; rather, economic theory describes and predicts an outcome based on given information about the starting point.[110] Wealth maximization as a goal sometimes departs from economics in this regard, however. Judge Posner, for example, argues that the principle implies an initial distribution of individual rights to their

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106. Posner, *Utilitarianism, supra* note 65, at 125 (wealth maximization ordains creation of system of exclusive rights). Note, however, that if efficiency in the welfare maximizing sense is intended, the choice between private property and some other regime is less clear. If individual preferences enter the equation, it becomes difficult to compare the different kinds of distributions of wealth and rights that would result under a private property system and, say, a forced sharing system. *See* Kennedy & Michelman, *supra* note 57, at 734 (impossible to choose between regimes without interpersonal comparison of satisfaction).

107. *See, e.g.*, Posner, *Utilitarianism, supra* note 65, at 123 (an honest buyer's wealth was probably accumulated through honest labor); *Id.* at 128 (under wealth-maximization, one born feeble-minded has no right to resources for self support); *Id.* at 135 (wealthier people are generally those who work harder or are smarter or luckier).

108. "Moreover, the buyer's $10,000 was in all likelihood accumulated through productive activity....The thief, in contrast,...may never have done a productive act in his life." Posner, *Utilitarianism, supra* note 65, at 123 (contrasting a man willing to pay for a necklace with one who has no money, but is willing to suffer the consequences of stealing it).

See also POSNER, *supra* note 64, at 436 (plausible that people who work hard to make money are those who value it the most).

109. *See* Kennedy & Michelman, *supra* note 57, at 719 ("how much people produce [depends on]...the actual distribution of rights..."); Posner, *Utilitarianism, supra* note 65, at 108 ("where wealth effects are important, economic analysis does not predict a unique allocation of resources unless the initial assignment of rights is specified");.

110. *See* Posner, *Utilitarianism, supra* note 65, at 109 (economics contributes to the ethical debate—not by advising on rightness or wrongness, but by indicating a consequence that may be relevant).

"natural owners," those who would be likely to value them most highly.[111] Thus the productive capabilities of a genius or a super athlete *should* allow that person to maximize wealth. Redistribution of that wealth would deny the genius individual autonomy.[112] Questions of natural rights, individual autonomy, and redistribution are very much questions of philosophy and are part of a rich debate about what the answers should be. To claim that progressive taxation is inefficient and to stop there, it seems to me, begs the far more important questions about equity, some of which are discussed below.[113]

C. *Equity*

As we have noted, the third traditional criterion for income tax policy is equity, which is divided into horizontal equity and vertical equity.[114] Horizontal equity is the principle that taxpayers with the same income should pay the same tax, while vertical equity means that taxpayers with higher incomes should pay tax at higher rates. Progressivity has been criticized on both counts. Because progressivity treats taxpayers differently depending on income level, it attracts support on grounds of vertical equity as well as the criticism of those who do not hold vertical equity as a goal of tax policy. In addition, progressive taxes sometimes treat similarly situated taxpayers differently, depending on how we identify similarly situated taxpayers.

While vertical equity provides strong arguments in favor of progressivity, opponents attack these arguments as inconclusive.[115] For the sake of completeness, this section will first provide an overview of the horizontal equity issues progressivity raises. I then turn to the arguments under the rubric of vertical equity that purport to support progressivity. The vertical equity arguments are inconclusive partly because of their relationship to the playing field of economic efficiency. The economic framework for analysis is based on principles that very possibly *cannot* support progressivity. The importance of examining the very foundations of the analytical framework again becomes apparent.

1. *Horizontal Equity*

The progressive tax debate inherently involves comparisons of taxpayers who are not similarly situated. Nevertheless, progressivity may have some implications for similarly situated taxpayers depending on how we determine which taxpayers are similarly situated. Horizontal equity issues arise in at least four contexts. First, progressivity may have the effect of treating investment income differently from wage income.[116] If the recipients of the two types of

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111. Posner, *Utilitarianism, supra* note 65, at 126. *But see* Dworkin, *supra* note 105, at 191; Anthony T. Kronman, *Wealth Maximization as a Normative Principle,* 9 J. LEGAL STUD. 227 (1981) (presenting arguments that wealth maximization has nothing to say about the original distribution of rights).

112. Posner, *Utilitarianism, supra* note 65, at 129. *See also* NOZICK, *supra* note 15, at 160–61 (redistribution would also deny all those who paid the genius the autonomy to use their wealth as they see fit).

113. Posner, *Utilitarianism, supra* note 65, at 125–27.

114. MICHAEL J. GRAETZ, FEDERAL INCOME TAXATION: PRINCIPLES AND POLICIES 15 (2d ed. 1989).

115. Even proponents sometimes attack these arguments as inconclusive. *See, e.g.,* Blum & Kalven, *supra* note 1, at 35–49 (discussing benefit and equal sacrifice theories).

116. *See infra* notes 118–23 and accompanying text.

income are deemed similarly situated, this distinction between investment income and wage income taxation violates horizontal equity.[117] Second, progressivity adversely affects taxpayers whose income fluctuates from year to year relative to those with steady incomes. Third, in the past, the phenomenon of bracket creep effectively resulted in tax increases as inflation pushed salaries into higher and higher brackets. Finally, under progressive rates equal deductions have different values to taxpayers in different brackets. These issues are discussed below.

a. Savers and Spenders

Progressive taxes may exacerbate the already unequal treatment of savers and spenders. Consider two individuals who have the same earnings in year one, as well as identical expenses, except that one saves a portion of her income and the other spends all of his on movies and restaurant meals. Assuming that we are taxing accretion rather than consumption, most would agree that the taxpayers are similarly situated in year one.[118]

But in year two, when the two individuals again have equal wage earnings, the saver will have additional income from saving. Are these two taxpayers now *not* similarly situated? Saver had to forego consumption in year one in order to have savings and investment income in year two. Over the two-year time period, then, Saver and Diner arguably are similarly situated with respect to the usefulness of their income. But if we only look at year two, Saver has more income than Diner. Even under a flat tax, Saver pays more tax than Diner as a result of postponing consumption. This is the gist of the argument in favor of a consumption-based or savings-exempt tax.[119] The argument goes even further, however, because under a progressive tax, Saver would not only

117. *But see* Kornhauser, *supra* note 3, at 478, for an argument that this criticism really addresses the choice between accretion and consumption as a tax base. I think the argument does go a step further, however, and implicates progressivity as well. *See infra* discussion accompanying notes 118–23.

Savings arguments can be made in the context of efficiency as well. We start with the assumption that we do not want to encourage consumption relative to savings because saving is necessary to provide capital for development. *See* McCaffery, *Hybrid*, *supra* note 18, at 1159–64 for a summary of the economic and cultural reasons for encouraging savings. Professor Kornhauser and others have questioned the role of taxation in discouraging savings. Kornhauser, *supra* note 3, at 478 n.46 (evidence that taxation does not discourage savings as expected).

For an interesting discussion of the concept of horizontal equity generally, see Louis Kaplow, *Horizontal Equity: Measures in Search of a Principle*, 42 NAT'L TAX. J. 139 (1989) (suggesting difficulties with traditional definitions of, and considering normative bases for, horizontal equity).

118. *But see* NOZICK, *supra* note 15, at 170. Nozick asks: why should the taxpayer who earns more to go to movies pay more tax than the one who enjoys sunsets and can, therefore, get the same satisfaction from less income? Perhaps the taxpayer who consumed less and saved is better off than the one who dined and went to shows. After all she (the first taxpayer) satisfied her leisure needs and still had enough left over to purchase future consumption or security. The diner required more income just to satisfy his leisure tastes in a way that tasted good and was unable to buy future security. Problems like this of interpersonal comparisons of utility are inevitable even if taxpayers dispose of their income in identical ways. *Id.*

119. *See* Fried, *supra* note 83, at 965 (consumption tax proponents assert that consumption tax is more fair because it places more equal burdens on spenders and savers); McCaffery, *Hybrid*, *supra* note 18, at 1149–50 (income ideal for taxation can be thought of as double tax on savings).

pay more total tax, Saver would pay tax at a higher rate on the additional income in year two.

This scenario raises at least two significant tax policy questions. The first is whether to tax investment returns at all. To the extent that interest merely matches inflation, Saver's interest earnings do not afford her more consumption power in year two than she had in year one. To the extent that interest represents the time value of money,[120] Saver is merely being compensated for foregoing consumption in year one and is not really better off than Diner.[121] Arguments of this nature seem not to take into account the psychic well-being that one may derive from the knowledge that future consumption is secure.[122]

In addition, arguments based on equal treatment of spenders and savers start from the proposition that spenders and savers should be treated equally. Why this should be is not entirely clear and must certainly rest on philosophical beliefs about entitlement to wealth.[123] Nevertheless, a general discussion of the appropriateness of taxing investment income is beyond the scope of this article.

The second policy question raised by Saver and Diner involves progressivity. Assuming, for simplicity, that we agree on an accretion-type income tax, the two taxpayers above are similarly situated in year one when they have identical wage income and no other income, and they are not similarly situated in year two when Saver has investment income in addition to her salary. Under a progressive tax, Saver's interest income effectively will be taxed at a higher marginal rate than Saver's wage income. If the two taxpayers are not similarly situated, there is no issue of horizontal equity to address, since horizontal equity pertains only to similarly situated taxpayers. If we believe that the two taxpayers are similarly situated, however, progressive rates compound the effects of taxing interest by taxing it at a relatively higher rate.

b. Fluctuating Incomes

One characteristic of progressive rates that clearly does raise horizontal equity concerns is the effect of progressive rates on taxpayers whose income

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120. For a clear discussion of the elements of a transaction that give rise to interest, see Alice G. Abreu, *Distinguishing Interest from Damages: A Proposal for a New Perspective,* 40 BUFF. L. REV. 373, 398–400 (1992). Professor Abreu presents a convincing case that the analysis of interest should go beyond an amount paid "for the use or forbearance of money" and that an additional element is that interest arises from a consensual extension of credit. *Id.* at 399. *See also* Bank of America v. United States, 680 F.2d 142 (Ct. Cl. 1982) (interest typically involves credit risk, credit administration and cost of funds).

121. Of course, Saver is better off than she would have been had she not foregone consumption in year one. Assuming that her savings behavior was voluntary, the Pareto principle tells us that she expected more utility from interest plus year two consumption than she would have derived from year one consumption. See *supra* notes 54–70 and accompanying text, for a discussion of efficiency and the Pareto principle. For a thorough analysis of the traditional arguments for a tax exemption for interest, see Fried, *supra* note 83, at 967–97 (traditional argument is that utility of later consumption is equal to psychic cost of deferring consumption, but this is a narrow view of returns to savers); McCaffery, *Hybrid, supra* note 18, at 1191 (life cycle savings are a type of "longevity insurance").

122. *See* Fried, *supra* note 83, at 968. Professor Fried presents a thorough analysis of the relative wealth of Saver and Diner and also asks why a spender and saver should necessarily get the same treatment. *Id.*

123. One argument for a consumption tax is that savers should be allowed to maintain their relative pre-tax positions. For a discussion of the possible philosophical foundation for this position, see Fried, *supra* note 83, at 1006–17.

fluctuates from year to year. Economically, such a taxpayer is in the same position as one who has the same average income, but receives an equal amount each year. The taxpayer with fluctuating income pays more tax under a progressive system.[124] In years when the taxpayer has relatively high income, some of that income is taxed in higher brackets than the steady-income taxpayer ever reaches.

This effect does not render progressive taxation irretrievably inequitable, provided the tax system allows income averaging. The Internal Revenue Code did allow income averaging before 1985. During this period the highest marginal rates ranged from fifty percent to, at one point, ninety-one percent. Since 1986, however, the Code has not included an income averaging provision. The 1986 Act significantly flattened the rate structure, rendering averaging mostly unnecessary.[125] In the last few years, although some progressivity has returned to the Code, income averaging has not,[126] and the current Code does not provide for income averaging.

c. Bracket Creep

Another argument against progressive rates applies only in the absence of indexing for inflation. If brackets are not indexed, taxpayers may become victims of "bracket creep." As the taxpayer's income increases to keep up with inflation, the added dollars are taxed at higher and higher rates, although the taxpayer's real income does not increase. The tax bite becomes increasingly painful.[127]

Since 1985 the Code has included provisions for indexing of brackets so that bracket creep has not been a problem.[128] The threshold income levels for the various brackets increase each year by the same percent as the consumer price index. A taxpayer whose raises exactly keep pace with inflation continues to pay the same proportionate amount of tax. Some policy makers have recently suggested eliminating indexing, however, in order to raise revenue for health care.[129]

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124. DAVIES, *supra* note 83, at 39; Berger, *supra* note 21, at 1006 (a single-rate tax eliminates the problem of income bunching). This result may also be inefficient in the allocation-of-resources sense because it would tend to discourage activities that result in uneven income. DAVIES, *supra* note 83, at 39.

125. The 1986 Act had only two brackets—at 15% and 28%, plus a 5% surtax imposed over the middle of the income range (the "bubble").

126. The 1990 Act added a 31% bracket in addition to the 15% and 28% brackets already in place. The 1993 Act added a 36% and a 39.6% bracket.

127. *See* Berger, *supra* note 21, at 1005–06 (discussing bracket creep). Contrary to popular belief, the additional dollars need not move the taxpayer into the next higher bracket to have this effect. All of the additional dollars will be subject to tax at the taxpayer's highest marginal rate, not at the taxpayer's effective rate. As the percentage of dollars taxed at the highest rate increases, so does the effective rate. *Cf.*, Daniel J. Mitchell, *Stark Example of Taxation By Stealth*, WALL ST. J. (May 5, 1994) (erroneously stating that taxpayers just above bracket threshold would suffer no immediate adverse effect from bracket creep if indexing were repealed).

128. Economic Recovery Tax Act of 1981, Pub. L. No. 97–34. *See* I.R.C. § 1(f) (Supp. 1993).

129. Mitchell, *supra* note 127.

d. Value of Deductions to Different Taxpayers

Progressive taxation also leads to horizontal equity concerns when taxpayers are similarly situated with respect to a specific deduction but not with respect to rate bracket. A high income taxpayer thus receives a greater benefit from a deduction, say, for home mortgage interest than does a low income taxpayer.[130] For example, consider two single taxpayers, A and B. Each taxpayer pays $100 of home mortgage interest deductible under I.R.C. § 163(h)(3). Taxpayer A is in the 39.6 percent bracket. If taxpayer A could not deduct the interest, the tax on the $100 when it is received as income would be $39.60. By deducting the interest payment, taxpayer A saves $39.60 on her federal income tax. Taxpayer B, on the other hand, is in the fifteen percent bracket. If taxpayer B could not deduct the interest, the tax on the $100 would be $15. Thus, taxpayer B saves only $15 in income tax as a result of the deduction. The difference in the tax value of the deduction is a result of the progressive rate brackets.

Although A and B are not similarly situated overall, they have made identical interest payments out of otherwise taxable gross income. The unequal value of the resulting deduction is one of the arguments against using the tax system to encourage or discourage specific economic behavior.[131] Home ownership might be encouraged through direct subsidies to home buyers rather than through tax relief. A discussion of the relative merits of tax expenditures and direct subsidies is beyond the scope of this article, however. I merely note here that the unequal deduction effect results from the interaction between progressive brackets and tax expenditure provisions. Deductions necessary to arrive at an accurate measure of net income do not have the same tax benefit character as tax incentive deductions and should not be included in this criticism of progressive taxation.

2. Vertical Equity as a Criterion for Tax Policy

Vertical equity is generally assumed to "imply the desirability of progressive tax structures."[132] While progressive taxation does have a certain intuitive appeal to many, this appeal is by no means universal.[133] Even those for whom progressivity does hold this appeal, however, seem to have a difficult time articulating why they favor progressivity.[134] In their landmark article on

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130. *See* Berger, *supra* note 21, at 1007–08 (advantage of single-rate tax is even handed treatment of deductions).

131. *See* Shurtz, *supra* note 8, at 1674, 1681 (under pragmatic approach to taxation, social and economic goals should be realized through direct subsidies, not the tax system); Stanley S. Surrey, *Tax Incentives as a Device for Implementing Government Policy: A Comparison with Direct Government Expenditures*, 83 HARV. L. REV. 705 (1970) (discussing logic of using tax incentives rather than direct incentives).

132. *See* DAVIES, *supra* note 87, at 18; Beaudry, *supra* note 3, at 266 ("[O]nly a progressive tax system can achieve the political goal of vertical equity.").

133. *See* Roberts & Hite, *supra* note 3, at 30 (upper income taxpayers perceive flat rates as more fair (citing Monica D. Gerbing, *An Empirical Study of Taxpayer Perceptions of Fairness* (1988) (paper presented at the annual meeting of the American Accounting Association, August 1988, Orlando, FL))).

134. Professor Edward McCaffery notes that although references to various theories of tax equity are frequent, there is no non-controversial measure of tax equity. McCaffery, *Hybrid*, *supra* note 18, at 1164.

progressive taxation, Professors Walter Blum and Harry Kalven began with the observation that

> Like most people today [1953] we found the notion of progression immediately congenial. Upon early analysis the notion retained its attractiveness, but our curiosity as to the source of its appeal increased....It is as though those who have most clearly detected the weaknesses of various lines of analysis previously offered to support progression were under a compulsion to find some new way to justify it rather than give it up. The hunch that there must be some basis on which an idea as initially attractive as progression can be justified is stubborn indeed.[135]

This section will provide an overview of the technical arguments that Blum and Kalven and others have found not quite convincing. This material has received considerable ink elsewhere so this discussion will be relatively brief.[136] There are basically two arguments in favor of progressivity: taxation should be based on a taxpayer's "ability to pay," or it should be equal to the benefits that the taxpayer receives as a result of taxation and government. As Blum and Kalven so carefully showed, however, neither of these arguments, taken separately, is overwhelmingly persuasive, and these arguments do not adequately address the claims of proponents of efficiency-based criteria.[137] In addition, there is one fairness argument that sometimes arises in opposition to progressivity, namely, that it is a politically irresponsible formula. We will consider this argument first.

a. Political Irresponsibility

Some have raised the argument that redistribution is a politically irresponsible formula. It almost seems obvious that the more numerous non-wealthy would vote to impose higher taxes on the few wealthy.[138] In order to prevent a slippery slope of wealth confiscation, therefore, no progressivity should be allowed.[139] In addition, progressivity reduces the incentive for any in the lower-income masses to acquire wealth, since most of it will simply be taxed away.[140]

That our democracy generally does not produce steeply progressive taxes may seem surprising. One explanation is that the wealthy have disproportionate political power.[141] One scholar attributes this to fragmentation created by the structure itself.[142] Taxpayers in different sub-classes have little interest in the

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135. Blum & Kalven, *supra* note 1, at 2–3.

136. *See generally* Blum & Kalven, *supra* note 1; GALVIN & BITTKER, *supra* note 7.

137. Blum & Kalven, *supra* note 1, at 35–49.

138. Blum & Kalven, *supra* note 1, at 19 (higher rates almost certain to apply only to a minority).

139. *See* Blum & Kalven, *supra* note 1, at 20; NOZICK, *supra* note 15, at 274 (that massive redistribution is not the product of democratic voting is puzzling).

140. But note, however, that in the case of income level, membership in the majority or minority is not necessarily permanent.

141. *Cf.* RAWLS, *supra* note 13, at 277–78 (stating that one reason for progressive taxes is to level off unequal distributions of wealth that result from gifts and bequests. Such unequal distributions are undesirable because they lead to disparate political power).

142. *See* O'Kelley, *Post-Liberal*, *supra* note 22, at 734.

structure as it applies to other income levels. As a result, discontentment with the system may not solidify into any one coherent view.[143]

In ANARCHY, STATE, AND UTOPIA, Robert Nozick offers a different explanation.[144] He notes that most government programs benefit the middle class, not the poor.[145] This result follows from the fact that the top forty-nine percent will always find it less expensive to buy off the next lower two percent (so as to have a coalition of the top fifty-one percent) than to allow a coalition of the bottom fifty-one percent to form. Thus, the bottom fifty-one percent is not the only possible voting majority. In practice, in fact, this coalition-forming phenomenon plays out over a much larger middle segment, so that it is never a simple question of the top small percentage over the bottom large percentage. Nozick concludes that in a democratic society, redistributive programs will tend to benefit the middle class.[146]

b. Ability to Pay

The most frequently offered reason for progressive taxation is that it most nearly correlates tax with ability to pay. Since ability to pay is also one of the mainstays of the choice of an income tax as opposed to a consumption tax, ability to pay seems almost intuitively to be the most logical parameter for defining a rate structure.[147] Musgrave and Musgrave note, however, that ability to pay arguments have been emphasized mostly by redistribution-oriented writers.[148]

While it seems intuitively clear that taxpayers with greater income have more ability to pay taxes than taxpayers with low incomes, it is not so clear how much of the higher income should go for taxes. Tax theorists have searched for a formula that would indicate the specific rates that various taxpayers would pay. An extreme approach would be to confiscate all income above some threshold, but such confiscation would eliminate any financial incentive to produce more income.[149] Under a proportionate tax, high-income taxpayers would always pay more money in taxes than low-income taxpayers, and even under some regressive structures, high-income taxpayers could pay more dollars than low-income taxpayers, although the percentage of income

143. O'Kelley, *Post-Liberal, supra* note 22, at 734. For a different view, *see* Blum & Kalven, *supra* note 1, at 19, accepting the possibility of the majority imposing unfair burdens on a minority as one aspect of majority rule that a democracy must address head on.

144. NOZICK, *supra* note 15.

145. NOZICK, *supra* note 15, at 274–75. Nozick offers no support for his claim that lots of critics have pointed this out.

146. NOZICK, *supra* note 15, at 274–75.

147. For discussions of ability to pay as grounds for an income tax, *see* Blum & Kalven, *supra* note 1, at 64; SIMONS, *supra* note 11, at 139; Beaudry, *supra* note 3, at 247 (ability to pay is "the backbone of vertical equity"). *But see* McCaffery, *Hybrid, supra* note 18, at 1166 (political economists generally agree that a consumption tax would be preferable to an income tax).

148. MUSGRAVE & MUSGRAVE, *supra* note 58, 223 n.5. Unless taxation is based solely on the benefit principle (discussed below), all taxation is redistributive. Professor Shurtz argues that progressive taxation is warranted solely by revenue-raising concerns, i.e., it is based on ability to pay in the sense that higher income taxpayers have more potentially taxable money. *See* Shurtz, *supra* note 8, at 1690 ("[B]ecause the purpose of taxation is to raise revenue, there is no question but that an efficient income tax system should employ a progressive rate structure.").

149. The ability-to-pay argument is thus proffered against a backdrop of a market economy and is constrained by economic efficiency concerns.

would be smaller. Progressive rates are somewhere between the proportionate tax and outright confiscation.

One appealing idea is that each taxpayer should make an equal sacrifice in order to support government programs.[150] There are at least three variants of this theory.[151] One is that each taxpayer should sacrifice an equal amount of satisfaction.[152] While high income taxpayers may have higher total satisfaction than low income taxpayers, they presumably derive less satisfaction from each additional dollar. Thus, a wealthy taxpayer would have to pay more dollars than would a poor taxpayer in order for each to make the same absolute amount of sacrifice.[153] Under this version of the equal sacrifice theory, however, a wealthy taxpayer, who enjoys more total satisfaction, would sacrifice *proportionately* less satisfaction than a poor taxpayer.[154] In addition, the theory requires that we somehow measure each taxpayer's total satisfaction so that we can determine the amounts of income that would provide an equal sacrifice.[155]

A second version of the sacrifice principle would require a proportionate sacrifice from each taxpayer.[156] In this view, whatever the taxpayer's total satisfaction, the taxpayer should sacrifice some given percentage of that total.[157] Assuming again that high-income taxpayers obtain less satisfaction from each additional dollar than do low-income taxpayers, high income taxpayers would have to contribute more of their (less satisfying) dollars in order to sacrifice the same proportion of their total satisfaction.[158]

The third version of equal sacrifice requires equal marginal sacrifice. This means that for each taxpayer, after paying the tax, paying the *next* dollar would entail the same amount of sacrifice.[159] If we assume that all individuals derive the same satisfaction from money at any given income level, the equal marginal sacrifice would entail a leveling off of income so that all taxpayers would actually *be* at the same income level and would, therefore, have to make the same sacrifice to pay the next dollar.[160] In theory, at least, confiscation of all income above a chosen level would minimize the total aggregate sacrifice across all taxpayers.

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150. *See* GALVIN & BITTKER, *supra* note 7, at 35 (one of the arguments against a head tax is that it requires unequal sacrifices).

151. RICHARD A. MUSGRAVE, THE THEORY OF PUBLIC FINANCE (1959). Professor Musgrave describes three variants: equal absolute sacrifice, equal proportional sacrifice, and equal marginal sacrifice. The third of these, equal marginal sacrifice, results in confiscation of all income above some level, although in theory it minimizes the aggregate sacrifice of all individuals. *Id.* at 97. Such a levelling of income is hardly to be considered plausible (or even desirable) so the discussion here is confined to the first two versions of sacrifice theory. *See also id.* at 110 (equal marginal utility of income amounts to utilitarianism).

152. Blum & Kalven, *supra* note 1, at 41.

153. This is a very old idea. *See Mark* 12:41–44 (poor woman who contributes two small coins gives more to the treasury than wealthy contributors who give large sums).

154. *See* SIMONS, *supra* note 11, at 6.

155. Musgrave notes that no discussion of sacrifice theory is possible without such interpersonal comparisons of utility. *See* MUSGRAVE, *supra* note 151, at 102–105 (discussing aspects of the declining marginal utility of income assumption).

156. *See* Blum & Kalven, *supra* note 1, at 41.

157. *See* MUSGRAVE, *supra* note 151, at 97.

158. High-income taxpayers would continue to enjoy more total satisfaction than low-income taxpayers, however.

159. MUSGRAVE, *supra* note 151, at 97.

160. MUSGRAVE, *supra* note 151, at 97.

All three versions of the sacrifice theory depend on the principle of diminishing marginal utility of income, the assumption alluded to above that taxpayers derive less and less satisfaction from each additional dollar as they move up the income scale.[161] Economists generally accept this principle at least across a substantial part of the income range.[162] Economists find empirical justification for diminishing marginal utility of income in the consumption choices that people make as they enjoy rising levels of income.[163] At the lowest levels, people choose to satisfy basic needs. Presumably then, people derive greater satisfaction from having these needs satisfied than they would from some other form of consumption instead. For example, at a lower income I will choose to buy groceries, but I will not buy theater tickets. At a higher level, I will buy the groceries and the theater tickets. From my low-income choices, we can surmise that groceries are more important to me (provide more utility or satisfaction) than the theater.[164]

In addition, however, sacrifice theory as a basis for taxation requires a comparison of the utility that taxpayer A derives from a marginal dollar with that of taxpayer B. For example, assume that A and B have the same income, but B derives twice as much satisfaction from the income because B's income utility curve has a gentler slope than A's (although both are downward sloping). Proportionate sacrifice (say twenty percent of the total satisfaction derived from income) would require A to pay more tax than B because a greater percentage of B's satisfaction is tied up in the last few dollars.

Of course, there is no way for anyone to know who gets more satisfaction from a marginal dollar. Economists and legal scholars alike are very clear that interpersonal comparisons of utility are a dead end.[165] Accordingly, sacrifice theory depends on the simplifying assumption that everyone has the same income-utility curve.[166] More specifically, sacrifice theory requires the assumption that individual income-utility curves have identical shapes and starting points.

Some scholars have rejected diminishing marginal utility of income based on a hierarchy of preferences on the grounds that consumption preferences depend on the current distribution of wealth. Blum and Kalven, for example, note that consumption preferences change with income level and conclude that all we can meaningfully say is that at a low income, I make the consumption choices that provide me the most satisfaction then, and at a high income, I make the consumption choices that provide me the most satisfaction at that level.[167]

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161. For a clear discussion of the evidence for diminishing marginal utility of income, *see* Stein, *supra* note 8. A necessary simplifying assumption is that all individuals have the same income utility curve.

162. MUSGRAVE, *supra* note 151, at 104.

163. *See, e.g.*, Stein, *supra* note 8, at 379–81.

164. While it seems clear that marginal utility of income decreases as one moves from low, subsistence-level income to middle income, it is not so clear that marginal utility of income continues to decrease at the same rate at higher income levels. Indeed, marginal utility of income may be constant or even increase at higher income levels. MUSGRAVE, *supra* note 151, at 103.

165. *See* NOZICK, *supra* note 15, at 170–71; Posner, *Utilitarianism, supra* note 65, at 114.

166. MUSGRAVE, *supra* note 151, at 98–99 (noting that implementation of equal sacrifice requires an income-utility curve and proceeding on assumption that the same curve applies to all); MUSGRAVE & MUSGRAVE, *supra* note 58.

167. Blum & Kalven, *supra* note 1, at 60.

Another way of stating this is that people get accustomed to whatever consumption level they have. If I have a relatively high income and have become accustomed to it, asking me to then give up some percentage of it is likely to be very painful to me for a while, until I get used to a lower level of consumption, at which point I will not mind so much. Thus the sacrifice of the same number of dollars would depend on the extent to which I had come to depend on those dollars.

There are two weaknesses in this attack on diminishing marginal utility of income. First, the fact that a taxpayer may temporarily mind a whole lot when asked to give up consumption does not mean the taxpayer does not have a declining income utility curve. The appropriate comparison would be asking the taxpayer to give up consumption from a relatively higher level to which the taxpayer is accustomed, and asking the same taxpayer to give up consumption at a low level of income after becoming accustomed to that consumption.

A second problem is the notion that preferences cannot be rank ordered across income levels. One example presented is that at a low income an individual buys a used car. At a higher level, the taxpayer does not just add to the used car, but reevaluates all of the individual's needs.[168] While this is likely to be true, it is probably true that the individual will continue to maintain *some* car or form of transportation. Thus the choice to use income for transportation presumably does provide more satisfaction than the choice to have a new car rather than an old one. Or more significantly, the choice at the low income level to buy groceries was more satisfying than a choice of a new car would have been at that level. If the individual continues to buy groceries and transportation and in addition changes the form of the transportation, the individual actually does simply add on additional consumption.

Even if marginal utility of income does decrease with increases in income for each individual, however, sacrifice theory does not conclusively justify progressive taxation. Under equal absolute sacrifice or equal proportionate sacrifice, the tax structure would depend on the shape and slope of the income utility curve. If marginal utility decreases, but not as fast as income increases, the equal absolute sacrifice approach would call for a regressive tax. As the slope of the utility curve increases, the tax becomes less regressive to the point where utility decreases at the same rate that income increases. At this point the tax would be proportionate to income. Only if utility were to decrease faster than income increases would equal absolute sacrifice require a progressive tax.[169]

Under proportional sacrifice the analysis is more complicated. Proportional sacrifice calls for progressive tax only if marginal utility declines faster than average utility as income increases. The bottom line is that, as in the case of equal sacrifice, the tax structure required by proportional sacrifice depends on the slope of the income utility curve.

While the assumption that people have the same income-utility curve may be palatable, no assumption about the actual degree of slope could be

168. *See* Stein, *supra* note 8, at 376 (criticizing Blum and Kalven's example of changing preferences).

169. See MUSGRAVE, *supra* note 151, at 100–01, for an explanation and formulaic presentation of these conclusions.

justified.[170] How would one measure actual utility? In addition, if as is likely, the slope does not remain constant over the range of income, but becomes flatter as one moves into the higher income levels, equal sacrifice theory could call for a tax structure that is progressive at the bottom of the range and regressive at the top.

Thus, sacrifice theory purely on its own terms does not provide a compelling case for progressive taxation. Nevertheless, a general preference for progressive taxation persists, and equal sacrifice or ability-to-pay theory is the vehicle most often chosen to support it. This analytical framework may not be appropriate, however, if we examine its underlying premises. First, in assuming that people are to be treated equally in terms of sacrifice, we implicitly assume that people are equally entitled to all their income. So, for example, income acquired through legitimate effort, for purposes of our calculations, is treated the same as income acquired through illegal means. All income is the same in this regard because the key variable is the satisfaction derived from each dollar. The very high income of a super athlete or movie star is treated the same as the minimum-wage earnings of someone moonlighting at a fast-food stand.

Moreover, sacrifice theory treats tax merely as a burden to be shared and tries to distinguish between taxpayers based on the relative weight of the burden to each. Tax burden presumably bears no relationship to the source of income. This is not to suggest that athletes and actors do not work hard. Rather, we might disagree about the extent to which people are entitled to the proceeds of great looks or native talent. In this sense sacrifice theory, like economic efficiency, appears to be value neutral. Yet both types of analysis start from similar assumptions about entitlement to wealth, and the need to minimize the burden of tax across the board.

The preference for progressivity, however, seems to go hand in hand with beliefs about high incomes that treat them as different in kind, not just magnitude, from low incomes. These beliefs are not reflected in the sacrifice theory, which operates within the same constraints of entitlement to wealth as does economic efficiency. These beliefs and assumptions about entitlement to wealth may not be universally acceptable, however, and perhaps if they were made explicit, clear conclusions about progressivity would be possible.

c. Benefit Theory

Another possible justification for a rate structure on grounds of equity is to impose a tax that is commensurate with the benefits that the taxpayer receives from the government.[171] Taxation imposed in accordance with the benefit principle satisfies the Pareto criterion.[172] Although taxation is not voluntary, the benefit taxpayers derive from government equals the tax they give up—no one is made worse off if tax is imposed according to benefit. Taxpayers receive something they presumably would be willing to pay for and at the price they presumably would pay. The benefit theory argument for progressivity, quite simply, is that the benefit of government services provided to all is greater for

170. MUSGRAVE, *supra* note 151, at 102.
171. *See* Blum & Kalven, *supra* note 1, at 35.
172. *See* Kornhauser, *supra* note 3, at 484 (stating that benefit theory is Pareto principle in action).

those with wealth than for those without.[173] For example, if government provides police services to prevent burglaries and theft, this service is more valuable to those who have things that could be stolen, and less valuable to those with no possessions.[174] Similarly, if government creates programs or institutions to stimulate the economy or monitor its stability, this is of more benefit to those whose investments would otherwise lose value.

Even those government services targeted at the poor provide some benefit to everyone. For example, public education provides a literate work force with greater ability to understand and participate in the political process. Owners of capital are likely to benefit from a better educated labor supply, and society as a whole benefits from an educated electorate.[175] Finally, many government programs directly benefit the middle or upper middle classes. The National Park System is one example.[176]

Most tax scholars, however, do not think this type of benefit analysis adequately supports progressivity.[177] Government probably does provide more benefit to wealthier taxpayers than to poorer ones in terms of the dollar value of the benefit, but opponents of progressive taxation emphasize the impossibility of accurately measuring the extent of benefits received at various income levels.[178] Advocates of progressive taxation admit that no precise measurement of benefit is possible, but insist that the relationship between income and benefits is not inverse, i.e., that benefits rise with income. Accordingly, they argue, at least some progression is justified.[179]

It is not enough to argue, or even prove, that benefits rise with income. The benefit theory only requires progressive taxation if benefits increase *faster* than income. Proponents of progressive taxation often neglect this point.[180] It is possible that benefits received from government might increase as income increases, but at a slower rate than the increase in income. In this case, a benefit theory of taxation would require a regressive tax, but as noted above, no one

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173. J.S. Mill, however, rejected the benefit theory because he thought it would require regressivity. He believed that government was of greatest benefit to those not equipped to help or defend themselves. Blum & Kalven, *supra* note 1, at 39 & n.98 (citing J.S. MILL, PRINCIPLES OF POLITICAL ECONOMY (1848)). In addition to receiving government services, taxpayers receive a benefit to the extent the tax system confers the power to make choices regarding the imposition and incidence of the tax. *See generally*, Abreu, *supra* note 9.

174. GALVIN & BITTKER, *supra* note 7, at 49 (French Revolution suggests that government is of greater benefit to those with much to lose). In addition, police and fire protection may actually be superior in some wealthy neighborhoods. *See* Kornhauser, *supra* note 3, at 494 (citing Robert P. Inman & Daniel L. Rubinfeld, *The Judicial Pursuit of Local Fiscal Equity*, 92 HARV. L. REV. 1662, 1663 (1979)).

175. Kornhauser, *supra* note 3, at 493–94.

176. Kornhauser, *supra* note 3, at 494–95 (citing Robinson, *Who Benefits from Subsidies? Does Anyone?*, 26 POL'Y REV. 59, 61 (1983)). See *supra* notes 137–46 and accompanying text, for an explanation of why a democratic system is likely to produce government programs benefitting the middle classes.

177. *See* Kornhauser, *supra* note 3, at 491 (benefit theory in disrepute).

178. Kornhauser, *supra* note 3, at 495.

179. The fact that benefits rise with income is not enough to justify progressivity via the benefit theory, however, if benefits do not rise as fast as income. Blum and Kalven make a similar argument with respect to declining marginal utility of income in the context of sacrifice theory. *See* Blum & Kalven, *supra* note 1, at 41. Professor Kornhauser argues, however, that if feminist values of caring and community are also counted, the benefit theory provides a strong case for progressivity. Kornhauser, *supra* note 3, at 497.

180. *See, e.g.*, GALVIN & BITTKER, *supra* note 7, at 53.

suggests a regressive income tax.[181] If it were clear that benefits did rise faster than income, even most theorists now opposed to progressivity presumably would find it acceptable.[182]

If the tax imposed is greater than the benefit received, on the other hand, or if income rises faster than benefits, then a progressive tax is redistributive and proponents seem compelled to search for some other justification.[183]

The thrust of the benefit theory as a justification for progressivity thus seems to be to rescue the income tax from claims that it is redistributive. But the benefit theory, like the ability-to-pay theory, fails on its own terms as a justification for progressive taxation. If the benefit theory really is just a discredited attempt to rescue progressivity from claims that it is redistributive, perhaps we should discuss progressivity in terms of redistribution. If the analytical framework for the benefit theory includes a philosophy of wealth that absolutely precludes redistribution, how could the benefit approach possibly be expected to support progressivity if progressivity is preferred for the sake of redistribution? The benefit theory seems to be an attempt to prove a case for progressivity within the constraints of the opponents' own starting assumptions. Its failure to do so may not indicate a weak case for progressivity, but rather, a fundamental assumption that should be examined.[184] To a great extent, however, tax scholars have been reluctant to address redistribution explicitly.[185]

III. EQUITY IN LEGAL THEORY

A. *Neglect of Equity as a Criterion in Tax Policy Analysis*

Tax theorists who are willing to put considerable energy into discussion of progressivity are often unwilling to enter into debate about redistribution. Rather, they characterize the preference for progressive taxation as "purely

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181. Bankman & Griffith, *supra* note 1, at 1911–12.

182. *But see* NOZICK, *supra* note 15, at 169 (any taxation to support more than a limited government is akin to forced labor); Bankman & Griffith, *supra* note 1, at 1917 (any tax imposed on unwilling taxpayers might be unacceptable under entitlement theories of distributive justice).

183. Professor Richard Epstein advocates a flat tax because it better minimizes the mismatch between taxes and indirect benefits. EPSTEIN, *supra* note 8, at 298. Epstein equates any redistributive effect with an unconstitutional taking of property without just compensation. In the case of a highly progressive tax, "the redistributive motive is powerful evidence of redistributive effects." *Id.* (citing Michael Graetz, *To Praise the Estate Tax, Not to Bury It*, 93 YALE L.J. 259, 274–78 (1983)).

184. Professor Marjorie Kornhauser attempts to raise progressivity above the stigma of redistribution by classifying it as payment of "just debts" to others arising from a "feminist" way of viewing society that includes caring and community values. In this sense, progressive taxation is not a redistribution of wealth, she asserts. Kornhauser, *supra* note 3, at 511. Notwithstanding her claim that such a tax is not redistributive, she introduces her approach as one that "naturally supports a redistributive progressive income tax." *Id.* at 506.

185. GALVIN & BITTKER, *supra* note 7, at 152 (Galvin comment: redistribution should not be effected through the tax laws); Bankman & Griffith, *supra* note 1, at 1915 (considering theories of distributive justice in relation to the rate structure). *But see* Abramson, *supra* note 35, at 763–68 (Nozick's entitlement theory fails as an argument against redistribution); Berger, *supra* note 21, at 997 (arguing that decades of progressive rates have left income disparity intact); Kornhauser, *supra* note 3, at 506–11 (feminist theory supports redistribution); O'Kelley, *Post-Liberal*, *supra* note 22, at 21–22 (Rawls's theory of justice as fairness supports redistribution).

subjective"[186] or as based on something other than logic.[187] While this element of personal preference is not necessarily a bad thing, it generally is seen as beyond the scope of economics and thus not suitable for logical debate.

Professor Boris Bittker once noted in a defense of progressivity that in the end, decisions about the choice of a rate structure do not depend on logic, but on "faith, personal preference, or fiat."[188] It is probably true that ultimately the choice of a rate structure rests on personal preference. But the choice does follow rationally from those preferences whether those preferences lead to a wealth maximization model of economic efficiency or to some other analytical framework. Thus, it is not so much that decisions about the rate structure cannot rest on logic, only that the logical analysis of the underpinnings of these decisions is largely ignored.[189] The preference for progressive taxation, if there is such, is not itself purely subjective, but can be logically derived from some set of beliefs (which may be subjective) about how society should be ordered.

While economics purports not to make claims on grounds of equity,[190] assumptions about what is equitable are built into the economic model itself. To that extent, claims for efficiency are also claims about equity.[191] For example, the choice of wealth maximization as the good to be achieved is a choice of one social goal—a large wealth pie—over other possible social goals, such as greater equality of wealth or a guaranteed minimum standard of living. Economists and tax analysts often state or imply that there is no principled way to make this choice, yet political philosophers and legal theorists address exactly this question in very principled ways.[192]

The traditional arguments in favor of progressivity produce a case that is, at best, uneasy. Taxation according to ability to pay has some intuitive appeal, but attempts to reduce this intuition to formula fail for lack of a suitable definition of "ability." As I have noted, the ability-to-pay or equal sacrifice theories rest on the assumption that all income should be treated the same, that all dollars come with the same degree of entitlement. In this sense, sacrifice theory rests on the same ground as economic efficiency.

Similarly, the benefit theory is essentially a non-redistribution theory. It not only rests on the notion that all income is the same, but it also seeks to maintain whatever inequality already exists. In this sense, it is non-equalitarian or is, at best, equality-neutral. Thus, benefit theory, like economic efficiency

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186. DAVIES, *supra* note 87, at 272. "Although the choice is no longer as clear cut as it was a decade ago, many citizens in industrialized democracies appear to favor a progressive tax as the most equitable kind. This preference by electorates, if it still is a preference, is purely subjective. Economists are unable to defend or attack taxes and tax structure on equity grounds." *Id.*

187. Norman B. Ture, *Comment, in* INCOME REDISTRIBUTION (Colin D. Campbell ed., 1976).

188. GALVIN & BITTKER, *supra* note 7, at 28.

189. *Cf.* GALVIN & BITTKER, *supra* note 7, at 121 (it is necessary to make judgments that cannot be backed up by rigorous logic).

190. DAVIES, *supra* note 87, at 272 (economists unable to defend tax structure on grounds of equity). *See also* Demsetz, *Professor Michelman's Unnecessary and Futile Search for the Philosopher's Touchstone, in* ETHICS, ECONOMICS AND THE LAW 41, 43 (J. Roland Pennock & John W. Chapman eds., 1982) (economics contains no judgment whether efficiency is good).

191. *See* Kornhauser, *supra* note 3, at 498 (the underlying normative values are personal liberty and sanctity of private property).

192. Judge Posner actually does address these questions in response to the philosophers who take issue with his model. Posner, *Utilitarianism, supra* note 65.

theory, rests on the assumptions that each is entitled equally to all wealth honestly obtained, and that the equality or inequality that ultimately results from voluntary transfers and exchanges is of no import.

Tax theory generally has neglected the examination of these specific preferences because they are seen as matters of personal philosophy and not appropriate for debate. But what then lends the economic efficiency framework its legitimacy? Does it not also rest on philosophical choices? Of course it does. A different set of philosophical choices can also be the basis for logical thinking about distribution of wealth. For some reason, however, analysis based on different philosophical choices has mostly been rejected by the tax policy world but not by the legal theory and political philosophy world.[193]

This section examines some of the details of three philosophers' theories in an effort to explore the possible justifications for tax rate structures that could develop from different sets of philosophical choices. None of these theories is presented as *the* justification for progressivity. Rather, I hope to show that rational thinking based on different philosophical choices is possible, that it is on-going, and that it is relevant to the progressivity debate.

The first theory I consider is that presented by John Rawls in *A Theory of Justice*.[194] Next I turn to Ronald Dworkin's theory of Equality of Resources presented in his article, *What Is Equality? Part 2*.[195] The third theory is Robert Nozick's entitlement theory in *Anarchy, State, and Utopia*.[196] Finally, I return to wealth maximization as described and defended by Richard Posner.[197] These four theories share a common acceptance of and dependence on a free market system of voluntary exchanges including a high degree of individual autonomy and a system of exclusive private property rights. Nevertheless, they begin with different starting assumptions and arrive, not surprisingly, at different conclusions. The choice of these four systems is not to suggest that other, more different, systems do not merit examination.[198] One would expect that different systems of property rights and allocation of wealth would logically produce different choices about taxation. The theoretical systems I consider here are similar enough that they can masquerade as one another. Thus, a Rawlsian and a Nozickian engaged in debate may not realize how far apart they really are. It seems especially critical, then, to highlight the various possibilities that underlie current debates about such issues as health care reform and baseball salaries.[199]

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193. *But see* Bankman & Griffith, *supra* note 1, at 1925 (arguing that efficiency costs must be weighed against benefits of redistribution).

194. RAWLS, *supra* note 13.

195. Ronald Dworkin, *What Is Equality? Part 2: Equality of Resources*, 10 PHIL. & PUB. AFF. 283 (1981).

196. NOZICK, *supra* note 15.

197. Posner, *Utilitarianism*, *supra* note 65.

198. *See* Kennedy & Michelman, *supra* note 57. Professors Kennedy and Michelman challenge the starting point of private property, especially insofar as it is deemed to be more "efficient" than other property regimes. They conclude that private property is not inherently more efficient than either a state-of-nature or a forced sharing system.

199. During the early days of the Great Baseball Strike that began during the summer of 1994, the main issue in contention was a cap on player salaries. One typically heard comments to the effect that no one with such a high income has any right to be quibbling about a salary cap. On the other hand, one also heard arguments to the effect that players should be entitled to the fruits of their labor. The first argument is reasonably consistent with a Rawlsian view; the second, a Nozickian.

In other words, philosophical considerations do play a role in choosing a tax-rate structure and that role should be made explicit. Even if we cannot agree on criteria that will produce one "correct" answer, we should identify those philosophical points on which we do not agree.

As we have noted, progressive taxation has an intuitive appeal to many theorists, which seems linked to a preference for redistribution.[200] Blum & Kalven note the valiant efforts of pro-progressivists to justify on economic grounds that which they apparently hold dear on some other grounds, mostly unexplored. Particularly, the case for progression depends at least to some extent on the case for redistribution in a society.[201] The case for redistribution, however, depends on underlying theories of how wealth is and should be distributed.

B. Equalitarianism: John Rawls

John Rawls[202] starts with a presumption of an initial equal distribution of wealth, and is the most equalitarian of the four theorists considered here. Rawls derives this initial equality by reasoning deductively within the framework of analysis he presents.[203]

Rawls presents a framework for choosing the principles that guide development of a political system. Rather than emphasizing the specifics of the resulting political system, Rawls asks how a diverse society can reach a stable agreement about the characteristics of its political system.[204]

To identify these principles on which presumably all can agree, Rawls reasons from what he calls the "original position."[205] In this hypothetical

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200. See *supra* notes 132–35 and accompanying text for, a brief discussion of progressivity's intuitive appeal.

201. Progressivity is linked to redistribution assuming that a benefit theory of taxation does not justify progressivity. See *supra* notes 170–85 and accompanying text, for a discussion of the benefit theory of taxation as a justification for progressivity.

Conceivably, progressivity could be seen as necessary to fund a very limited government, such as Nozick's minimum state, because it is the only way to raise enough revenue to provide minimum benefits that (arguably) benefit all citizens equally. *See* Shurtz, *supra* note 8, at 1690–91. Such a system would still be redistributive because the wealthy would be subsidizing the police power benefit for the poor. The underlying social goal of the progressivity might not be to redistribute income, but to provide a social good in which all, even the poor, partake equally. The redistributive effect of the tax in this case would be incidental. If the cost of providing such services is such that a proportionate tax would have to be unworkably high, there may be a revenue raising motive for imposing a progressive tax based solely on where the money is. Such a motive would focus more on where money comes from than on who benefits when it is spent. This is basically the approach that Professor Nancy Shurtz takes in emphasizing the revenue raising function as the only relevant criterion. *See id.*

See also Bankman & Griffith, *supra* note 1, at 1945. Bankman and Griffith examine theoretical models of "optimal taxation" under different assumptions about individual and social welfare. They conclude that under a broad range of assumptions about the relative importance of total welfare and the distribution of that welfare, the optimal income tax would be at least somewhat progressive.

202. *See* RAWLS, *supra* note 13.

203. RAWLS, *supra* note 13, at 121 ("the argument aims...to be strictly deductive").

204. JOHN RAWLS, POLITICAL LIBERALISM (1993). Rawls recognizes that in a pluralistic society, people adhere to differing and incompatible "comprehensive doctrines." In other words, people hold different religious, philosophical, and moral beliefs. Nevertheless, to coexist in society, it is necessary to find an "overlapping consensus" on what principles we will embrace in the development of social institutions. *Id.*

205. RAWLS, *supra* note 13, at 12.

original position, individuals negotiate the principles that will guide society. Individuals in the original position represent all segments of society but they do not know what positions they, themselves, will occupy.[206] Thus they are situated behind a "veil of ignorance."[207] Because they do not know their own positions in society, the negotiators in the original position will not negotiate from specific self interest, but from a consideration of what they would consider fair if they found themselves among the worst off in the resulting society. The principles on which such individuals could agree would guide the development of the basic institutions of society.[208]

For example, Rawls reasons that individuals in such a position would agree, in the first instance, to an equal distribution of basic rights and liberties.[209] It would be unreasonable for any one individual initially to expect a greater than equal share, and irrational to accept less than equal. Thus the initial distribution of rights should be equal.[210] Similarly, there should generally be equality of economic opportunity, meaning that each would have equal access to education and culture, as well as free choice of profession. Despite this emphasis on equality, Rawls reasons that some economic inequality might be acceptable if it served to improve the lot of the worst off members of society.[211] An individual in the original position might agree to some unequal distribution if the worst off under the inequality would be better off than under an equal distribution. Rawls calls this the difference principle. If some level of inequality would not improve the condition of the worst off, the negotiators in the original position presumably would have no reason to agree on that inequality.[212]

Once the original distribution is in place, voluntary exchanges in a free market could take place to reallocate resources. One might be willing to give up some leisure time, for example, in order to have the means to buy more books. Or one might even be willing to work as a lawyer in order to live in a bigger house. Presumably, these differences in allocation of resources resulting from

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206. RAWLS, *supra* note 13, at 12, 18. Rawls asserts that in choosing principles of justice, a negotiator's own natural fortune and social circumstance should not enter into the process. Thus, he characterizes the original position as "the appropriate initial status quo." *Id.* at 12.

207. RAWLS, *supra* note 13, at 18–19, 136–37.

208. *See* RAWLS, *supra* note 13, at 14–15.

209. RAWLS, *supra* note 13, at 150.

210. RAWLS, *supra* note 13, at 150.

211. RAWLS, *supra* note 13, at 150.

212. *But see* Lawrence G. Sager, *Pareto Superiority, Consent, and Justice,* 8 HOFSTRA L. REV. 913, 920-22 (1980). Sager argues that the worst off should prefer the inequality if there is some chance of a better position but no chance of a worse one. In this sense a move to greater inequality is like a free lottery ticket—for no cost, one gets a chance to be better off. The negotiators in the original position should be willing to accept the scenario in which *someone* is better off, even if the worst off are not, because they would not hurt their possible positions in the resulting society and might improve them. Unless there is something independently valuable about a more equal distribution, the Pareto superior position should be preferable even in Rawls's original position. *Id.*

Rawls, however, is opposed to accumulations of wealth, and this would presumably extend also to unequal distributions of wealth even if the poor were not made worse off by such distributions. RAWLS, *supra* note 13, at 278.

free exchanges would be acceptable to all, provided the underlying distribution was just.[213]

One aspect of the equality upon which the bargainers in the original position would insist is equality of opportunity. By this Rawls means "equal chances of education and culture for persons similarly endowed and motivated."[214] Thus Rawls reasons that the original position would result in equality of opportunity limited by "endowment" or natural ability. But inequalities in "endowment" and motivation lead, in a free market, to inequalities in distribution of resources, an effect to which inheritance contributes. Rawls recognizes that inequalities will evolve and even welcomes some of this resulting inequality. Nevertheless, Rawls believes that too much inequality is inherently bad in its effect on social institutions. Specifically, Rawls states that social institutions that preserve equality of opportunity are "put in jeopardy when inequalities of wealth exceed a certain limit; and political liberty likewise tends to lose its value, and representative government to become such in appearance only."[215]

Rawls would rely on a transfer tax to prevent too much of this inequality of inherited wealth. He does not express an opinion, however, on how much inequality of inheritance is too much. Rather, he notes that the limit of acceptable inheritance is "a matter of political judgment guided by theory, good sense, and plain hunch...."[216] Inherited intelligence raises a similar issue. Probably there is no socially acceptable way to provide an equal starting point with respect to talent or intelligence. Accordingly, all we can do is level off the result by taxing it away.

The main purpose of Rawls's tax so far is to level wealth, i.e., it is redistributive, and no income tax has been mentioned.[217] The second purpose for a tax system, however, would be the familiar one of raising revenue, which would be needed to ensure a "social minimum."[218] Even with an underlying just distribution, it is necessary to ensure a social minimum because competitive prices do not take needs into account.[219] In a system that arises from a just distribution, Rawls would prefer a proportional expenditure tax to raise revenue because it treats everyone the same and is applied to what a person

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213. It is thus evident that the Pareto principle in particular, and free market resource allocations in general, are acceptable to Rawls, provided the starting point is equality. Along these lines, see also O'Kelley, *Rawls*, *supra* note 35, at 20.

214. RAWLS, *supra* note 13, at 275.

215. RAWLS, *supra* note 13, at 278.

216. RAWLS, *supra* note 13, at 278.

217. Professor Charles O'Kelley argues that the tax represents amounts to which the taxpayer is not morally entitled, but to which others, less privileged, are. *See* O'Kelley, *Rawls*, *supra* note 35, at 21.

218. RAWLS, *supra* note 13, at 278. Rawls assumes that government would establish certain background institutions including a social minimum, as well as freedom of conscience and political thought, and equality of opportunity in education, economic activities, and choice of occupation. *Id.* at 275.

219. Rawls's acceptance of a market structure thus conflicts with his equalitarian starting point in a second sense as well. Rawls derives a guaranteed social minimum from his underlying principle of justice, but recognizes that a market system could not maintain the minimum without intervention. The social minimum could be effected either by transfer payments or a negative income tax. RAWLS, *supra* note 13, at 275. Providing for the social minimum is necessary because "a competitive price system gives no consideration to needs and therefore it cannot be the sole device of distribution." *Id.* at 276.

takes out rather than what the person puts in.[220] Rawls provides no more analysis than this for his preference for a consumption tax.

On the other hand, Rawls admits that progressive rates may be necessary to prevent harmful accumulations of property and power. In addition, even "steeply progressive" income taxes may be appropriate, all things considered.[221] But given that progressive taxes might be appropriate, it is not clear how one decides, within Rawls's framework, whether "all things" indicate progressive income taxes.

Rawls's theory of justice is probably too general to produce a clear case for one type of taxation over another. It does, however, uncover an important starting assumption or preference; Rawls provides a reasoned case for an equal distribution as a mode. Equalitarianism is not necessarily appealing to everybody. James Tobin, for example, sneers at Rawls's criterion as having no intuitive appeal: "I doubt that the 'haves' of contemporary society would find convincing the contention that they voted for redistribution in a constitutional convention held before that random drawing of endowments of human capital and other wealth in which they were so fortunate as to become 'haves.'"[222]

But arguments such as this strengthen the case for Rawls's original position. No one would have agreed to accept a lower level than they now have, knowing what that level is. Therefore, all would have voted for the highest possible minimum (the "maximin"). All would have agreed to inequality only if it improved the position of the bottom.

Rawls begins with his original position with its veil of ignorance precisely because no privileged person would agree to be worse off than under the status quo.[223] The equalitarian starting point requires intervention in a market system. The appropriateness of that intervention, from this view, has nothing to do with economic efficiency. Rather, it is redistributive for the sake of providing for basic needs and to prevent accumulations of wealth for political reasons.

To summarize, Rawls reasons that from a "veil of ignorance" people would agree on principles of general equality with the goal of maximizing the position of those who are worst off. To the extent that some inequality results, people are entitled to that inequality as long as it does not jeopardize the very institutions developed under the equality principles.

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220. RAWLS, *supra* note 13, at 278. *See* O'Kelley, *Rawls*, *supra* note 35, at 3 (Rawls's theory justifies an income tax).

221. RAWLS, *supra* note 13, at 279.

222. James Tobin, *Considerations Regarding Taxation and Inequality*, *in* INCOME REDISTRIBUTION 127 (Colin D. Campbell ed., 1976). *But see* O'Kelley, *Rawls*, *supra* note 35, at 21. Many would agree that the purpose of the income tax is to extract from a taxpayer the portion of pre-tax income to which the taxpayer is not morally entitled. *Id.* This notion of moral entitlement to income is one of the foundations of Dworkin's approach to distributive justice. See *infra* notes 229–43 and accompanying text, for a summary of Dworkin's reasoning in favor of a progressive tax.

223. Richard Posner, however, says that Rawls's conclusions about what the negotiators in the original position would have agreed to depends on assumptions about relative levels of risk aversion. Rawls assumes people are risk averse and would refuse to risk a very low level even for the possibility of getting a high level. Posner, *Utilitarianism*, *supra* note 65, at 118–19. Because of the need for assumptions regarding personal income utility and risk aversion, Rawls's theory suffers from the infirmity of indefiniteness, in Posner's view. *Id.*

Any system developed under Rawls's principles, then, would require constant "correction" to maintain the ideals of equality. Some of this correction would come in the form of wealth transfer taxes and progressive income taxes. That such "correction" might reduce the overall size of the economic pie is not such a concern for Rawls because the main goal is not a maximum pie overall, but maximum slices for those at the bottom. This "maximin" is not chosen as a goal because we feel sorry for those at the bottom or because we think that wealth is undeserved, but because it seems logical that as a matter of social contract, people in the original position would agree to such an arrangement in order to improve their own worst case scenarios.

C. Distinctions Among Types of Wealth: Ronald Dworkin

Ronald Dworkin also incorporates the role of self interest in improving one's own worst-case scenario in his theory of equality of resources. Dworkin believes his theory justifies progressive taxes, but he does not rely on any of the traditional tax policy grounds.[224] Like Rawls, Dworkin starts from a fair original distribution of resources. Dworkin begins by employing an envy test to hypothesize this equal initial distribution of resources. Under the envy test, a distribution of resources is fair if no individual would prefer another individual's bundle of resources.[225] Because people have different preferences, an even division of specific resources might achieve this result, but still be unsatisfactory to some individuals.[226] Dworkin embraces the workings of a free market to allow people to trade until each prefers the bundle of resources that he or she ends up with to anyone else's bundle or to any other bundle attainable through trading.[227] The market thus facilitates satisfaction of the envy test and has the added virtue of measuring the amount of each individual's resources in terms of the importance of those resources to other people.[228]

The initial equal distribution would not satisfy the envy test for long, however, because some people would work hard to produce a maximum amount of the things that other people value most, while others would not be willing to make that same effort.[229] Soon some people would have larger bundles of resources than others and a snapshot at this later point would show some people owning bundles of resources that others would prefer to their own.[230] This effect is acceptable, however, if we look at the resources devoted

224. Dworkin, *supra* note 195. Dworkin describes his ideas about equality in two articles. In the first, he discusses theories of equality based on welfare and rejects these theories. *See* Ronald Dworkin, *What is Equality? Part 1: Equality of Welfare,* 10 PHIL. & PUB. AFF. 185 (1981). In the second article, Dworkin describes his theory of Equality of Resources. Because Dworkin endorses this theory and aspects of it are apparent in some of his other writings, the Equality of Resources theory will be the focus of this section. *See also* STEPHEN GUEST, RONALD DWORKIN 254–87 (1991).

225. Dworkin, *supra* note 195, at 285. Dworkin reasons from the situation of a group of shipwreck survivors who must start from scratch on an uninhabited island with abundant resources but no hope of rescue. *Id.*

226. Dworkin, *supra* note 195, at 285–86.

227. Specifically, Dworkin suggests an auction where each participant starts with the same amount of purchasing power (measured by clamshells or whatever is available). Dworkin, *supra* note 195, at 286.

228. Dworkin, *supra* note 195, at 288.

229. Dworkin, *supra* note 195, at 292–93.

230. Rawls acknowledges this same distributional instability and finds in it a justification for redistributive taxes. *See* RAWLS, *supra* note 13, at 278. Nozick notes that no patterned

to an individual over the individual's lifetime and include in the package the kind of lifestyle the individual has chosen. Thus if everyone has the same amount of talent for producing what others value, differences in accumulation would be due entirely to ambition. I may prefer my neighbor's bundle of material resources but not be willing to live the life that would be necessary to accumulate that bundle.[231] On the whole, then, I do not really prefer my neighbor's circumstances, since if I did, I could obtain the same bundle for myself.[232]

The analysis is different, however, for differences in accumulation that spring from handicap, lack of talent, or what Dworkin terms "brute bad luck."[233] Dworkin invokes a hypothetical insurance market to spread the risk of these misfortunes in a way that does not destroy equality of resources. If in each case we imagine that insurance is available and we can calculate the average level of insurance that people would buy, we can posit a tax scheme whereby we would exact "premiums" as tax and would compensate victims of misfortunes up to the insured level of resources.[234]

In the case of differing incomes resulting from differences in talent, Dworkin provides somewhat more detail as to how this scheme would work. First, he notes that commercial insurance is a financially bad deal because insurance companies would not be able to exactly cover the risks they insure and meet their administrative costs if the insurance they offered were not a financially bad deal.[235] The reason people buy insurance anyway is that they are risk averse, which is just another way of saying that people have diminishing marginal utilities of money.[236] For example, if Dworkin owns a house worth $50,000 and there is a ten percent chance of the house being destroyed by fire, that risk may be said to cost $5,000.[237] In other words, without insurance the value of the house is only $45,000.[238] Assume that insurance against this risk is $6,000. This is a bad deal financially, but Dworkin would most likely enter into

distribution (such as the initial equal distribution) could ever be stable for long. NOZICK, *supra* note 15, at 168.

231. Dworkin, *supra* note 195, at 306.

232. The revised envy test "requires that no one envy the bundle of occupation and resources at the disposal of anyone else over time, though someone may envy another's bundle at any particular time." Dworkin, *supra* note 195, at 306.

233. Dworkin distinguishes between "option luck" and "brute luck." Option luck is what causes some calculated risks to succeed and others to fail. Different outcomes based on option luck do not destroy equality of resources if the value of the outcome of a risk is weighted by the likelihood of the outcome. In other words, the risk is taken into account since it is a voluntary risk.

Brute luck, on the other hand, is the kind of outcome that no one voluntarily risks—outcomes such as being struck by lightning or suddenly going blind. Insurance, according to Dworkin, can link these two kinds of luck. If insurance is available against brute bad luck, then failing to purchase such insurance is similar to entering into a calculated risk, and the result is converted from brute luck to option luck. Dworkin, *supra* note 195, at 293.

234. Dworkin, *supra* note 195, at 298 (compensation for handicaps), 313 (talent).

235. Dworkin, *supra* note 195, at 318.

236. Dworkin, *supra* note 195, at 318. *See also* POSNER, *supra* note 64, at 11 (popularity of insurance is evidence of risk aversion).

237. The magnitude of the potential outcome times the likelihood of its occurring—in this case, the $50,000 loss times the 10% risk (or .10) is $5,000.

238. If Dworkin owned 10 houses each worth $50,000, for a total value of $500,000, and could predict with certainty that one would be destroyed by fire, he would be left with $450,000. Each house is thus worth $45,000 when the risk of its being destroyed by fire is considered.

it anyway. The reason is that the $6,000 skimmed off the top of his income is not nearly as painful as the loss of the house would be. In fact, the loss of the house would be at least nine times as bad as the $6,000,[239] so from a *welfare* perspective, Dworkin is not willing to risk this loss.[240]

Second, under an insurance scheme, we would again figure out an average level of coverage that people would purchase if there were actually such an insurance market. Dworkin reasons that no one would buy insurance for a really high income level, even though such a contract might initially seem attractive. The premium for such an income would be so high that the actual increase in income level for people who are not talented enough to earn at that level would be slight.[241] The increase would be slight because most of it would go to cover the premiums. People who actually could earn at the high level, however, would be much worse off having bought the insurance than they would have been without it. They would have to use a big chunk of their high income to pay the premiums and would probably have to work full-time at their highest income potential. In effect, they would become slaves to their insurance premiums for insurance that might have paid only a small return had they not turned out to be so talented. Dworkin concludes that people would not purchase insurance for a high level of income.[242]

People would, however, purchase insurance for a much lower level. The premiums would not be all that much because the likelihood of anyone not being able to earn the covered level would be slight.[243] In addition, presumably there would be many choices of occupation that would earn enough to cover the lower premiums for those who did earn enough, leaving them with much more freedom of choice about how to earn a living.[244]

Dworkin suggests that the average income level should be chosen and the insurance "premiums" should be paid by a progressive income tax.[245] He starts with the premise that it would seem unfair to require poor and rich to pay the same premium rate.[246] Dworkin does not make clear whether he intends "rate" to mean absolute premium amount or some percentage of income.[247] He suggests that because people have diminishing marginal utility of income, they would be willing to pay a progressive income tax for this talent insurance. Insurance companies would accept it if it raised more money than the "flat-rate premium."

239. The potential loss of the house is worse than the certain loss of a premium. The negative value of the loss for someone who is risk averse is more than the potential outcome multiplied by its probability.

240. Dworkin, *supra* note 195, at 318–19.

241. Thus there is a high probability of a small reward. Dworkin, *supra* note 195, at 320.

242. Dworkin, *supra* note 195, at 320.

243. Dworkin, *supra* note 195, at 321.

244. Dworkin, *supra* note 195, at 322.

245. Dworkin, *supra* note 195, at 323–24.

246. Dworkin, *supra* note 195, at 324.

247. Dworkin seems to equate "flat rate" with "the same tax." He explains: "it seems unfair that everyone, rich and poor alike, should pay *the same tax*, but this would seem to be the consequence of modeling tax rates on hypothetical premiums." Dworkin, *supra* note 195, at 324 (emphasis added). "For suppose the insurance firms had offered, in place of the *flat rate premium* for a given coverage...a premium fixed as an increasing percentage of the income the policy owner turns out to earn." *Id.*

I do not take Dworkin's argument to make a strong case for nominal progressive taxation. First, as we have seen, the mere fact of diminishing marginal utility of income does not justify a progressive rate structure by itself.[248] Only if utility of income declines faster than income increases would progressive rates be warranted under what appears to be another version of the sacrifice theory represented as a willingness to pay for insurance. Second, Dworkin argues that the premium for lower levels of coverage would drop off faster than the level of coverage. Conversely, as the covered income level increases, the premium would increase faster. Since the premium is the tax amount, this would call for a progressive tax rate. But is it true that the premium would increase faster than the rate of coverage? Since Dworkin presents no analysis of actual insurance premium structures, it is hard to evaluate this claim.

Even though Dworkin's answer to the question of progressive taxation is not particularly helpful, his theory is useful in this regard on other grounds. Dworkin presents a cohesive theory of when inequalities of income and wealth might be "fair." Unlike the traditional ability-to-pay or sacrifice theory which treats all income alike, Dworkin's equality of resources theory makes a distinction between above average (or below average) income resulting from differences in ambition, and similar differences in income resulting from differences in endowment or luck. While it may be difficult to actually draw a line between these two types of individual differences, Dworkin's theory at least provides a logical theoretical distinction that seems to resolve the tension between equalitarian fair start preferences and market-based incentive preferences. We might say along with Dworkin that a distribution of resources is unfair if it could not have developed from an initial equal division of resources in a system including income insurance.[249]

Dworkin admits that this starting point of an initial equal distribution is an assumption about equality. If we agree with this assumption, however, Dworkin provides a logical analysis of why we should accept inequality that springs from differences in ambition but not from differences in talent.[250] If we accept Dworkin's analysis and endorse his view that differences in talent should not lead to differences in accumulation, we have a reasoned argument in favor of some redistribution of income.[251]

On the other hand, we may agree that inequality should be allowed to arise from differences in ambition and that the only justification, therefore, for confiscating some portion of one's income is to collect "premiums" for insurance against lack of talent, or some other form of brute bad luck. If we can show that neither the insurance premium model nor diminishing marginal

248. See *supra* notes 161–68 and accompanying text, for a discussion of the diminishing marginal utility of income.

249. *Cf.* O'Kelley, *Rawls, supra* note 35, at 3 (starting distribution must be just).

250. Robert Nozick does not specifically disagree that such a distribution might be just, but he would consider other possible original distributions just as well. Specifically, Nozick would consider an original distribution as just if all of the holdings in that distribution were acquired in just ways. While Nozick is not specific about what would be considered just in this regard, he is clear that it does not include theft, fraud, etc. Whether or not these justly acquired holdings are equal is irrelevant to Nozick's theory, which focuses on the process by which holdings come to be held and not on the resulting pattern of distribution.

251. And a better-reasoned version of the argument that baseball players should not be so greedy.

utility of income justifies graduated premium rates, however, we might conclude that progressive taxation cannot be justified.

D. Entitlement to Wealth: Robert Nozick

Robert Nozick presents a theory that neither starts with equality nor discriminates between income attributable to different kinds of characteristics. Rather, Nozick starts with the premise that individuals are entitled to do as they please with any wealth acquired through just means even if their choices lead to large inequalities of distribution.[252] Because people are entitled to their wealth, the only legitimate role for government is a very limited one, and redistribution of wealth generally is not part of that role.

Nozick reasons from a so-called "natural state" in which there is no government and each person uses whatever means are available to obtain desired goods and services.[253] A very limited government would evolve "naturally" in such a state. People would form protective associations by common agreement, resulting in (or justifying) a very limited state. In this rudimentary state, people would be entitled to whatever they manage to acquire.[254] Thus Nozick's starting point is entitlement to acquisitions, and he asserts that no claim of justice could be made against such original holdings.[255]

From this original acquisition of goods and services that is not necessarily equal but is not unjust, Nozick develops a theory based on two principles:

(1) A person who acquires a holding in accordance with the principle of justice in acquisition is entitled to that holding.[256]

(2) A person who acquires a holding in accordance with the principle of justice in transfer, from someone else entitled to the holding, is entitled to the holding.[257]

Holdings that arise through applications of these two principles, and only such holdings, are just holdings, and if all holdings are just holdings, then the whole distribution of holdings is just.[258]

Nozick's purpose in starting with an original distribution that may or may not be equal is to distinguish his theory from what he terms "patterned principles of distributive justice."[259] Patterned principles can be expressed with a formula: "to each according to his moral merit, or needs, or marginal

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252. NOZICK, *supra* note 15.

253. NOZICK, *supra* note 15, at 7–25.

254. NOZICK, *supra* note 15, at 185 (in "social non-cooperation" individuals deserve what they get through their own efforts; no claim of justice can be made against such holdings).

255. NOZICK, *supra* note 15, at 185. *But see* O'Kelley, *Rawls, supra* note 35, at 32 (arguing that negotiators in Rawls's original position would never arrive at such a system of "natural liberty"; rather, only "those who hold, and cherish privileged positions" would be able to imagine agreeing to such a system).

256. Nozick does not develop the principle of justice in acquisition, but notes that it would involve working out complicated issues of what "unheld" things come to be held and how. NOZICK, *supra* note 15, at 150.

257. The topic of transfers would also involve "complicated truth," which Nozick does not attempt to develop, except to note that it would include "descriptions of voluntary exchange, and gift and (on the other hand) fraud." NOZICK, *supra* note 15, at 150–51.

258. NOZICK, *supra* note 15, at 151.

259. NOZICK, *supra* note 15, at 156.

product, or how hard he tries, or the weighted sum of the foregoing, and so on."[260]

Patterned distributions are unjust in Nozick's view because they do not give people the right to choose what to do with their holdings.[261] Thus, in addition to a "state of nature" rule that says I am entitled to whatever I get my hands on, the theory of entitlement rests on a notion of private property rights that includes the right to do whatever I want with my holdings. One thing I might want to do with my holdings is give them away. Perhaps I wish to give a small portion of my holdings to Yo Yo Ma to hear him play his cello. Perhaps a large number of people do the same thing and, as a result, Yo Yo Ma becomes wealthy.[262] If we say that the Maestro is not entitled to all of the wealth he might accumulate, we must recognize that we are limiting the freedom of others to give it to him. We are not recognizing their rights to do as they wish with their holdings.[263]

In fact, no patterned distribution would be stable if people are allowed to give their holdings to whomever they please. Thus, if we allow people to own their wealth in the sense that they can give it to whom they please, unequal distribution will result that will not be the result of ambition, hard work, honesty, etc. (whatever characteristics the reigning end-state result considers to be a just foundation for disparities in wealth distribution).

Because the right to dispose of one's holdings is an important part of Nozick's theory of entitlement, Nozick is willing to tolerate discrepancies in inherited wealth as well as in talent-based wealth. A couple might prefer to use their accumulated holdings in order to ease the way for their children.[264]

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260. NOZICK, *supra* note 15, at 156–57. Distribution according to the benefit to others, Nozick sees as a "major patterned strand in a free capitalist society," although it does not describe the whole system. More specifically, "in a capitalist society people often transfer holdings to others in accordance with how much they perceive these others benefiting them." *Id.* at 159.

261. NOZICK, *supra* note 15, at 167.

262. Nozick's example is Wilt Chamberlain. If a large number of people each pay 25 cents on top of the regular price of a basketball ticket, and the 25 cents goes to Wilt, he might become very wealthy. NOZICK, *supra* note 15, at 161–63.

I chose a classical music example because, although many people seem to find it offensive that athletes become wealthy because of talent combined with hard work, very few express this sentiment about classical musicians. (Perhaps no classical musicians become very wealthy.) In addition, this example makes more sense to me personally. I might feel that I have the right to pay a nominal amount on top of the normal price of an orchestra ticket in order to hear Yo Yo Ma, but I would not pay 25 cents (or any other price) to see Wilt Chamberlain. (No offense to Mr. Chamberlain intended.)

263. NOZICK, *supra* note 15, at 167.

264. NOZICK, *supra* note 15. Nozick criticizes patterned principles because they do not allow people to "choose to pursue an end involving...the enhancement of another's position." *Id.*

This focus on an individual's right to dispose of wealth rather than on each individual's right to have wealth in the first place also leads Nozick to criticize patterned principles because they cannot account for disposition of wealth within a family. Consider, for example, a family with three average kids and a musical prodigy. Are the parents wrong to devote a disproportionate amount of their wealth to lessons with a violin master in order to develop the young musician's talent? We might find no fault with the unequal distribution of wealth in this family. Yet the resulting distribution would not necessarily conform to the patterned distribution with which the parents started.

Rawls's difference principle is also problematic from this perspective. See *supra* notes 211–12 and accompanying text, for a discussion of the difference principle. Does the difference

In addition, in Nozick's view, individuals are entitled to any holdings that result from their superior talent or intelligence. To justify the view that people are not so entitled, one would have to start with the premise that holdings should be equal unless there is some moral reason for them not to be.[265] Nozick questions this starting point. Why, he asks, should holdings be equal, or follow any other pattern, for that matter?[266] An argument that starts with equality as an assumption cannot be used to justify intervention to create greater equality than results from the actual distribution of natural assets.[267]

Nozick's focus on the equality assumption serves to illuminate a basic difference between his entitlement theory and some of the other theories of distributive justice. Nozick's theory does not start with a premise that holdings should be equal, only that they should be acquired in just ways. From this focus on just acquisition, there is nothing troubling about the outcome of an argument that does not have equality (or increased equality) as a goal.

The Kaldor–Hicks version of economic efficiency,[268] for example, may be obtained by a series of exchanges that result in great inequality, provided the

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principle mean that the family above should only pay for music lessons if nurturing the prodigy's talent somehow improves the position of the least talented child? Or, to take a more common example, if only one of a family's several children is academically inclined, should the family refuse to pay college tuition for that child simply because the option is not available to all of the children? Nozick argues that if the difference principle (or any other patterned principle) could not apply in a family where people love each other, it should not apply in society as a whole. NOZICK, *supra* note 15, at 167.

Of course, one response to Nozick might be that he is defining "benefit" too narrowly. In a family where people love each other, perhaps each does benefit from seeing the others achieve their goals. It could be that sending one child to college or helping one child to develop musical talents does improve the position of the least talented or least intelligent. In this regard, see Kornhauser, *supra* note 3, at 508–11.

265. Nozick considers several forms of argument for the conclusion that people are not entitled to differences in holdings arising from differences in natural assets. NOZICK, *supra* note 15, at 216–24. His rejection of the proof beginning with equality of holdings is the only one we will consider here because it is grounded on the most fundamental challenge to most other notions of distributive justice. Specifically, the argument to be considered takes the following form:

> 1. Holdings ought to be equal, unless there is a (weighty) moral reason why they ought to be unequal.
> 2. People do not deserve the ways in which they differ from other persons in natural assets; there is no moral reason why people ought to differ in natural assets.
> 3. If there is no moral reason why people differ in certain traits, then their actually differing in these traits does not provide, and cannot give rise to, a moral reason why they should differ in other traits (for example in holdings).
>
> Therefore,
> 4. People's differing in natural assets is not a reason why holdings ought to be unequal.
> 5. People's holdings ought to be equal unless there is some other moral reason (such as, for example, raising the position of those worst off) why their holdings ought to be unequal.

Id. at 222.

266. NOZICK, *supra* note 15, at 223.

267. Nozick criticizes Rawls's original position on similar grounds. Rawls's original position is designed to nullify the effects of natural assets. Rawls then reasons that people in the original position would reject any principle that had the effect of distributing wealth according to natural assets (unless such system satisfied the difference principle, of course). NOZICK, *supra* note 15, at 215 (citing RAWLS, *supra* note 13, at 15).

268. *See supra* notes 71–72 and accompanying text.

overall pie increases. Similarly, the benefit theory[269] leaves overall wealth unchanged since people pay tax equal to the benefit they receive.Thus, a philosophy such as Nozick's that does not require equality might more logically support some of the analytical tools traditionally employed in the progressive tax debate than would a starting point that does require equality.

Nozick challenges Rawls's theory because it is an "end-result principle."[270] A patterned end-result principle is one that looks around at the actual distribution at some point in time and pronounces it just or unjust without regard to how it came to be that way.[271] In other words, the pattern, rather than the history of the distribution, is what matters. The problem is that, as noted above, no acceptable end-result pattern would be a stable one if people are allowed to make choices about the disposition of their property. Rawls, of course, recognizes this instability and advocates taxes that would reduce the level of inequality even if that inequality develops legitimately.

Under Nozick's theory, on the other hand, people are entitled to their natural assets. In addition, provided there is no injustice in the transfer or acquisition of holdings, people are entitled to the resulting holdings, however unequal. Nozick's purpose for probing this subject is to determine whether there is a justification for a state "more extensive than the minimal state" based on distributive justice.[272] Essentially, Nozick generally finds no moral justification for redistribution to support more than the most minimal state.[273]

Nozick does make an exception, however, for redistribution to rectify injustice in the prior acquisition or transfer of holdings.[274] While Nozick does not attempt to specify the circumstances that would constitute rectifiable injustice, he raises numerous questions about how one might determine the effects of prior injustices, how far back we should go to clean the slate, what happens if the direct parties are no longer involved, and what victims might do to bring about rectification. Nozick proceeds on the assumption that a complete principle of rectification could be developed that would address these questions.[275]

Under the principle of rectification of injustice, Nozick would allow some redistribution if we assume "(1) that victims of injustice generally do worse than they otherwise would and (2) that those from the least well-off group in the society have the highest probabilities of being the (descendants of) victims of the most serious injustice who are owed compensation by those who benefited from the injustices (assumed to be those better off, though sometimes the perpetrators will be others in the worst-off group)...."[276] Nozick cautiously allows that a rough rule of thumb might justify a principle that would maximize the position of the worst off. Indeed, Nozick makes the very strong statement that his entitlement theory should not be used to condemn transfer payments

269. *See supra* notes 171–85 and accompanying text.
270. NOZICK, *supra* note 15, at 198–99.
271. NOZICK, *supra* note 15, at 156–57.
272. NOZICK, *supra* note 15, at 149, 230.
273. NOZICK, *supra* note 15, at 230–31.
274. Holdings that are acquired or transferred by stealing, fraud, enslavement, or forcible exclusion from competition are impermissible under the principle of justice in transfer. NOZICK, *supra* note 15, at 152.
275. NOZICK, *supra* note 15, at 152–53.
276. NOZICK, *supra* note 15, at 230–31.

unless the system of payments *could not* be based on considerations of rectification of justice.[277] In the short term, then, past injustices might justify a "more extensive state" along with the redistribution such a state would imply.[278]

Nozick also does not agree with Rawls and Dworkin on the desirability of providing some social minimum.[279] The argument in favor of making such provision, according to Nozick, does not address the question of whether the things to be so provided already belong to someone else or "whether they come already tied to people who have entitlements over them...."[280]

The difference then between Nozick's theory at the most basic level and Rawls's theory at the most basic level, is that Nozick believes that what Dworkin considers "luck" is something to which people are [morally] entitled. Whatever the initial draw of the cards, government is not called upon to try to change it. Rawls and Dworkin, on the other hand, believe fundamentally in some sort of equality as a desirable starting point, and in the role of government to maintain some semblance of that initial equality.

The question is not whether Nozick's theory logically denounces progressive taxation. In fact, Nozick's theory logically disallows almost all taxation.[281] But Nozick's theory of entitlement serves to highlight some of the most fundamental assumptions about property rights on which the framework within which we argue about the rate structure must rest. Specifically, should the starting point be equal holdings? Should "holdings" imply a right to give as much as we wish to whomever we wish secure in the belief that no one will undo our gifts? In other words, is our focus on how we can dispose of our wealth? or on relatively how much each of us receives? Do we agree with Nozick that redistribution is appropriate only to rectify injustice? If so, do we agree as to what qualifies as injustice?

If the case for or against progressive taxation boils down to an underlying theoretical bias toward entitlement on the one hand or equality on the other, the debate should proceed on these terms. Voters should have the means of ascertaining whether their elected representatives agree with them on fundamental values such as these. The debate as it has been conducted has generally served to mask these underlying theories.

IV. WEALTH MAXIMIZATION REVISITED

Judge Posner has argued that wealth maximization can be viewed as a normative theory with as much appeal as other normative theories. A significant difference, however, between wealth maximization and the three theories we have just reviewed is that the wealth maximization principle is imposed on some, presumably preexisting, distribution of resources, whereas the other three all start from some state in which resources have not yet been distributed, and they build from there. Wealth maximization thus does not

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277. NOZICK, *supra* note 15, at 231.
278. NOZICK, *supra* note 15, at 230–31.
279. NOZICK, *supra* note 15, at 233–34 (citing Bernard Williams, *The Idea of Equality*, in PHILOSOPHY, POLITICS, AND SOCIETY, 2D SER. 110–31 (Peter Laslett & W.G. Runciman eds., 1962), *reprinted in* MORAL CONCEPTS (Joel Feinberg ed., 1969)).
280. NOZICK, *supra* note 15, at 235.
281. Nozick equates taxation of earnings with forced labor, arguing that taking five hours' worth of earnings is like requiring five extra hours of labor. NOZICK, *supra* note 15, at 169.

provide the same kind of ground-up analysis that starts with fundamental beliefs and then develops a system of analysis.

Yet wealth maximization, as we touched upon in Part II, must also rest on certain philosophical beliefs. For example, in his defense of wealth maximization, Posner argues that it respects differences in individual productive capacities.[282] Posner criticizes Rawls because the initial position of the negotiators does not adequately respect these differences. Presumably Posner would level the same complaint against Dworkin's initial auction and insurance mechanism.[283] Thus Posner, like Nozick, apparently believes that individuals should be entitled to whatever proceeds they are able to derive from their natural attributes.[284] And like Nozick, Posner objects to most forms of redistribution because it "impairs the autonomy of those from whom redistribution is made."[285] Thus, wealth maximization has a systematic bias in favor of the status quo.[286]

The extent to which individuals deserve to keep the proceeds derived from differences in natural attributes is a point about which theorists can (and do) disagree. In addition, it is a point that can result in diametrically opposed views, logically derived, about progressive taxation.

While most of the arguments about allocation of tax burdens are framed in terms of a version of economics that includes maximization of wealth,[287] this paper asks the question why only economics should have a voice in this discussion.[288] Economists generally claim not to be discussing issues of equity. Rather, they describe certain effects given some assumptions about how the world works. When normative claims are made on the basis of economics, however, it is because, at some level, the policy maker believes the described effect is more important than other effects outside the reach of economists' equations.[289] As we have seen, economic analysis, particularly when based on wealth maximization, rests on philosophical beliefs about how society should be ordered.[290]

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282. Richard A. Posner, *The Value of Wealth*, 9 J. LEGAL STUD. 243, 251 (1981).

283. Although Posner cites Dworkin's specific criticisms of wealth maximization, Posner does not mention Dworkin's Equality of Resources theory. *Id.* at 243 (citing Ronald Dworkin, *Is Wealth a Value*, 9 J. LEGAL STUD. 191 (1980)).

284. *See* Posner, *Utilitarianism*, *supra* note 65, at 128 ("To treat the inventor and the idiot equally so far as their moral claim to command over valuable resources is concerned does not take the differences between persons seriously").

285. Posner, *Utilitarianism*, *supra* note 65, at 128.

286. Morton J. Horwitz, *Law and Economics: Science or Politics?*, 8 HOFSTRA L. REV. 905, 906 (1980). *See also* NOZICK, *supra* note 15, at 186–87. Nozick asks whether it is not enough that people make voluntary exchanges at mutually acceptable ratios. "Why isn't the appropriate (a not inappropriate) set of holdings just the one which *actually occurs* via this process of mutually-agreed-to exchanges whereby people choose to give to others what they are entitled to give or hold?" *Id.*

287. Kornhauser, *supra* note 3, at 481 (citing Manuel H. Johnson, *President Reagan's Modified Flat Tax: Analysis & Comparison*, 5 CATO J. 499 (1985)).

288. *See* Horwitz, *supra* note 286, at 905 (the "attraction of efficiency analysis" is the "promise of a single scientific right answer"). *See also* Kornhauser, *supra* note 3, at 469 (citing Donald N. McCloskey, *The Rhetoric of Law and Economics*, 86 MICH. L. REV. 752 (1988)).

289. *See* Demsetz, *supra* note 190, at 43 ("a judgment that efficiency is good...is not self-contained in the logic or substance of economics; when such judgments are made, they are based on a value scheme outside 'economics'").

290. Professor O'Kelley notes that pursuit of wealth is a paramount goal of citizens in a post-liberal society and is nearly "biologically compelled." A post-liberal society is one

CONCLUSIONS

All four of the philosophical frameworks discussed above rely to some extent on the free market model in which individuals act primarily to maximize their own utility or wealth or satisfaction, and the result is an allocation of resources. Is it possible to think about distributive justice without using a model of individuals in a market? Critical legal theorists would say that it is. Instead of asking how we decide which individuals get how much stuff, perhaps we should ask, why should property be owned by individuals at all?[291] Why should we assume that people just want to be as wealthy as possible? Or as smart, or as talented? Is there some sense in which the mere existence of a market encourages people to behave in these self-maximizing ways? While these questions are beyond the scope of this paper, they are worth asking, even if only to further clarify our thinking about these issues.

Given, however, that we are proceeding within the general rubric of a market economy, fundamental distinctions among philosophical starting points are important if only because they are not obvious. The first of these starting points is the role of equality. If the initial distribution need not be equal, it is unlikely that any analysis of later distributions or distributional tools would require any degree of equality. Thus, process-oriented analytical systems, like efficiency theory or Nozick's entitlement theory, do not require equality at any stage of the game. Progressive taxes can only be justified within these systems if they do not disturb the inequality that develops as a result of the market processes that the systems embrace. Not surprisingly, any support for progressivity that can be marshalled within analytical frameworks such as the benefit theory is indeed "uneasy." The support is uneasy because one of the main pillars of the support structure, distributional equality, is missing.

A similar conclusion applies to equality at some later stage of the game. Even if the original distribution is equal, later distributional patterns may not be. As noted above, if processes are all-important, equality is not likely to seem relevant to the analysis. On the other hand, if one of the starting points is continuing equality or provision of some minimum level of social welfare, an approach that emphasizes processes cannot possibly provide the justification for the redistribution that becomes necessary from time to time. As Nozick so powerfully argues, redistribution fails to consider the interests that others already have in that which is redistributed (derived according to proper processes).

This brings us to the second major tenet underlying rate structure arguments: beliefs about entitlement to wealth. Do we believe as a fundamental matter that each individual is entitled to all of the fruits derived from the application of talent? Or do we believe that to a certain extent, individuals have a lesser claim on the proceeds of talent than on the proceeds of ambition. If

characterized by tension between a dominant liberalism of individualism and subordinate communitarian or altruistic views. O'Kelley, *Post-Liberal*, *supra* note 22, at 736. Professor Kornhauser would probably characterize post-liberal society as one dominated by a male view with tension created by a subordinated female view. *See* Kornhauser, *supra* note 3, at 508–11. But she would not agree that wealth maximization is in any way "biologically compelled." *Id.*

291. Professor Michelman asks whether property must be individually owned in his comparison of private property, regulation, and a state of nature on grounds of efficiency. *See* Frank I. Michelman, *Ethics, Economics, and the Law of Property*, *in* ETHICS, ECONOMICS AND THE LAW 3 (1982). *See also* Michelman & Kennedy, *supra* note 57.

there is a basis for treating wealth differently depending on its source, then a system that treats all wealth or income the same, such as the various sacrifice theories, is not likely to produce a case for progressivity that matches the intuitive feeling that major league baseball players should not mind so much paying a higher rate of tax than someone born without such lucrative talent or luck.

Finally, to the extent that one is entitled to wealth, to what extent do we agree with Nozick that owning something means we have an unfettered right to give it to whomever we please without the concern that taxation will interfere if the recipient happens to receive a lot from other sources? Is taxing the recipient really the same as taxing the giver?

If the theoretical structure supporting progressivity is made of pillars such as equal distribution and distinctions between wealth arising from luck and ambition, perhaps the case for progressivity is not so uneasy. Rather, it is the relevance of the traditional arguments,themselves, that becomes uneasy. Instead of wondering what it is that really supports progressivity, we can see more clearly how the intuitive appeal that progressivity seems to hold for many actually does lend some logical support to the case for progressivity. Rather than being beyond the scope of the argument, philosophical considerations complete the picture and should be part of the discussion.[292]

292. *Accord* Gregory S. Crespi, *Teaching the New Law & Economics*, 25 U. TOL. L. REV. 713, 714 (1994) (law and economics training that neglects behavioral assumptions and value premises is dangerous); O'Kelley, *Rawls*, *supra* note 35, at 27–29 (asserting a moral obligation to expose the underlying moral structure supporting assertions of moral entitlement).