Printed in U.S.A.
Vol. 117, No. 1

THE MISSING U.S. VAT: ECONOMIC INEQUALITY, AMERICAN FISCAL EXCEPTIONALISM, AND THE HISTORICAL U.S. RESISTANCE TO NATIONAL CONSUMPTION TAXES

Ajay K. Mehrotra

ABSTRACT—Since the 1970s, economic inequality has soared dramatically across the globe and particularly in the United States. In that time, one of the obstacles of using fiscal policy to address inequality has been the growing myth of the "overtaxed American"—the misguided notion that U.S. taxpayers pay more in taxes than residents of other advanced, industrialized countries. This myth has persisted, in part, because of the peculiar and distinctive nature of the fractured American fiscal and social welfare state. Even a cursory review of comparative tax data shows that the United States, by most measures, is a low-tax country compared to other affluent nations. One reason for this shortfall is the missing U.S. value-added tax (VAT).

Unlike the United States, other developed countries fund robust social spending through a balanced mix of levies, including by relying on broad-based national consumption taxes such as a VAT, which produces a tremendous amount of government revenue. By contrast, the United States has historically rejected comprehensive national consumption taxes, suggesting something distinctive about American fiscal policy. This American fiscal exceptionalism leads to a series of important research questions that may help us understand the relationship among fiscal policy, social welfare spending, and economic inequality: Why is the United States such an outlier in global comparisons of national taxes? Why have Americans historically resisted broad-based national consumption taxes of any kind? Simply put, why is there no U.S. VAT?

This Essay begins to address these fundamental questions by, first, synthesizing the existing literature to provide several stylized facts about global economic inequality and the particular concentration of wealth in the United States. Second, the Essay explores the distinctive and peculiar nature of the modern American fiscal and social welfare state, illustrating how the U.S. reliance on direct and progressive taxes and indirect and stealth social welfare spending may be perpetuating the myth of the overtaxed American. Finally, the essay identifies three key historical time periods when the United States seriously considered, but ultimately rejected, a broad-based national consumption tax. This Essay focuses mainly on the first period of the early 1920s, when post-World War I historical conditions provided tax experts, lawmakers, and social groups an opportunity to consider the adoption of a wide-ranging national consumption tax. The Essay concludes with some reflections on how the missing U.S. VAT may inform future tax reform and attempts to address economic inequality.

AUTHOR—Executive Director & Research Professor, American Bar Foundation; Professor of Law, Northwestern University Pritzker School of Law; Affiliated Professor of History, Northwestern University. Earlier versions of this paper were presented at the *Northwestern University Law Review* 2021 Symposium, *Reimagining Property in the Era of Inequality*, and the American Bar Foundation Legal History Workshop. Many thanks to participants at those venues for useful comments and questions, and special thanks to those who provided feedback on earlier drafts of this essay and the broader research project, including Steve Bank, Alexandra Dakich, Joanna Grisinger, Isaac William Martin, Monica Prasad, Chris Schmidt, Nadav Shoked, and Joe Thorndike. For their outstanding research assistance, I'm grateful to Emma Conner, Oren Depp, Lauren Escudero, Alex Freund, Minji Kim, Niko Letos, Jeff Svehla, Aaron Wang, and Jerry Zhang. The editors and staff of the NULR, especially Megan Cahillane, Sarah Chanski, Deepa Chari, Anthony Khilkov, Bradford McGann, Michael Palmer, Megha Sorot, Kathryn Speckels, Jared Stehle, Sarah Wolf-Knight and Summer Zofrea, provided excellent substantive feedback and guidance on final revisions.

INTRODUCTION

Since the 1970s, the United States has witnessed a dramatic increase in economic inequality. As numerous scholars and policy analysts have demonstrated, income and wealth disparities have grown tremendously, with the greatest concentration of wealth existing at the top end of the economic spectrum.[1] These inequalities, moreover, have been skewed disproportionately by race and gender.[2] And they have been exacerbated by both long-term declining opportunities for social and economic mobility and the more recent impact of the global healthcare crisis.[3]

The United States is not alone. The growing concentration of wealth and limited upward mobility have been occurring in nearly every advanced industrialized nation-state, even as globalization and greater economic liberalization have elevated those in poverty and raised the middle-class standard of living in many developing countries, particularly India and

[1] *See* EMMANUEL SAEZ & GABRIEL ZUCMAN, THE TRIUMPH OF INJUSTICE: HOW THE RICH DODGE TAXES AND HOW TO MAKE THEM PAY 6–7 (2019) [hereinafter SAEZ & ZUCMAN, INJUSTICE]; Emmanuel Saez & Gabriel Zucman, *Wealth Inequality in the United States Since 1913: Evidence from Capitalized Income Tax Data*, 131 Q.J. ECON. 519, 520 (2016) [hereinafter Saez & Zucman, *Wealth Inequality*].

[2] *See generally* DOROTHY A. BROWN, THE WHITENESS OF WEALTH: HOW THE TAX SYSTEM IMPOVERISHES BLACK AMERICANS—AND HOW WE CAN FIX IT 1–10 (2021) (discussing how the American tax code may disproportionally favor white families); Edward N. Wolff, *The Decline of African-American and Hispanic Wealth Since the Great Recession* 2 (Nat'l Bureau of Econ. Rsch., Working Paper No. 25198, 2018), https://www.nber.org/system/files/working_papers/w25198/w25198.pdf [https://perma.cc/35EP-MPM6] (documenting the deterioration of Black and Hispanic household wealth compared to white households between 1983 and 2016).

[3] AMBAR NARAYAN ET AL., FAIR PROGRESS? ECONOMIC MOBILITY ACROSS GENERATIONS AROUND THE WORLD 23 (2018); *cf.* Raj Chetty, Nathaniel Hendren, Patrick Kline, Emmanuel Saez & Nicholas Turner, *Is the United States Still a Land of Opportunity? Recent Trends in Intergenerational Mobility*, 104 AM. ECON. REV.: PAPERS & PROC. 141, 141 (2014) (finding that income inequality increased over time for children born between 1971 and 1993).

China.[4] Still, the United States leads much of the developed world in its level of economic disparity.[5] Indeed, at least one recent U.S. President has identified economic inequality as the "defining challenge of our time."[6]

One way to address growing American economic inequality is through national fiscal policy, namely the federal tax-and-transfer system.[7] Along with other essays in this Symposium issue, *Reimagining Property in the Era of Inequality*, this Essay attempts to provide a useful foundation for subsequent research. Specifically, this Essay's comparative-historical analysis outlines the role of U.S. tax law and social policy in undergirding—and perhaps mitigating—increasing inequality in the United States.

Taxation, after all, is a critical subset of property rights.[8] Tax laws govern a fundamental relationship between individuals and the state, between subjects and the sovereign. How and whom we tax helps define notions of "fiscal citizenship,"[9] and how wide we draw the circle of we. In addition, the revenues generated by taxes in a liberal democracy, like the

4 Homi Kharas & Brina Seidel, *What's Happening to the World Income Distribution? The Elephant Chart Revisited* 15–16 (Glob. Econ. & Dev. at Brookings, Working Paper No. 114, 2018), https://www.brookings.edu/wp-content/uploads/2018/04/workingpaper114-elephantchartrevisited.pdf [https://perma.cc/7TGD-9Q55]; Christoph Lakner & Branko Milanovic, *Global Income Distribution: From the Fall of the Berlin Wall to the Great Recession*, 30 WORLD BANK ECON. REV. 203, 223 (2016).

5 Ho-fung Hung, *Recent Trends in Global Economic Inequality*, 47 ANN. REV. SOCIO. 349, 354 (2021); Arthur S. Alderson & Roshan K. Pandian, *What Is Really Happening with Global Inequality?*, 4 SOCIO. DEV. 261, 264 (2018); *Income Inequality*, OECD DATA (2022), https://data.oecd.org/inequality/income-inequality.htm [https://perma.cc/HDK5-7XPZ] (demonstrating that the United States has the highest income inequality of any G7 country).

6 Barack Obama, President of the United States, Remarks by the President on Economic Mobility, (Dec. 4, 2013), https://www.whitehouse.gov/the-press-office/2013/12/04/remarks-president-economic-mobility [https://perma.cc/2E75-T38M].

7 For more on this relationship, see generally the essays in INEQUALITY AND FISCAL POLICY (Benedict J. Clements, Ruud de Mooij, Sanjeev Gupta & Michael Keen eds., 2015), discussing how fiscal policy may reduce global income inequality.

8 *See generally* LIAM MURPHY & THOMAS NAGEL, THE MYTH OF OWNERSHIP: TAXES AND JUSTICE 8 (2002) (noting that "[t]axes must be evaluated as part of the overall system of property rights that they help to create"); STEPHEN HOLMES & CASS R. SUNSTEIN, THE COST OF RIGHTS: WHY LIBERTY DEPENDS ON TAXES 15 (1999) (explaining the necessity of taxes to protect and enforce property and welfare rights); Isaac William Martin & Monica Prasad, *Taxes and Fiscal Sociology*, 40 ANN. REV. SOCIO. 331, 332 (2014) (reviewing research on the relationship between taxation, poverty, and inequality).

9 On the concept of fiscal citizenship, see generally James T. Sparrow, *"Buying Our Boys Back": The Mass Foundations of Fiscal Citizenship in World War II*, 20 J. POL'Y HIST. 263 (2008); AJAY K. MEHROTRA, MAKING THE MODERN AMERICAN FISCAL STATE: LAW, POLITICS, AND THE RISE OF PROGRESSIVE TAXATION, 1877–1929, at 40, 61–67 (2013); and LAWRENCE ZELENAK, LEARNING TO LOVE FORM 1040: TWO CHEERS FOR THE RETURN-BASED INCOME TAX 17 (2013).

United States, underwrite nearly all other realms of lawmaking, from housing policy to environmental regulation to educational spending.[10]

In the past half-century, there have been many obstacles to using U.S. fiscal policy to address growing inequality. One of the most politically salient has been the myth of the "overtaxed" American—the misguided notion that U.S. taxpayers pay more in taxes than individuals in other advanced, industrialized countries.[11] This canard has, in part, prevented the United States from adopting new, more robust forms of taxation. Even though tax revenues provide the funds necessary for nearly every aspect of government, many politicians and everyday Americans continue to cling to the antiquated notion that a modern regulatory, administrative, social welfare state can function effectively with insufficient taxes and limited government. To support this view, many political leaders on the right have perpetuated the myth that Americans are overtaxed compared to our global counterparts.[12]

One possible reason why this myth has persisted is the peculiar and distinctive nature of the modern American fiscal and social welfare state. The revenue-extraction side of U.S. fiscal policy (i.e., taxation) is, for the most part, highly visible and direct. Although scholars have disagreed about the cognitive impact of different types of taxes, most concur that direct taxes, like progressive income taxes, are generally more prominent and thus more

[10] My fellow authors that participated in the *Northwestern University Law Review* 2021 Symposium, *Reimagining Property in the Era of Inequality*, discuss each of these topics in detail. *See, e.g.*, Carol M. Rose, *Property Law and Inequality: Lessons from Racially Restrictive Covenants*, 117 Nw. U. L. Rev. 225 (2022) (reviewing the history of racially restrictive covenants and their role in curtailing opportunities for Black communities to acquire and pass on wealth); LaToya Baldwin Clark, *Family | Home | School*, 117 Nw. U. L. Rev. 1 (2022) (arguing that school residency laws perpetuate race–class–gender subordination of and restrict access to education for children from family structures that do not reflect the archetypical nuclear family); Laura S. Underkuffler, *Challenging Equality: Property Loss, Government Fault, and the Global Warming Catastrophe*, 117 Nw. U. L. Rev. 335 (2022) (arguing that the increase in severity and cost of catastrophic events due to climate change will force a change in traditional loss-compensation solutions such as insurance and direct government relief payments).

[11] *See generally* Kenneth Rapoza, *Are Americans Overtaxed?*, FORBES (Mar. 14, 2013, 5:06 PM), https://www.forbes.com/sites/kenrapoza/2013/03/14/are-americans-over-taxed/ [https://perma.cc/34MJ-EJC8] (arguing that Americans are not overtaxed based on a comparison of national salary); William G. Gale, *Are Americans Really Overtaxed?*, BROOKINGS (Feb. 24, 1999), https://www.brookings.edu/opinions/are-americans-really-overtaxed [https://perma.cc/KM4H-BJBM] (finding that the tax burden on Americans has decreased over time); Howard Gleckman & Aravind Boddupalli, *No, the US Is Not Overtaxed*, TAX POL'Y CTR. (Aug. 20, 2019), https://www.taxpolicycenter.org/taxvox/no-us-not-overtaxed [https://perma.cc/AW89-TXXK] (stating that Americans are taxed less than residents of other developed countries).

[12] *See infra* notes 89–92 and accompanying text.

economically salient to most taxpayers.[13] By contrast, many Americans take for granted the array of goods and services provided by the modern state. By definition, basic public goods—from roads to national defense to public health funding—belong to everyone. Using the language of public economics, pure public or collective goods are those that are "nonexcludable" and "nonrivalrous." Everyone benefits from public goods, and one person's consumption does not limit the amount of the good for others.[14]

In the realm of social spending, many of the benefits furnished by the government to individuals and families are provided indirectly, often through the tax code itself or through private channels. From the Earned Income Tax Credit (EITC) to employer-provided healthcare coverage and retirement savings, the federal government provides vital anti-poverty and social welfare benefits indirectly via "tax expenditures."[15] These benefits, moreover, are generally linked to participation in the formal labor market, and thus subsumed as part of everyday employment. As a result, the spending side of the American fiscal state is often hidden, fractured by public–private social benefits, submerged from the surface, and hence less visible to the public.[16] In sum, Americans may feel the grip or pinch of direct and

---

13 *See, e.g.*, Edward J. McCaffery, *Cognitive Theory and Tax*, 41 UCLA L. REV. 1861, 1864 (1994) (arguing that cognitive biases help explain "major structural features" of the American tax system); Raj Chetty, Adam Looney & Kory Kroft, *Salience and Taxation: Theory and Evidence*, 99 AM. ECON. REV. 1145, 1146 (2009) (finding that "commodity taxes that are included in the posted prices that consumers see when shopping (and are thus more salient) have larger effects on demand"); David Gamage & Darien Shanske, *Three Essays on Tax Salience: Market Salience and Political Salience*, 65 N.Y.U. TAX L. REV. 19, 98 (2011) (reviewing empirical literature on market and political salience to argue for improving policymakers' understanding of tax salience); Jacob Goldin, *Optimal Tax Salience*, 131 J. PUB. ECON. 115, 115 (2015) (studying the salience of commodity taxes and finding that low-salience taxes decrease "the burden . . . associated with distortionary taxes" but cause "taxpayers to make optimization errors").

14 JOSEPH E. STIGLITZ, ECONOMICS OF THE PUBLIC SECTOR 128–29 (2000); N. GREGORY MANKIW, PRINCIPLES OF ECONOMICS 209–22 (6th ed. 2012).

15 Tax expenditures are generally defined as revenue losses resulting from tax provisions that grant special tax relief to encourage certain behavior or to aid taxpayers in particular circumstances. Jane G. Gravelle, *Tax Expenditures*, *in* THE ENCYCLOPEDIA OF TAXATION AND TAX POLICY 406–08 (Joseph J. Cordes, Robert D. Ebel & Jane G. Gravelle eds., 2005).

16 *See generally* CHRISTOPHER HOWARD, THE HIDDEN WELFARE STATE: TAX EXPENDITURES AND SOCIAL POLICY IN THE UNITED STATES 3, 13 (1999) (describing the concept of viewing certain tax expenditures as a form of "hidden welfare"); JACOB S. HACKER, THE DIVIDED WELFARE STATE: THE BATTLE OVER PUBLIC AND PRIVATE SOCIAL BENEFITS IN THE UNITED STATES 7 (2002) (reviewing America's public–private welfare regime and discussing "how it shapes the politics of social policy in the United States"); MARIE GOTTSCHALK, THE SHADOW WELFARE STATE: LABOR, BUSINESS, AND THE POLITICS OF HEALTHCARE IN THE UNITED STATES, at viii (2000) (using healthcare reform in the United States to address questions "related to the politics of economic restructuring"); KIMBERLY J. MORGAN & ANDREAS LOUISE CAMPBELL, THE DELEGATED WELFARE STATE: MEDICARE, MARKETS, AND THE GOVERNANCE OF SOCIAL POLICY 4 (2011) (discussing delegated governance in the United States using

progressive taxes, but public goods and subsidized social welfare benefits often go unnoticed or are taken for granted.

In contrast to the U.S. system, other advanced, industrialized countries provide social welfare benefits and attempt to address economic inequality in more direct ways, frequently through progressive, citizenship-based public sector expenditures such as national education and healthcare.[17] These nation-states fund their large public sectors by taxing their citizens and residents through a balanced mix of levies, including by relying on robust broad-based national consumption taxes such as a value-added tax (VAT).[18] Indirect consumption taxes, like a VAT, not only produce tremendous public revenue, but also frequently go less noticed by taxpayers.[19]

Generally, a VAT is remitted by an entity in each stage of the production and distribution process, although the ultimate buyer of the good or service may bear the tax. Consumers who pay the VAT generally see a small levy on each purchase, as opposed to a large sum each April from direct income taxes. Reliance on the VAT may, in turn, explain the strength and resilience of many European social welfare states, as some scholars have argued,[20] though the correlation between abundant VAT revenues and robust

the 2003 Medicare Modernization Act as an example); SUZANNE METTLER, THE SUBMERGED STATE: HOW INVISIBLE GOVERNMENT POLICIES UNDERMINE AMERICAN DEMOCRACY 7 (2011) (arguing that a lack of transparency in government spending threatens American democracy).

17 *See* GØSTA ESPING-ANDERSEN, THE THREE WORLDS OF WELFARE CAPITALISM 26–27 (1990); KEES VAN KERSBERGEN & BARBARA VIS, COMPARATIVE WELFARE STATE POLITICS: DEVELOPMENT, OPPORTUNITIES, AND REFORM 2 (2014).

18 A value-added tax is a consumption tax assessed on the value added at each stage of the production process for a good or service. It is often similar in its economic effects to a retail sales tax, which many U.S. state and local governments levy. Unlike a sales tax, which is collected by the retailer at the point of sale of goods and services, a VAT is collected by business entities in each stage of the production process. LEONARD E. BURMAN & JOEL SLEMROD, TAXES IN AMERICA: WHAT EVERYONE NEEDS TO KNOW 98–100 (2d ed. 2020); *see also* Martin A. Sullivan, *Introduction: Getting Acquainted with VAT*, *in* THE VAT READER: WHAT A FEDERAL CONSUMPTION TAX WOULD MEAN FOR AMERICA 7, 12–13 (2011) (discussing the impact of a VAT system); ALAN SCHENK & OLIVER OLDMAN, VALUE ADDED TAX: A COMPARATIVE APPROACH 16–17 (2007) (explaining the European Commission's VAT system).

19 McCaffery, *supra* note 13, at 1886; Chetty et al., *supra* note 13, at 1165.

20 *See generally* JUNKO KATO, REGRESSIVE TAXATION AND THE WELFARE STATE: PATH DEPENDENCE AND POLICY DIFFUSION 1, 3, 199 (2003) (examining how resilient welfare states are generally funded by a VAT); MONICA PRASAD, THE LAND OF TOO MUCH: AMERICAN ABUNDANCE AND THE PARADOX OF POVERTY, at xii–xiii (2012) (arguing that differences in U.S. poverty compared to European nations can be attributed to the United States' pattern of progressive taxation); KATHRYN JAMES, THE RISE OF THE VALUE-ADDED TAX 8 (2019) (examining and explaining the widespread implementation of VAT systems). Professor Kato's research indicates that countries with regressive consumption taxes frequently use progressive social welfare spending to overcome regressive tax incidence, and those countries that have had more long-standing commitments to the combination of regressive consumption taxes and progressive social spending have been able to withstand recent attacks on the social welfare state. KATO, *supra*, at 1, 9.

social spending does not imply causation.[21] In this sense, the United States is a stark outlier in the conspicuous absence of an American VAT. Whereas all other advanced, industrialized countries have a comprehensive national consumption tax in the form of a VAT, the United States has historically rejected broad-based national consumption taxes, suggesting something distinctive about American fiscal policy.[22]

This American fiscal exceptionalism[23] leads to a series of important questions that may help us understand the relationship between fiscal policy and economic inequality: Why is the United States such an outlier in global comparisons of national taxes? Why are overall U.S. taxes lower than similarly situated countries? And why have Americans historically resisted broad-based national consumption taxes of any kind? Simply put, why is there no U.S. VAT?

This Essay begins to address these fundamental questions by providing some important background information about growing economic inequality, the peculiar nature of the modern American fiscal and social welfare state, and the historical evolution of U.S. resistance to broad-based national consumption taxes.

The Essay proceeds in three parts. Part I synthesizes the existing scholarly literature on economic inequality, illustrating through a series of stylized facts how the high-end concentration of wealth has increased dramatically since the 1970s across the globe, especially in the United States. Part II shows how the combination of direct and progressive taxes on income and the shrouded nature of U.S. social spending have helped perpetuate the myth of the "overtaxed" American. Part III explores the fundamental question of why the United States has failed to adopt a more robust form of indirect, comprehensive, national consumption taxes. Exploring this comparative-historical query may shed light on the origins of U.S. economic

---

[21] Steffen Ganghof, *Tax Mixes and the Size of the Welfare State: Causal Mechanisms and Policy Implications*, 16 J. EUR. SOC. POL'Y 360, 370–71 (2006). Ganghof raises the important point that many strong European social welfare states may have preceded the rise of the VAT, indicating that the demand for greater public revenue has driven the adoption of VATs in other countries. *Id.* at 362, 364–66.

[22] KATO, *supra* note 20, at 113; JAMES, *supra* note 20, at 12–13. The United States has had national excise taxes on particular goods, such as alcohol and tobacco, throughout its history, but we have resisted broad-based, comprehensive consumption taxes at the national level. On the history of national excise taxes, see generally W. ELLIOT BROWNLEE, FEDERAL TAXATION IN AMERICA: A SHORT HISTORY 1–8 (1994), reviewing the history of American tax systems and discussing recent trends in tax policies.

[23] To be sure, the notion of "American exceptionalism" has come under increasing scholarly scrutiny. *See generally* RETHINKING AMERICAN HISTORY IN A GLOBAL AGE (Thomas Bender ed., 2002) (placing the development of the United States within the context of globalization); GODFREY HODGSON, THE MYTH OF AMERICAN EXCEPTIONALISM, at xiv–xvi, 14–15 (2009) (tracing the notion of American exceptionalism throughout the United States' development and challenging its validity).

inequality and how lawmakers might use fiscal policy to address the growing disparities in wealth and opportunity.

More specifically, this final Part identifies three key historical time periods when the United States considered, but ultimately rejected, a national consumption tax—a tax that might have evolved into a modern VAT and perhaps been the foundation for a more vigorous American fiscal and social welfare state. The Essay ends with a conclusion and coda about the promise and limits of a U.S. VAT in addressing economic inequality.

I. Stylized Facts About Economic Inequality

In recent years, empirical research about economic inequality has become a cottage industry among scholars, especially among French and American economists. Thanks to the scholarship of Emmanuel Saez, Gabriel Zucman, and of course Thomas Piketty,[24] among others,[25] there are now a series of "stylized facts" about the changing landscape of economic inequality in the United States and across most of the world.[26] This well-established literature has shown that over the last few decades there has been variation in how the forces of globalization and economic liberalization have affected different segments of the world's population. While poverty has declined and the middle class has grown in some developing countries, namely China and India, the upper-middle classes across the world have stagnated while the super-wealthy have prospered. Meanwhile, income inequality *within* countries has increased dramatically, with the concentration of wealth at the top end of the spectrum skyrocketing,

[24] *See, e.g.*, Thomas Piketty, Emmanuel Saez & Gabriel Zucman, *Distributional National Accounts: Methods and Estimates for the United States*, 133 Q.J. ECON. 553, 553 (2018) (using a combination of data types to calculate pre- and post-tax income in America and drawing conclusions about redistribution and inequality); Thomas Piketty & Emmanuel Saez, *Income Inequality in the United States, 1913–1998*, 118 Q.J. ECON. 1, 1–41 (2003) (using empirical tax data to show how economic inequality has decreased and then increased during the long twentieth century); Gabriel Zucman, *Global Wealth Inequality*, 11 ANN. REV. ECON. 109, 119–22, 124–26 (2019) (performing a similar analysis on a global scale). These French economists fall in a long line of astute French observers of American politics and culture. *See generally* ALEXIS DE TOCQUEVILLE, DEMOCRACY IN AMERICA 4, 11 (Henry Reeve trans., 2002) (1835) (observing the early development of democracy in America).

[25] *See, e.g.*, ANTHONY B. ATKINSON, INEQUALITY: WHAT CAN BE DONE? 9–14, 16–23 (2015) (summarizing foundational works in empirical economic equality scholarship); AMARTYA SEN & JAMES FOSTER, ON ECONOMIC INEQUALITY 2–10 (1997) (outlining measurements and methodologies for empirical economic welfare research); GANESH SITARAMAN, THE CRISIS OF THE MIDDLE-CLASS CONSTITUTION: WHY ECONOMIC INEQUALITY THREATENS OUR REPUBLIC 227–30 (2017) (describing empirical studies that depict a shrinking American middle class and decreased economic mobility).

[26] *See Stylized Facts*, DICTIONARY OF THE SOCIAL SCIENCES (Craig Calhoun ed., 2002). The term "stylized facts" is generally associated with the mid-twentieth-century economist Nicholas Kaldor, who argued that economic theorists should work from "a 'stylized' view of the facts" by concentrating on "broad tendencies, ignoring individual details." Nicholas Kaldor, *Capital Accumulation and Economic Growth*, *in* THE THEORY OF CAPITAL 177, 178 (D.C. Hague ed., 1961).

especially in the United States. This section summarizes these stylized facts.[27]

Although scholars and researchers have disagreed about the exact contours of shifts in economic inequality, there are a few points of general agreement. First, many analysts agree that since the 1980s, global inequality, as measured by *cross-country* comparisons, has actually decreased. For example, using one standard economic metric for inequality, the Gini coefficient,[28] scholars have shown that population-weighted, real income inequality between countries has declined from a Gini of roughly 0.6 in the 1970s to a Gini below 0.5 by 2014, meaning that global inequality has diminished.[29] This decline has been driven mainly by rapid industrialization and accompanying income growth among the poor and lower-middle classes in developing countries, mainly China and India. Because these two countries alone account for over 36% of the world's population, their income growth offsets a drop in other parts of the global South and developing world.[30] Thus, between-country estimates have demonstrated that global inequality has been declining in the last few decades.[31]

By contrast, the second stylized fact indicates that for the past four decades or so, economic disparities *within* countries have increased dramatically across the world. Using a wide variety of evidence, from household surveys to tax administrative data, scholars have shown that *income* inequality, in particular, has increased in roughly two-thirds of the world's societies since the 1980s, with greater disparities in the developing world.[32] The average increase has generally been striking. According to one set of estimates, between the 1980s and 2010s, the median level of income inequality increased roughly 4.5 Gini points.[33]

There has been a similar upward trend for *wealth* inequality. Since the 1980s, within-country wealth concentration has been growing. Focusing

---

27 In this sense, this first section is meant to be a concise synthesis of the existing social science and law review literature on economic inequality.

28 The Gini coefficient is an often-used, albeit imperfect, metric to measure the dispersion of income across an entire income distribution. Gini coefficients range from zero, indicating perfect equality, to one, denoting perfect inequality. *Gini Coefficient*, DICTIONARY OF THE SOCIAL SCIENCES (Craig Calhoun ed., 2002); STIGLITZ, *supra* note 14, at 121.

29 Alderson & Pandian, *supra* note 5, at 267.

30 *Id.* at 271.

31 Hung, *supra* note 5, at 352–53.

32 Alderson & Pandian, *supra* note 5, at 262–63. *See generally* James K. Galbraith, *Inequality and Economic and Political Change: A Comparative Perspective*, 4 CAMBRIDGE J. REGIONS, ECON. & SOC'Y 13, 21–22 (2011) (describing changes in inequality in the world economy since 1963); BRANKO MILANOVIC, GLOBAL INEQUALITY: A NEW APPROACH FOR THE AGE OF GLOBALIZATION 19–20 (2016) (examining factors that increase global inequality).

33 Alderson & Pandian, *supra* note 5, at 264.

mainly on the top 1% of the global spectrum, researchers have shown that the world's leading economies have witnessed greater wealth concentration. More specifically, the top 1% wealth share for China, Europe, and the United States combined has increased from 28% in 1980 to roughly 33% in 2019.[34] Meanwhile, the bottom 75% share has stagnated at 10%.[35] Simply put, the world's rich have gotten richer while others have not over the last four decades.

Third, there is near consensus that since the 1980s, both income and wealth disparities in the United States have grown markedly. In fact, there has been an explosion of research documenting the rise of economic inequality in the United States, with a particular focus on the concentration of wealth among the richest Americans. This near consensus appears to persist even as scholars continue to debate the different ways to measure income and wealth.[36] One useful metric demonstrating the increasing disparity is the share of pretax income earned by different segments of American income earners. As the research of Saez and Zucman illustrates, the wealthiest Americans have doubled their share of the total economic pie in the last forty years.[37] In the 1980s, the richest Americans, those in the top one percent of income earners, received roughly 10% of the nation's total pretax income (before government taxes and transfers), while the working class and poor (the bottom 50%) earned around 20% at that time.[38] By 2019, these figures were practically inverted.[39] The richest (top one percent) were capturing more than 20% of national income, while the bottom half was collecting about 12%.[40]

Similar trends exist for American wealth concentration. Although reliable estimates related to wealth are more difficult to collect for the United States, mainly due to the lack of data, recent estimates suggest that the high-end of the American economic spectrum continues to accumulate

[34] Zucman, *supra* note 24, at 111; *see, e.g.*, Florian Scheuer & Joel Slemrod, *Taxing Our Wealth*, 35 J. ECON. PERSPS. 207, 207 (2021) ("In 2016, . . . the top 1 percent of households ranked by net worth held 40 percent of US wealth . . . .").

[35] Zucman, *supra* note 24, at 111.

[36] *See generally* Emmanuel Saez & Gabriel Zucman, *Trends in U.S. Income and Wealth Inequality: Revising After the Revisionists* (Nat'l Bureau of Econ. Rsch., Working Paper No. 27921, 2020), https://www.nber.org/system/files/working_papers/w27921/w27921.pdf [https://perma.cc/L3HV-8RK] (reviewing past studies on income inequality and finding that income inequality continues to rise); Matthew Smith, Danny Yagan, Owen Zidar & Eric Zwick, *Capitalists in the Twenty-First Century*, 134 Q.J. ECON. 1675, 1676–78 (2019) (using administrative tax data to "characterize top incomes").

[37] SAEZ & ZUCMAN, INJUSTICE, *supra* note 1, at 6.

[38] *Id.*

[39] *Id.*

[40] *Id.*

astonishing amounts of resources.[41] In 1980, the top one percent of wealthiest tax units owned roughly 23% of total assets. By 2020, that figure nearly doubled to almost 40%.[42] Such growing concentration of wealth is even more pronounced for higher tax units. As Saez and Zucman have recently concluded, "[b]y any metric, the period from 1980 to 2020 has been an era of extraordinary wealth accumulation among the rich in the United States."[43]

Even when accounting for the potential impact of redistributive government tax-and-transfer laws and policies, the wealthiest Americans still prospered tremendously, while the working class witnessed only moderate relief. In 2018, the United States had the second-highest level of wealth inequality among thirty-three Organisation for Economic Co-operation and Development (OECD) countries, after taking into account taxes and transfers.[44] Such a finding suggests that well-intentioned fiscal and social policy by itself has done little to alter the acceleration of inequality. This has been a longstanding historical trend. From 1977 to 2014, the top one percent's share of national income, before taxes and transfers, increased by nearly 90%. After accounting for tax and transfer, the top one percent's share still managed to increase by more than 81%. In other words, progressive taxes appear to have had only a modest dampening effect. At the opposite end of the spectrum, the bottom 50% saw their share of national income decline to about 20%, post tax and transfer, instead of 26% pretax and transfer over the same period. Thus, the American social welfare state has only modestly cushioned the slide.[45]

In fact, these trends are even more pronounced when one goes beyond the top one percent and looks more closely at the über-wealthy in America today, who have been particularly skilled at limiting their tax liability.[46] The causes behind these trends are, of course, multifaceted and beyond the scope of this brief Essay. But we know that worldwide changes in technology, economic globalization, international tax competition, increased

---

[41] *See* Scheuer & Slemrod, *supra* note 34, at 207.

[42] Emmanuel Saez & Gabriel Zucman, *The Rise of Income and Wealth Inequality in America: Evidence from Distributional Macroeconomic Accounts*, 34 J. ECON. PERSPS. 3, 10 fig.1 (2020).

[43] *Id.* at 11. A "tax unit" is a term of art in tax scholarship. It refers to "an individual or married couple that files a tax return or would file a tax return if their income were high enough, along with all dependents of that individual or married couple." *TPC's Microsimulation Model FAQ*, TAX POL'Y CTR., https://www.taxpolicycenter.org/resources/tpcs-microsimulation-model-faq [https://perma.cc/9DD5-L4M3].

[44] Lily Batchelder & David Kamin, Taxing the Rich: Issues and Options 2 (Sept. 11, 2019) (unpublished manuscript), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3452274 [https://perma.cc/L2WQ-9SQA].

[45] *See* ADAM TOOZE, CRASHED: HOW A DECADE OF FINANCIAL CRISES CHANGED THE WORLD 458 (2018).

[46] *See* Saez & Zucman, *Wealth Inequality*, *supra* note 1, at 519.

deregulation of finance, relentless assaults on progressive taxation, excessive executive compensation, the decimation of organized labor, and related factors have widened the earnings gap between ordinary, working-class Americans and the most affluent.[47]

Consider a final startling comparison of wages. In 1965, the average chief executive officer made about twenty-four times as much as an average worker.[48] By 1978, that ratio climbed to thirty-five times as much.[49] By 1989, it was seventy-one times as much. And by 2000, the figure had skyrocketed to nearly three hundred times as much.[50] The C-suite has come to dominate the shop floor like never before.

II. THE FRACTURED U.S. FISCAL/SOCIAL WELFARE STATE AND THE MYTH OF THE "OVERTAXED" AMERICAN

As the earlier set of stylized facts indicates, U.S. fiscal and social welfare policies have only modestly mitigated the dramatic increase in American economic inequality. One possible reason for this limitation is the institutional design of the U.S. fiscal and social welfare state. Indeed, the combination of a highly salient system of direct and progressive taxation and a more "hidden" social welfare state has helped perpetuate the myth of the "overtaxed" American—a myth that has been exploited by politicians and lawmakers for decades. As a result, many U.S. policymakers and taxpayers alike seem unaware of the unique and peculiar aspects of the American system of taxes and transfers, and what those aspects might tell us about the relationship among taxes, inequality, and social welfare spending.

By most definitions, the tax side of fiscal policy entails a legal obligation on taxpayers to contribute money or goods to the state in exchange for nothing in particular. Certain tax revenues, to be sure, are often

---

47 *See generally* GRETA R. KRIPPNER, CAPITALIZING ON CRISIS: THE POLITICAL ORIGINS OF THE RISE OF FINANCE 60, 83–85 (2011) (discussing the historical events that contributed to the evolution of finance in the United States); PRASAD, *supra* note 20, at 170–71; QUINN SLOBODIAN, THE GLOBALISTS: THE END OF EMPIRE AND THE BIRTH OF NEOLIBERALISM 1–26 (2018) (tracing the history of neoliberalism in the establishment of the world economy); MONICA PRASAD, STARVING THE BEAST: RONALD REAGAN AND THE TAX CUT REVOLUTION 121–24 (2018) (examining the history of tax-cut policies in the United States and its ties to the political agenda of the Republican party); Reuven S. Avi-Yonah, *Globalization, Tax Competition, and the Fiscal Crisis of the Welfare State*, 113 HARV. L. REV. 1573, 1578 (2000) (describing "the problems of tax competition" and developing solutions that balance competing needs).

48 KEVIN M. KRUSE & JULIAN E. ZELIZER, FAULT LINES: A HISTORY OF THE UNITED STATES SINCE 1974, at 234 (2019); Lawrence Mishel, *CEO-to-Worker Pay Imbalance Grows*, ECON. POL'Y INST. (June 21, 2006), https://www.epi.org/publication/webfeatures_snapshots_20060621 [https://perma.cc/T4R5-DR6J].

49 Mishel, *supra* note 48.

50 *Id.*

earmarked for particular uses. But in most modern liberal democracies, taxation comes with the implicit premise that resources will be extracted equitably from different taxpayers, and that tax revenues will be spent on public or collective goods and services.[51]

Indeed, taxes have been defined historically as a coercive part of state power. In 1888, one leading American economic theorist, Richard T. Ely, characterized taxes as "one-sided transfers of economic goods or services *demanded* of the citizens . . . by the constituted authorities of the land."[52] A century later, the World Bank similarly described taxes as "unrequited, *compulsory* payments collected primarily by central governments."[53] At the same time, taxpayers have generally complied with their tax obligations not only out of fear of punishment because it is demanded or compulsory, but also because they believe others are in compliance and because they see the tangible benefits of their contributions to the public sector. The notion of what scholars have referred to as "quasi-voluntary compliance" thus entails both a highly punitive aspect, namely the possibility of penalty for noncompliance, and a normative element that taxes are levied fairly and for good use.[54]

If modern taxes rest on "quasi-voluntary compliance," the particular design of the U.S. tax system seems to skew towards those levies which are most prominent, visible, and open to state coercion.[55] Compared to most other advanced industrial democracies, the United States as a whole relies significantly more on the direct taxation of income and property—two highly salient types of tax bases.[56] Even a cursory examination of data from the

---

51 *See generally* CAROLYN WEBBER & AARON WILDAVSKY, A HISTORY OF TAXATION AND EXPENDITURE IN THE WESTERN WORLD (1986) (examining how different governments have handled common tax issues).

52 RICHARD T. ELY, TAXATION IN AMERICAN STATES AND CITIES 6–7 (Thomas Y. Crowell & Co. 1888) (emphasis added).

53 THE WORLD BANK, WORLD DEVELOPMENT REPORT: ISSUES IN PUBLIC FINANCE 79 (1988) (emphasis added).

54 MARGARET LEVI, OF RULE AND REVENUE 56–58 (1988). For further discussion of quasi-voluntary compliance, see WHY PEOPLE PAY TAXES: TAX COMPLIANCE AND ENFORCEMENT (Joel Slemrod ed., 1992); ELINOR OSTROM, GOVERNING THE COMMONS: THE EVOLUTION OF INSTITUTIONS FOR COLLECTIVE ACTION 94–95 (1990); and Itai Grinberg, *The Battle over Taxing Offshore Accounts*, 60 UCLA L. REV. 304, 355 (2012).

55 Although there is variation in the tax literature on what makes a particular levy more or less salient, there appears to be general agreement that direct taxes on income and property are cognitively more prominent in the minds of taxpayers than indirect taxes like the retail sales tax. For further information on salience, see *supra* note 13 and accompanying text.

56 For property tax salience, see, for example, Marika Cabral & Caroline Hoxby, *The Hated Property Tax: Salience, Tax Rates, and Tax Revolts* 1 (Nat'l Bureau of Econ. Rsch., Working Paper No. 18514, 2012) ("[Property tax] is more likely to be salient than taxes that are indirect, rolled into gross-of-tax

OECD shows the stark contrast. In 2019, individual income taxes (at the federal, state, and local level combined) were the primary source of U.S. tax revenue, accounting for nearly 41% of total tax revenue.[57] By contrast, OECD countries on average raised 24% of total tax revenue from individual income taxes.[58] Likewise, the direct taxation of property differs dramatically. Whereas the average OECD country raised only about 6% of total tax revenue from property taxes, the U.S. figure is twice as high, at more than 12% of total tax revenue.[59]

More specifically, the U.S. *federal* government relies heavily on income and payroll taxes, which are generally considered more prominent, visible, and salient than consumption taxes.[60] In 2019, approximately 57% of total federal tax revenue came from individual (50%) and corporate (7%) taxes, with another 36% from payroll taxes related to social insurance programs such as Social Security and Medicare.[61]

These levies are clearly legible in the paychecks and withholding figures of all American wage earners. The high visibility and salience of these direct and often graduated taxes makes the collection process of U.S. taxation starker and more excruciating than other more indirect forms of taxation, such as consumption taxes, which are often blended into the price of goods and services. While everyday workers may not be aware of or regularly pay attention to how much of their paychecks go to income tax withholding or Social Security, they are well aware that their net income does not match their gross receipts.[62] Similarly, every April 15, U.S. taxpayers are reminded of the arduous process of filing their income taxes where they get to reconcile just how much of their annual earnings have gone to the federal government.[63]

---

prices, collected through withholding, fragmented, or otherwise difficult to compute or notice.”). For income tax salience, see, for example, Amy N. Finkelstein, *E-ZTax: Tax Salience and Tax Rates*, 124 Q.J. ECON. 969, 969–70 (2009) (citing concerns that “lower visibility of a VAT [relative to income tax] would affect the size of government”).

[57] *Revenue Statistics - OECD Countries: Comparative Tables*, OECD.STAT, https://stats.oecd.org/index.aspx?DataSetCode=REV [https://perma.cc/3ML8-LMS2].

[58] *Id.*

[59] *Id.*

[60] *See supra* note 13 and accompanying text.

[61] *See* OFF. OF MGMT. & BUDGET, HISTORICAL TABLES tbl.2.1, https://www.whitehouse.gov/omb/budget/historical-tables/ [https://perma.cc/K3A5-2TTE].

[62] *See* VANESSA S. WILLIAMSON, READ MY LIPS: WHY AMERICANS ARE PROUD TO PAY TAXES 14–15 (2017).

[63] *See* ZELENAK, *supra* note 9, at 1–2; WILLIAMSON, *supra* note 62, at 13; Ajay K. Mehrotra, *Reviving Fiscal Citizenship*, 113 MICH. L. REV. 943, 943 (2015) (“April 15 is a day that most Americans dread. That date is, of course, when federal and nearly all state-level individual income tax returns are due.”);

It is this aspect of direct taxation—its cognitive prominence or highly conspicuous nature—that has fueled tensions between taxpayers and the state, across both space and time. To be sure, the introduction of any type of new tax, direct or indirect, is frequently accompanied by some level of protest.[64] Thus, it is difficult to generalize about the popularity of particular taxes.[65]

Still, we know that policy design and broader social, political, and economic conditions often affect the reception of new taxes. Under some circumstances, when taxes are levied as part of a national emergency, such as war or economic catastrophe, taxpayers may embrace the need to support the civic community and hence the state through increased taxes.[66] At other times, when rates reach unexpectedly high levels or the benefits of taxes are ambiguous or provided to perceived outsiders, taxes are less acceptable.[67]

In the United States, even the founding of the Republic is often associated with a tax revolt.[68] Unsurprisingly, commentators have debated the virtues and vices related to the pain of paying taxes.[69] Yet many agree that the existing U.S. system of income taxation, based on withholding and return filing, makes taxpayers highly cognizant of the coercive impact of taxation.[70]

---

see also Dennis J. Ventry Jr., *Americans Don't Hate Taxes, They Hate Paying Taxes*, 44 U.B.C. L. REV. 835, 841 (2011) (arguing that Americans do not necessarily hate taxes but rather hate navigating the "unduly burdensome process of paying" their taxes).

64 *See generally* Isaac William Martin & Nadav Gabay, *Tax Policy and Tax Protest in 20 Rich Democracies, 1980–2010*, 69 BRITISH J. SOCIO. 647, 648 (2018). Historians of democracy have shown that the introduction of new VATs has also triggered social protests. *See* PAUL ALMEIDA, MOBILIZING DEMOCRACY: GLOBALIZATION AND CITIZEN PROTEST 1–9 (2014).

65 Isaac William Martin & Heather Harper, *What Makes a Tax Policy Popular? Predicting Referendum Votes from Policy Text*, SOCIUS: SOCIO. RSCH. FOR A DYNAMIC WORLD (Jan. 1, 2021), https://journals.sagepub.com/doi/pdf/10.1177/23780231211066069 [https://perma.cc/QH9P-QRSK].

66 For more on how taxpayer consciousness and fiscal citizenship are heightened during national emergencies, see generally Mehrotra, *supra* note 63, at 944; and ZELENAK, *supra* note 63, at 1–2.

67 Martin & Harper, *supra* note 65, at 9.

68 BROWNLEE, *supra* note 22, at 2; Joseph J. Thorndike, *A Tax Revolt or Revolting Taxes?*, TAXANALYSTS (Dec. 14, 2005), http://www.taxhistory.org/thp/readings.nsf/ArtWeb/1BC5839831CD15EE852570DD0061D496 [https://perma.cc/L8WU-WHTX].

69 *See, e.g.*, Joseph J. Thorndike, *Hurts So Good*, N.Y. TIMES (Apr. 15, 2005) (arguing that the pain of paying taxes "keeps people vigilant" and helps hold the government in check); Grover Norquist, President, Ams. For Tax Reform, President's Advisory Panel on Federal Tax Reform: Ninth Meeting 119–21 (May 17, 2005) (comparing the argument for less painful tax filing to the argument for the guillotine); Lawrence Zelenak, *Justice Holmes, Ralph Kramden, and the Civic Virtues of a Tax Return Filing Requirement*, 61 TAX L. REV. 53, 57 (2007) (explaining that some argue that "taxes should be as visible and painful as possible, on the theory that the public will resist high levels of visible and painful taxes").

70 *See* Zelenak, *supra* note 69, at 57–59.

At the other end of U.S. fiscal policy—the transfer side of the tax-and-transfer system—American social welfare benefits are frequently provided in a much more inconspicuous manner. They are delivered either indirectly via the Internal Revenue Code or through public/private partnerships that obscure the pivotal role of the federal government. Indeed, as numerous scholars of comparative political economy have shown, the American welfare state is not so much a laggard compared to other affluent countries as it is a "hidden welfare state."[71]

The expansive and generous use of "tax expenditures"—as opposed to direct spending—to achieve social welfare objectives is one reason why the American welfare state is largely invisible to most everyday taxpayers. Popularly known as "tax breaks," these tax expenditures are technically defined as "departures from the normal tax structure . . . designed to favor a particular industry, activity, or class of persons."[72] Generally, tax expenditures take the form of deductions, credits, and outright tax exclusions, as well as preferential tax rates and even tax deferrals.[73] Within social policy, tax expenditures effectively parallel direct spending for things like "income security, health care, employment and training, housing, social services, education, and veterans' benefits," to name a few.[74] Rather than provide direct expenditures for these social welfare benefits based on citizenship or residency, as most other advanced countries do, the United States subsidizes these activities based mainly on employment status and tax payments. In short, by not taxing individuals, or by providing refunds on taxes already paid, tax expenditures essentially disguise the many ways in which the United States delivers anti-poverty relief, as well as social benefits to the middle class and the affluent.[75]

The scale and scope of U.S. tax expenditures supporting social policy underscore how prevalent and important this type of indirect spending is to the modern American fiscal and social welfare state. Overall, U.S. tax expenditures in 2019 totaled roughly $1.2 trillion, or nearly 5.8% of GDP.[76]

---

71 HOWARD, *supra* note 16, at 3–12; Jeffrey P. Owens, *Tax Expenditures and Direct Expenditures as Instruments of Social Policy*, *in* COMPARATIVE TAX STUDIES 171, 175–78 (Sijbren Cnossen ed., 1983).

72 HOWARD, *supra* note 16, at 3 (quoting STANLEY S. SURREY & PAUL R. MCDANIEL, TAX EXPENDITURES 2–3 (1985)). Surrey is often regarded as the intellectual godfather of tax-expenditure analysis. *See generally* Lawrence Zelenak & Ajay K. Mehrotra, *Editors' Introduction—Stanley S. Surrey: A Life in Taxes*, *in* A HALF-CENTURY WITH THE INTERNAL REVENUE CODE: THE MEMOIRS OF STANLEY S. SURREY (Lawrence Zelenak & Ajay K. Mehrotra eds., 2022).

73 HOWARD, *supra* note 16, at 3; Gravelle, *supra* note 15, at 406.

74 HOWARD, *supra* note 16, at 3.

75 *Id.*; HACKER, *supra* note 16, at 13–14.

76 BILAL HABIB, EDWARD HARRIS, JOHN MCCLELLAND & JOSEPH ROSENBERG, CONG. BUDGET OFF., THE DISTRIBUTION OF MAJOR TAX EXPENDITURES IN 2019, at 10 (Scott Craver ed., 2021).

According to the U.S Congress's Joint Committee on Taxation, social welfare-related tax expenditures were among the largest tax breaks provided to individuals in fiscal year 2021. In fact, the largest tax expenditure in that year, of roughly $190 billion, went to the exclusion of employers' contributions for employees' medical insurance premiums and medical care.[77] Similarly, the third- and fifth-largest tax expenditures were for tax-qualified retirement savings accounts, totaling in the aggregate an estimated $267 billion.[78] Finally, the federal government's ostensibly most robust anti-poverty program, the EITC, accounted for over $73 billion.[79]

Although most Americans may not realize they benefit from tax expenditures, the socioeconomic distribution of such indirect government spending mainly helps upper- and middle-class taxpayers. Because many of these benefits are generally tied to employment, the top two tax expenditures in 2019 were for the tax exclusion related to employer-provided health insurance and retirement security. According to the Congressional Budget Office, the leading 2019 tax expenditure of employment-based health insurance went to higher-income households, with 44% of the indirect spending accruing to households in the highest quintile of the income distribution.[80] By contrast, only 11% of this benefit went to the bottom two quintiles combined.[81] This is not to say that tax expenditures do not help the poor. The main U.S. anti-poverty measure, the EITC, is generally among the country's largest annual tax expenditures. And, in 2019, 82% of the benefits from the EITC accrued to households in the two lowest quintiles.[82]

In some cases, the indirect spending associated with specific tax expenditures surpasses the entire budgets of departments that spend money for related purposes. The value of tax breaks for homeownership, for instance, exceeds total spending by the U.S. Department of Housing and Urban Development.[83] Even though these tax benefits are distributed unevenly, with upper-income taxpayers benefiting, on average, more than

77 STAFF OF JOINT COMM. ON TAX'N, 117TH CONG., REP. ON ESTIMATES OF FEDERAL TAX EXPENDITURES FOR FISCAL YEARS 2019–2023, at 28 (2019).

78 *Id.* at 29. For a full list of the leading tax expenditures, see OFF. OF TAX ANALYSIS, U.S. DEP'T OF THE TREAS., TAX EXPENDITURES (2020), https://home.treasury.gov/system/files/131/Tax-Expenditures-2021.pdf [https://perma.cc/9FL2-PYBX].

79 STAFF OF JOINT COMM. ON TAX'N, *supra* note 77, at 29. For more on the EITC, see Hilary Hoynes, *The Earned Income Tax Credit*, 686 ANNALS AM. ACAD. POL. & SOC. SCI. 180, 180–93 (2019); and Anne L. Alstott, *The Earned Income Tax Credit and the Limitations of Tax-Based Welfare Reform*, 108 HARV. L. REV. 533, 533–36 (1994).

80 HABIB ET AL., *supra* note 76, at 12.

81 *Id.*

82 *Id.* at 2, 14.

83 *What Are the Largest Tax Expenditures?*, TAX POL'Y CTR., https://www.taxpolicycenter.org/briefing-book/what-are-largest-tax-expenditures [https://perma.cc/5SY6-HFCS].

low-income taxpayers,[84] overall knowledge about these tax breaks seems to be elusive. Many taxpayers either don't realize they are eligible for these tax benefits, or when they do, they underestimate the magnitude and importance of these tax expenditures.[85]

It is not only through the Internal Revenue Code that the United States obscures its social welfare spending. The methods that are used to further social policy also give the false impression that the public sector and public policy are absent; that somehow private spending on social welfare has emerged autonomously and separate from American politics and public policy. Scholars often refer to this distinctive U.S. system as a hybrid model of social spending or as the uniquely "America[n] public-private welfare regime."[86] As political scientist Jacob Hacker has explained:

> [P]rivate benefits, although nominally situated in the private sector, have become an essential adjunct to public social programs in the United States. They are systematically intertwined with public policy. They are molded by government intervention. They are fought over by political leaders. They are championed by groups that wish to preserve and expand them. The rise of private social benefits in the United States, in short, is as much a political story as the rise of public social benefits, and no less defining of America's distinctive path.[87]

Simply put, one cannot accurately gauge the extent of the American social welfare state without acknowledging how U.S. lawmakers have harnessed private power to enact public social welfare policies.

The concealed nature of American social policy further exacerbates the public's limited knowledge and misperception of the role of the public sector.[88] Looking beyond tax expenditures and public/private healthcare and retirement savings, scholars have shown that even more obvious forms of government assistance go unheeded by most everyday Americans. Consider student loans. As political scientist Suzanne Mettler has demonstrated,

---

[84] DANIEL BERGER & ERIC TODER, DISTRIBUTIONAL EFFECTS OF INDIVIDUAL INCOME TAX EXPENDITURES AFTER THE 2017 TAX CUTS AND JOBS ACT 5–6 (2019).

[85] *See* Jacob Goldin & Yair Listokin, *Tax Expenditure Salience*, 16 AM. L. & ECON. REV. 144, 148 (2014) (reporting survey findings for taxpayers' understanding of the charitable deduction and the home mortgage interest deduction).

[86] HACKER, *supra* note 16, at 6–12.

[87] *Id.* at 8. For more on the historical origins and development of the divided American social welfare state, see generally JENNIFER KLEIN, FOR ALL THESE RIGHTS: BUSINESS, LABOR, AND THE SHAPING OF AMERICA'S PUBLIC-PRIVATE WELFARE STATE 2–4 (2003); and MOLLY C. MICHELMORE, TAX AND SPEND: THE WELFARE STATE, TAX POLITICS, AND THE LIMITS OF AMERICAN LIBERALISM 1–16 (2012).

[88] METTLER, *supra* note 16, at 3–4. More specifically, Mettler defines the "submerged state" as including "a conglomeration of federal policies that function by providing incentives, subsidies, or payments to private organizations or households to encourage or reimburse them for conducting activities deemed to serve a public purpose." *Id.* at 4.

education loans once benefited from government subsidies provided to third-party private lenders.[89] Although the policy was eventually eliminated with the federal government taking more direct control over student loans, the dramatic change went little noticed by borrowers or others.[90]

The example of government-subsidized student loans highlights the political importance of optics. It demonstrates how the "submerged state" obscures the vital role of the public sector from the clear view of the general public, including those who are frequently the primary beneficiaries of these laws and policies. This invisibility not only makes the electorate oblivious to the positive role of government; it also makes them more passive. It conceals the state and amplifies the market. It marginalizes the public sector and magnifies the private realm. When government largess is provided indirectly via tax expenditures or funneled through third-party private institutions, citizens, taxpayers, and voters do not have a full understanding of how power operates. As a result, democratic deliberations are diminished, public opinions are distorted, and voters are left disengaged.[91]

The historical combination of an extractive fiscal state and shrouded social welfare spending has created a type of political cognitive dissonance. At times, Americans rail against an overintrusive government, yet they continue to enjoy the benefits of the public sector. Indeed, there appears to be a longstanding and odd disjuncture between American beliefs about governance and reality. As early as 1887, noted American journalist Albert Shaw acutely observed this tension. "The average American has an unequalled capacity for the entertainment of legal fictions and kindred delusions," wrote Shaw. "He lives in one world of theory and in another world of practice . . ." "[T]he people of the United States have assiduously pursued and cherished a practical policy utterly inconsistent with [laissez-faire] theory and have not perceived the discrepancy."[92]

A century later, U.S. lawmakers echoed Shaw's consternation about this incongruity. During his 1984 run for the presidency, U.S. Senator Ernest "Fritz" Hollings famously delivered several versions of a story about

> a guy who came home from the Korean War, went to college on a form of the GI Bill, opened a business with a Small Business Administration loan, made sure his parents' farm was adequately wired through Rural Electrification and irrigated with assistance from the Army Corps of Engineers, saw his kids get

[89] *Id.* at 69–87.

[90] *Id.*

[91] *Id.* at 5–6.

[92] William J. Novak, *The Myth of the "Weak" American State*, 113 AM. HIST. REV. 752, 753 (2008) (quoting Albert Shaw, *The American State and the American Man*, 51 CONTEMP. REV. 695, 696–97 (1887)).

> subsidized school lunches at a school that received lab equipment from a National Science Foundation grant, got his mortgage from the FHA and hurricane disaster relief from FEMA, and one day, took AMTRAK to Washington to complain to his congressman about getting big government off people's back.[93]

The mental misalignment between political beliefs and actual behavior continues to afflict American law and statecraft.

In many ways, this political cognitive dissonance has come to exacerbate the distrust between citizens and their government—a distrust fueled by many leaders on the political right. Roughly four decades ago, Republican President Ronald Reagan articulated and advanced this sentiment when he famously announced, "[G]overnment is not the solution to our problem; government is the problem."[94] Reagan's denouncement was part and parcel of a long historical process of politicizing the public sector—and the taxes that support it.[95]

As part of that process, many conservative politicians began perpetuating the myth that Americans were overtaxed compared to citizens of other advanced, industrialized nations. "I oppose any new spending programs which will increase the tax burden," President Richard Nixon proclaimed in 1972 as he accepted the Republican Party's presidential nomination.[96] "The truth is that Americans are overtaxed, not undertaxed," Jack Kemp claimed in 1993.[97] "Besides, it's not the people who need to sacrifice, it's the bloated Government."[98] More recently, false claims about high American taxes have also provided political cover for tax cuts. "The people of this country want tax cuts; they want lower taxes," President

93 *Id.*

94 Michael R. Adamson, *Reagan and the Economy: Business and Labor, Deregulation and Regulation*, *in* A COMPANION TO RONALD REAGAN 149, 149 (Andrew L. Johns ed., 2015).

95 Andrea Louise Campbell, *What Americans Think of Taxes*, *in* THE NEW FISCAL SOCIOLOGY: TAXATION IN COMPARATIVE AND HISTORICAL PERSPECTIVE 48, 48–67 (Isaac William Martin, Ajay K. Mehrotra & Monica Prasad eds., 2009).

96 Richard Nixon, Remarks on Accepting the Presidential Nomination of the Republication National Convention, PUB. PAPERS 790 (Aug. 23, 1972).

97 Jack Kemp, *Taxes vs. Growth*, N.Y. TIMES, Feb. 19, 1993, at A27, https://www.nytimes.com/1993/02/19/opinion/taxes-vs-growth.html [https://perma.cc/Y5M8-C9TP]. I have explored the myth of the overtaxed American elsewhere. *See generally* Ajay K. Mehrotra, *The Myth of the "Overtaxed" American and the VAT that Never Was*, 2 MOD. AM. HIST. 97 (2019). Remaining portions of this Essay are drawn from my earlier work.

98 Kemp, *supra* note 97.

Donald Trump repeatedly (and mistakenly) asserted. "We're the highest taxed nation in the world."[99]

Despite these claims, there is little empirical evidence to support the fable of the "overtaxed" American. Even a perfunctory review of well-known statistics shows that the United States is a stark outlier in how *little* it taxes its citizens. Turning once again to OECD data, one can clearly see that the United States is among the least taxed developed nations in the world.[100] For 2020, the United States had a total taxes/GDP ratio of 25.5%, well below the OECD average of nearly 34%, and far below other affluent countries such as France (45%), the United Kingdom (33%), and Germany (38%).[101] Moreover, the spread between U.S. taxes and the OECD average has been relatively consistent since 1965.[102]

Analyzing comparative tax data in other ways reinforces the claim that the United States remains a relatively low-tax country. When one examines tax revenue per capita, the United States is above the OECD average but still well behind other leading industrialized economies such as France, Germany, and the Nordic countries, which have the most robust social welfare states.[103]

To use another measure, consider the average income earner. A single worker with no children earning the average income in the United States has an effective or average tax rate of 28%, meaning that they retain approximately 72% of their annual income post-tax.[104] The OECD average tax rate for a similarly situated taxpayer is nearly 35%.[105] When one

---

[99] Rebecca Savransky, *Trump Repeats False Claim that US Is the Highest Taxed Nation in the World*, HILL, (Oct. 10, 2017, 1:12 PM), http://thehill.com/homenews/administration/354729-trump-repeats-false-claim-that-us-is-the-highest-taxed-nation-in-the [https://perma.cc/4T3J-EMZF]; John W. Schoen, *Sorry, President Trump, the US Is Not the 'Highest Taxed Nation in the World,'* CNBC (Sept. 6, 2017, 5:19 PM), https://www.cnbc.com/2017/09/06/sorry-president-trump-the-us-is-not-the-highest-taxed-nation-in-the-world.html [https://perma.cc/W9NF-YXA3].

[100] ORG. FOR ECON. COOP. & DEV., REVENUE STATISTICS 2021: INITIAL IMPACT OF COVID-19 ON OECD TAX REVENUES 3 (2021), https://www.oecd.org/tax/tax-policy/revenue-statistics-highlights-brochure.pdf [https://perma.cc/8SF9-RXWR].

[101] *Id.*

[102] *Revenue Statistics - OECD Countries: Comparative Tables*, *supra* note 57.

[103] In 2019, the United States had per capita tax revenue of approximately $16,000, while France and Germany were closer to $18,000, and Norway was at approximately $30,000. *See Tax Revenue Data*, COUNTRYECONOMY.COM, https://countryeconomy.com/taxes/tax-revenue [https://perma.cc/PLD7-LLR8]; *see also* OECD, *Tax Revenue*, https://data.oecd.org/chart/4TZt [https://perma.cc/9AFE-9U8C] (showing that the U.S. per capita tax revenue has been below the OECD average since approximately 2007).

[104] Cristina Enache, *A Comparison of the Tax Burden on Labor in the OECD*, TAX FOUND. (May 19, 2021), https://taxfoundation.org/publications/comparison-tax-burden-labor-oecd/#Country [https://perma.cc/KB3K-BT69].

[105] *Id.*

incorporates consumption taxes—in the form of VATs or sales taxes—into the analysis, the United States remains well below the OECD average for the total tax burden on labor.[106]

One explanation for the gap between the United States and other OECD countries is the conspicuous absence of a broad-based *national* U.S. consumption tax. Whereas all other OECD countries have such a levy, usually in the form of a VAT, the United States has throughout its modern fiscal history rejected any type of comprehensive federal tax on consumption, including even crude forms of a VAT. Because the VAT accounts, on average, for almost 7% of total taxes/GDP among OECD countries, the missing U.S. VAT explains much of the U.S. shortfall in total taxation as a percentage of GDP.[107]

III. HISTORICAL U.S. RESISTANCE TO NATIONAL CONSUMPTION TAXES

What explains the historical American resistance to broad-based national consumption taxes? Why is the United States the only OECD country without a VAT? Part of the answer to these questions may rest with the relationship between robust VATs and resilient social welfare states. As we have seen, there is a growing amount of empirical evidence linking regressive consumption taxes with progressive social spending.[108] Some commentators point to this correlation to suggest that a VAT lacks political support in the United States, from both sides of the aisle.

The regressive incidence of consumption taxes along with their potential to fund strong social welfare states may explain part of the historical American resistance to the VAT. Indeed, there is an old Washington, D.C., "inside-the-beltway" adage, often attributed—apocryphally perhaps—to Harvard University economist and former U.S. Treasury Secretary Lawrence Summers, which states that the VAT has failed in the United States because liberals fear that it will harm low-income

[106] *Id.*

[107] *Revenue Statistics - OECD Countries: Comparative Tables*, *supra* note 57. The United States does, of course, have consumption taxes at the state and local level in the form of state and local sales taxes. But these taxes account for only about 2% of GDP. *Id.*

[108] KATO, *supra* note 20, at 41; PRASAD, *supra* note 20, at 102, 149–51; Ganghof, *supra* note 21, at 370. Given the tight historical and comparative link between VATs and robust social welfare states, the central research question "Why no VAT in the United States?" is perhaps a subset of the classic Werner Sombart question "Why no socialism in the United States?" Or the more compelling contemporary question "Why so little social spending in the United States?" WERNER SOMBART, WHY IS THERE NO SOCIALISM IN THE UNITED STATES?, at xv–xvii (C.T. Husbands ed., Patricia M. Hocking & C. T. Husbands trans., Macmillan Press 1976) (1906).

Americans with its regressive incidence, and conservatives fear that it will be a "money machine" for big government.[109]

There may be a great deal of truth to the adage. But understanding empirically why American liberals and conservatives have resisted national consumption taxes requires a comparative and historical analysis of how these political preferences have come into existence and been shaped over time. Complex and changing historical contexts, both in the United States and abroad, have influenced how Americans have come to think about fiscal policy, about progressive taxation and social spending. Broad forces, seminal events, and the actions of key actors have all come together during pivotal and contingent historical moments to determine the development of American law and political economy.

To borrow language from the historical social sciences: the U.S. resistance to the VAT can be viewed as part of the "path-dependent process" of policymaking.[110] During previous "critical junctures," American lawmakers "locked in" U.S. fiscal policy down a particular path, with specific decisions that have subsequently created "feedback mechanisms" that may have ossified the U.S. resistance to broad national consumption taxes in general and the value-added tax in particular.[111] Although path dependency theory is not always clear about what constitutes "critical junctures" and how "locked in" certain policies become, the general concept is helpful in understanding the historical contingency of contemporary American fiscal policy.[112] It helps demonstrate that there is nothing natural, neutral, or necessary about the way we tax and spend today. In short, the past matters in understanding the missing U.S. VAT today.

A historical and comparative analysis shows that rejecting national consumption taxes was not the only path available to the United States. Throughout modern U.S. fiscal history, namely the long twentieth century,

---

109 Jan M. Rosen, *Tax Watch: The Likely Forms of New Taxes*, N.Y. TIMES, Dec. 19, 1988, at D2, https://www.nytimes.com/1988/12/19/business/tax-watch-the-likely-forms-of-new-taxes.html [https://perma.cc/T96M-X5NS]; Robert J. Barro, *The Coming Crises of Governments*, FIN. TIMES, Aug. 3, 2011, at 9, https://scholar.harvard.edu/barro/files/11_0803_thecomingcrises_ft.pdf [https://perma.cc/P3M9-ALY7]. Summers is purported to have said about a U.S. VAT: "'Liberals think it's regressive and conservatives think it's a money machine.' If they reverse their positions, a V.A.T. may happen . . . ." Rosen, *supra*, at D2.

110 *See* PAUL PIERSON, POLITICS IN TIME: HISTORY, INSTITUTIONS, AND SOCIAL ANALYSIS 17–22, 73, 85 (2004); JAMES, *supra* note 20, at 206–09.

111 W. Brian Arthur, *Competing Technologies, Increasing Returns, and Lock-In by Historical Events*, 99 ECON. J. 116, 117, 127 (1989). For an example of how path dependency theory has shaped corporate law, see generally Lucian Arye Bebchuk & Mark J. Roe, *A Theory of Path Dependence in Corporate Ownership and Governance*, 52 STAN. L. REV. 127 (1999).

112 On the limits of path dependency theory, see generally Adrian Kay, *A Critique of the Use of Path Dependency in Policy Studies*, 83 PUB. ADMIN. 553, 554–55 (2005).

there were several "critical junctures," or historically contingent moments, when American policymakers could have adopted a crude form of general federal consumption taxes but chose not to. In fact, well before France became the first nation-state to adopt a modern VAT in 1954,[113] Western industrialized countries were experimenting with simple forms of business sales taxes, frequently referred to as "turnover" taxes because they were imposed on the turnover of business inventory.[114] These early turnover taxes were rudimentary and imperfect business activity taxes that eventually evolved into modern VATs.[115]

In many cases, the emerging modern VATs complemented, rather than replaced, existing income tax regimes. Over time, these VATs became fiscal workhorses funding strong social welfare states.[116] If the United States had adopted even a crude federal consumption tax during earlier critical junctures, it might have followed the path of other advanced, industrialized countries towards a modern VAT. Thus, this Part explores several earlier periods of historical contingency—when political, social, and economic conditions suggested that U.S. fiscal policy was "up for grabs"—to begin the process of trying to understand why the United States continues to be a VAT laggard.[117]

There have been at least three pivotal periods in modern American fiscal history when the United States explored, but eventually rejected, national consumption taxes.[118] These periods share two key characteristics. First, in each of these episodes, the historical context afforded experts, lawmakers, and social groups the opportunity to reimagine American fiscal

---

[113] Kathryn James, *Exploring the Origins and Global Rise of VAT*, *in* THE VAT READER, *supra* note 18, at 15, 16. On the origins of the French VAT, see Carl S. Shoup, *Taxation in France*, 8 NAT. TAX J. 325, 328 (1955). *See generally* CARL S. SHOUP, THE SALES TAX IN FRANCE (1930) [hereinafter SHOUP, SALES TAX]; Mirja Salo, *The Ideas of Maurice Lauré on VAT in the 1950s*, 3 WORLD J. VAT/GST L. 130 (2014).

[114] Richard D. Pomp, *Turnover Taxes: Their Origin, Fall from Grace, and Resurrection*, 40 J. STATE TAX'N 17, 18 (2021).

[115] *Id.*, at 17.

[116] Richard W. Lindholm, *The Origin of the Value-Added Tax*, 6 J. CORP. L. 11, 13–14 (1980); *see also* James, *supra* note 113, at 15–16 (noting that "the VAT has been adopted by more than 140 countries and accounts for approximately 20 percent of worldwide tax revenue").

[117] In this sense, this essay is part of a larger, long-term research project exploring the historical American resistance to broad-based federal consumption taxes during the long twentieth century. For an overview of that broader project, see generally Mehrotra, *supra* note 97.

[118] Other scholars have identified several similar and different periods. *See generally* Steven A. Bank, *The Progressive Consumption Tax Revisited*, 101 MICH. L. REV. 2238, 2239 (2003); PRASAD, *supra* note 109, at 99–124; JOSEPH J. THORNDIKE, THEIR FAIR SHARE: TAXING THE RICH IN THE AGE OF FDR 123–30 (2013); Lawrence A. Zelenak, *The Federal Retail Sales Tax that Wasn't: An Actual History and an Alternate History*, 73 L. & CONTEMP. PROBS. 149, 150–72 (2010) (providing a history of the debates around federal taxation during World War II).

policy. Broad, deep-seated forces for reform provided the necessary backdrop, while seminal events, like global wars and other national emergencies, acted as triggers launching new ideas and policy prescriptions. Second, and perhaps most importantly, key historical actors, from leading experts—mainly economists and lawyers[119]—to legislators and politicians, to ordinary citizens working through voluntary associations, came to shape the future of American fiscal policy.

A. *The Failed Post-World War I Attempt*

From the late-nineteenth century to the ratification of the Sixteenth Amendment to the U.S. Constitution in 1913,[120] widespread forces for reform helped build the modern American fiscal state.[121] Leading experts, lawmakers, and social groups challenged the prevailing system of indirect and regressive taxes associated mainly with the nineteenth-century national tariff. In its place, these reformers sought to install a new fiscal regime, one based on the principle of "ability to pay," which had at its core the direct and progressive taxation of individual income and business profits.[122] This new tax system became the foundation for a revolution in American fiscal governance.

At the height of World War I, the unprecedented demand for government revenue to wage a global conflict built upon this foundation. In the process, the Great War became a seminal event that fundamentally transformed the U.S. tax system, and nearly every part of American society and the economy.[123] Before the war, the federal income tax was an anemic source of national revenue. In 1913, Congress enacted a mildly progressive national income tax that raised little federal revenue but sought to recalibrate the distribution of tax burdens according to the concept of ability to pay.[124]

Six years later, the international conflict revolutionized the income tax into a muscular fiscal machine. During the war, tax rates skyrocketed, and

---

[119] For more on the porous boundary between lawyers and economists in the making of law and public policy during this historical period, see generally Herbert Hovenkamp, *The First Great Law & Economics Movement*, 42 STAN. L. REV. 993 (1990); BARBARA FRIED, THE PROGRESSIVE ASSAULT ON LAISSEZ FAIRE: ROBERT HALE AND THE FIRST LAW AND ECONOMICS MOVEMENT (2009).

[120] U.S. CONST. amend. XVI.

[121] BROWNLEE, *supra* note 22, at 42–49.

[122] MEHROTRA, *supra* note 9, at 238.

[123] *See generally* DAVID M. KENNEDY, OVER HERE: THE FIRST WORLD WAR AND AMERICAN SOCIETY 111–13 (1980) (describing the fiscal revolution in the United States ushered in by WWI); CHRISTOPHER CAPOZZOLA, UNCLE SAM WANTS YOU: WORLD WAR I AND THE MAKING OF THE MODERN AMERICAN CITIZEN 6–17, 210 (2008); MEHROTRA, *supra* note 9, at 293–301 (detailing the dramatic changes in tax laws and policies that occurred during and after the war).

[124] The Revenue Act of 1913, ch. 16, 38 Stat. 114 (1913).

exemption levels dropped. Whereas the top marginal income tax rate was only 7% in 1913, by 1919, at the tail end of WWI, the top rate had jumped to 77%.[125] During the same period, exemption levels dropped to the point where nearly 20% of American wage earners were on federal tax rolls, an enormous increase from roughly 2% in the prewar period.[126] At the same time, innovative and highly complex "excess profits" taxes were levied on businesses, and an array of excise taxes was imposed on numerous everyday goods, from gasoline to chewing gum. Unlike other war participants, the United States funded a large portion of its war efforts with direct and progressive taxes on individuals and businesses.[127] Led by Democratic President Woodrow Wilson, the federal government actively transformed nearly every part of American state, society, and economy during the war.[128]

After the war, conservative Republicans swept into national political office and took control of policymaking. Elected in the wake of the war, these new leaders focused on economic retrenchment as an integral part of a "return to normalcy."[129] Their primary target quickly became the robust wartime fiscal state. Led by the new Treasury Secretary, Andrew W. Mellon, Republicans sought to slash top marginal tax rates, abolish the complex wartime profits taxes, and provide generous tax benefits to owners of capital.[130] On the other side of the political aisle, many progressive lawmakers and populist social groups wanted to retain the high "surtax" rates and the innovative wartime business levies to pay off war debts, fund a

[125] MEHROTRA, *supra* note 9, at 299.

[126] *See id.* at 293–342. *See generally* BROWNLEE, *supra* note 22, at 48–59, 77–78; HEW STRACHAN, FINANCING THE FIRST WORLD 79–82 (2004); STEVEN A. BANK, KIRK J. STARK & JOSEPH J. THORNDIKE, WAR AND TAXES 49–83 (2008); HUGH ROCKOFF, AMERICAN ECONOMIC WAY OF WAR: WAR AND THE U.S. ECONOMY FROM THE SPANISH–AMERICAN WAR TO THE PERSIAN GULF WAR 111, 115–18 (2012).

[127] ROCKOFF, *supra* note 126, at 115–18.

[128] For more on the transformative impact of WWI on American society, see generally KENNEDY, *supra* note 123, at 93–143 (describing the effects the war had on the U.S. political and economic front); ELLIS W. HAWLEY, THE GREAT WAR AND THE SEARCH FOR MODERN ORDER: A HISTORY OF THE AMERICAN PEOPLE AND THEIR INSTITUTIONS, 1917–1933, at 1–5 (1979); BARRY D. KARL, THE UNEASY STATE: THE UNITED STATES FROM 1915 TO 1945, at 34–50 (1983); and THOMAS J. KNOCK, TO END ALL WARS: WOODROW WILSON AND THE QUEST FOR A NEW WORLD ORDER 85–104 (1992).

[129] The phrase "return to normalcy" was famously invoked by President Warren G. Harding during the 1920 presidential campaign. *See generally* Justin P. Coffey, *Harding Biographies*, *in* A COMPANION TO WARREN G. HARDING, CALVIN COOLIDGE, AND HERBERT HOOVER 79, 83 (Katherine A.S. Sibley ed., 2014) ("Harding's famous call for a 'return to normalcy' struck a chord with voters, who longed for a time of peace and prosperity.").

[130] ROY G. BLAKEY & GLADYS S. BLAKEY, THE FEDERAL INCOME TAX 189–222 (1940); MEHROTRA, *supra* note 9, at 349–56.

veterans bonus, and perhaps even regulate large corporations.[131] During this political conflict, the broader American economy witnessed a severe, albeit brief, postwar recession, which brought further scrutiny to fiscal policy. Consequently, many Americans of all political stripes were open to fundamental tax reform.[132]

A comprehensive national consumption tax quickly became a popular idea at the time among several key historical actors. In 1920 and 1921, numerous business leaders recommended a "spending tax" to replace the income tax and the excess profits levies. Republican lawmakers, led by Utah Senator Reed Smoot and New York Congressman Ogden Mills, advanced a variety of consumption taxes, or "spending taxes" as they put it, that gradually gained some legislative traction.[133] Yet what was most intriguing about this pivotal postwar period was the idea of a proto-VAT proposed by Thomas S. Adams, a leading U.S. Treasury Department official and Yale University political economist.

Adams had a long and distinguished career as a "scholar in politics."[134] When he was a professor at the University of Wisconsin–Madison, Adams played a central role in advancing the Badger State's first effective income tax, which soon became a model for many other states and commonwealths.[135] During the war, Adams was also a principal spokesperson for the Treasury Department in congressional hearings; many of his studies and proposals were adopted during the conflict.[136] And even after the war, Adams was an influential figure in designing international tax laws and policies.[137]

Adams's primary goal in the postwar period was to preserve the progressive income tax. He agreed with some government critics that the wartime tax regime, with its high marginal tax rates and complex war profits taxes, had become an administrative burden for both the government and

---

[131] Anne Alstott & Benjamin Novick, *War, Taxes, and Income Redistribution in the Twenties: The 1924 Veterans' Bonus and the Defeat of the Mellon Plan*, 59 N.Y.U. TAX L. REV. 373, 374 (2006); PAUL DICKSON & THOMAS B. ALLEN, THE BONUS ARMY: AN AMERICAN EPIC 25–31 (Dover Publ'ns, Inc. 2020) (2004).

[132] BROWNLEE, *supra* note 22, at 61; Bank, *supra* note 118, at 2241–42.

[133] BLAKEY & BLAKEY, *supra* note 130, at 201, 203; Bank, *supra* note 118, at 2243.

[134] A. E. Holcomb, *George A. Boissard's Tribute to Thomas Sewell Adams*, 18 BULL. NAT'L TAX ASS'N 194, 194 (1933); Michael J. Graetz & Michael M. O'Hear, *The "Original Intent" of U.S. International Taxation*, 46 DUKE L.J. 1021, 1032 (1997).

[135] W. ELLIOT BROWNLEE, PROGRESSIVISM AND ECONOMIC GROWTH: THE WISCONSIN INCOME TAX, 1911–1929, at 62 (1974); MEHROTRA, *supra* note 9, at 231–48.

[136] BROWNLEE, *supra* note 135, at 60, 110; MEHROTRA, *supra* note 9, at 335–39.

[137] Graetz & O'Hear, *supra* note 134, at 1028–41.

taxpayers.[138] Yet, unlike the conservative lawmakers who sought to replace the income tax with a consumption tax, Adams had a more sophisticated vision of combining moderate progressive income taxes with a new business sales tax, and a series of lighter excise levies on commodities.[139]

In a seminal 1921 journal article, Adams made the case for the administrative simplicity and economic efficiency of his tax reform vision. "[T]he simple truth is that we are overburdening the income tax," Adams wrote.[140] "Nothing is more common in the history of taxation than the demoralization of what has been a good tax, as taxes go, by increasing its rates until the breaking point is reached."[141] To ease the burden on the income tax, Adams proposed a unique "modified business sales tax" as a replacement for the war profits taxes. "In the case of producers and sellers of 'goods, wares and merchandise' further simplicity could be achieved," he wrote, "by giving the tax the form of a sales tax with a credit or refund for taxes paid by the producer or dealer (as purchaser) on goods bought for resale or for necessary use in the production of goods for sale."[142] With this proposal, Adams provided the first conceptual articulation of what tax experts today would call a "credit-invoice" method of value-added taxation.[143] Adams was, thus, one of the intellectual fountainheads of the VAT.[144]

Adams was also a political realist. After several decades traversing between the academy and policymaking, he understood that economic logic and administrative simplicity did not exist in a vacuum. Broader social and political forces often determined the shape of tax law and fiscal policy. The U.S. victory in World War I, for example, seemed to assure the permanency of progressive income taxes. Because the United States had successfully

---

138 Thomas S. Adams, *Fundamental Problems of Federal Income Taxation*, 35 Q.J. ECON. 527 (1921) [hereinafter Adams, *Fundamental Problems*] (discussing the administrative burden of the wartime tax regime and the need for other taxes to relieve the administrative pressure on the graduated income tax); T. S. Adams, *Sales Tax Favorite Remedy for All the Ills of the Taxpayer: Expert Points Out Some of the Difficulties of Equal Levy, and Compares Operation with Present System*, N.Y. EVENING POST, August 2, 1920, at 9.

139 Adams, *Fundamental Problems*, *supra* note 138, at 528.

140 *Id.* at 536.

141 *Id.*

142 *Id.* at 553.

143 For more on the credit-invoice VAT, see SCHENK & OLDMAN, *supra* note 18, at 20; and BURMAN & SLEMROD, *supra* note 18, at 99–100, 107–09.

144 JAMES, *supra* note 20, at 1; CLARA K. SULLIVAN, THE TAX ON VALUE ADDED 12 (1965) (discussing the historical origins and early development of VAT proposals). I have elsewhere explored in greater detail how Adams navigated the tension between democracy and expertise in proposing the first proto-VAT. Ajay K. Mehrotra, *Experts, Democracy, and the Historical Irony of U.S. Tax Policy: Thomas S. Adams and the Beginnings of the Value-Added Tax*, MOD. AM. HIST. (forthcoming) (on file with author).

waged a global war with highly progressive income and complex war profits levies, Adams realized that few Americans would be willing to sacrifice the apparent fairness and effectiveness of the existing progressive income tax regime for a supposedly simpler yet possibly less equitable alternative. The democratic and popular will for fairness and equity would be difficult to overcome.

Indeed, Adams acknowledged the futility of his ideas. "The plan has little chance of adoption," Adams presciently observed about his proto-VAT proposal.[145] But that did not mean that one could not learn from this potential failure. In words that would resonate for decades as future U.S. policy makers and analysts considered other forms of national consumption taxes, Adams eloquently explained how and why the democratic desire for fairness and equity always seemed to overcome the economic logic of simplicity and administrative ease. The failure to adopt a consumption tax serves "the useful purpose of illustrating the futility of basing one's principles on one's personal experience," Adams conceded:

> It demonstrates the supreme necessity of subordinating administrative logic and personal predilections to the great political and social forces which control the evolution of tax systems. These forces must be accepted as facts. The historical fact is that modern states prefer equity and complexity to simplicity and inequality. The cry for equality and justice is louder and more unanswerable than the demand for certainty and convenience. You may think it sentimental and stupid, but that does not alter the fact.[146]

Adams's prediction soon came true. Although Senator Smoot proposed several types of "general sales taxes" during the 1921 legislative session, including a proposal that vaguely resembled Adams's proto-VAT, none of them was adopted by Congress.[147] The crude "spending taxes" championed by Smoot and others might have evolved over time into something resembling a VAT. Like European countries experimenting with a general sales tax at the time, the United States in 1921 could have adopted a broad-based national sales tax; doing so may have put U.S. fiscal policy on a different historical path—one that might have led to the subsequent adoption of a U.S. VAT and perhaps even a more vigorous social welfare state. Whereas European counterparts had crude forms of consumption (turnover) taxes in place that permitted them in later years to refine their commitment to taxing consumption, the United States had no such foundation—no history of effectively taxing consumption broadly at the national level. Thus, during

---

145 Adams, *Fundamental Problems*, *supra* note 138, at 554.

146 *Id.*

147 Bank, *supra* note 118, at 2239; BLAKEY & BLAKEY, *supra* note 130, at 87–88.

this critical juncture in global tax history, some nation-states appeared to have been more open and flexible than others.

One reason why the 1921 consumption tax proposals failed was the fractured support among business leaders. While some industrialists were eager to have a sales tax replace the wartime focus on progressive income and profits taxes, others were more concerned about the economic uncertainty of a new tax base. Anxious about how a new general sales tax might affect their bottom line, some businesses preferred to stick with a levy that was more predictable rather than experiment with a new tax that might have an adverse impact, especially during an ongoing economic recession.[148]

Others in the business community feared the political implications of moving from a highly progressive tax regime to a potentially regressive one. The National Industrial Conference Board, a leading business association created during the war, concluded that supporting a sales tax was "indefensible."[149] The Conference Board believed that the distributional consequences of shifting from progressive income and profits taxes to a regressive sales tax undermined their promotion of good corporate fiscal citizenship. The committee explained:

> We haven't the nerve, as good citizens of the country—which we believe we are, and are trying to be—to say to a body of business men in this country, who are suggesting that business be relieved from a billion dollars of excess profits tax, that we propose a tax which will cause the billion to be paid by the ultimate consumer. That is such a violent divergence from the principle of payment upon the basis of ability to pay, that we cannot ask this body of businessmen to get behind that sort of tax. . . .
>
> We don't think that is good citizenship; and we don't think that is good economics. That is the real reason that we . . . rejected the sales tax, upon the assumption that the tax is paid by the ultimate consumer.[150]

Thus, it was generally conservative business interests in 1921 that were uncertain and anxious about the regressive incidence of a sales tax.

Progressive advocates, who were eager to maintain the wartime tax regime, seized upon the business community's ambivalence. Organized labor and agricultural associations and their representatives in Congress came out strongly against the sales tax proposals.[151] As petitions from farm

[148] MEHROTRA, *supra* note 9, at 389.

[149] NAT'L INDUS. CONF. BD., PROCEEDINGS OF THE SECOND NATIONAL INDUSTRIAL TAX CONFERENCE: SPECIAL REPORT NUMBER 17, at 42 (1920).

[150] *Id.* at 40. For more on the importance of the concept of "ability to pay" as a touchstone for early-twentieth-century U.S. progressive taxation, see MEHROTRA, *supra* note 9, at 10.

[151] MEHROTRA, *supra* note 9, at 381–82.

federations and labor unions opposing the sales tax poured into congressional offices, leaders of these organizations testified before Congress about the unfairness of shifting to a consumption tax. "I believe that if the sales tax was substituted for the higher surtax brackets and the excess profits tax," proclaimed H.S. McKenzie of the American Farm Bureau Federation, "you would be putting an undue burden on the people who are already heavily burdened under the present tax rate."[152]

Just as Adams had predicted, the popular demand for fairness and the democratic desire for equity triumphed over administrative calls for efficiency and simplicity. Ultimately, the early-1920s potential for a profound change to the U.S. tax system dissipated into Treasury Secretary Mellon's grand plan for "scientific" tax reform based on tax cuts for the wealthiest Americans.[153] Thus, during the country's first opportunity to experiment with a broad-based national consumption tax, concerns about the regressive incidence of consumption taxes triumphed among both traditional groups on the political left, as well as some conservative business leaders.

B. Later Unsuccessful Efforts

The early-1920s attempt at a comprehensive national consumption tax may have marked the conceptual beginnings of the first serious U.S. consideration of a proto-VAT. But it was not the only historically contingent moment in the twentieth-century history of American fiscal policy. A second pivotal period occurred during the 1930s and 1940s when a new era of national crises, namely the Great Depression and the start of World War II, provided tax experts, national lawmakers, and social groups with another opportunity to reconsider broad-based national consumption taxes.

As historian Joseph J. Thorndike has persuasively shown, New Deal tax policy was rooted in the prior Republican response to the Great

---

[152] *Internal-Revenue Hearings on the Proposed Revenue Act of 1921 Before the S. Comm. on Fin.*, 67th Cong. 310 (1921); *Opposes Sales Tax., National Grange Representative Protests to a Senate Committee*, N.Y. TIMES, May 19, 1921, at 5, https://www.nytimes.com/1921/05/19/archives/opposes-sales-tax-national-grange-representative-protests-to-senate.html [https://perma.cc/FV89-WBAS] (describing opposition from a leader of the National Grange, the oldest American agricultural advocacy group).

[153] For more on the Mellon Plan, see Alstott & Novick, *supra* note 131, at 376–80; Lawrence L. Murray, *Bureaucracy and Bi-partisanship in Taxation: The Mellon Plan Revisited*, 52 BUS. HIST. REV. 200, 221–23 (1978) (discussing the bipartisan coalition that formed behind the Mellon Plan); M. Susan Murnane, *Selling Scientific Taxation: The Treasury Department's Campaign for Tax Reform in the 1920s*, 29 L. & SOC. INQUIRY 819, 821–41 (2004) (detailing the story of how the Mellon plan took shape); and ISAAC WILLIAM MARTIN, RICH PEOPLE'S MOVEMENTS: GRASSROOTS CAMPAIGNS TO UNTAX THE ONE PERCENT 5–7 (2013).

Depression.[154] During the early years of the Depression, the economic orthodoxy of balancing budgets dominated fiscal policymaking. The economic downturn devasted federal revenues, and by 1932 lawmakers were scrambling to find ways to increase revenue and balance the budget. Even conservative Republicans, like Mellon, conceded that a tax hike was necessary.

A variety of proposals were floated. President Herbert Hoover's administration recommended increasing individual and corporate income tax rates and lowering exemption levels for the personal income tax, as well as enacting a variety of excise taxes on an array of goods. The Hoover Treasury Department was led in late 1932 by the newly appointed Ogden Mills, after Mellon had been appointed ambassador to England. Although Mills had recommended a sales tax in 1921, and even alluded to the success of the 1930s Canadian general sales tax, he was reluctant to return to a failed proposal in his new, more powerful role. Instead, Mills echoed the administration's view that higher and broader income taxes along with more excise taxes on a variety of goods were the sound way to raise badly needed revenue.[155]

Others disagreed. The businesses affected by the tax hikes, particularly by the long list of excise taxes, protested. They recommended, instead, a general sales tax on all goods. In his testimony before the House Ways and Means Committee, T.S. Adams refrained from advocating for his proto-VAT. The harsh lessons of 1921 may have still resonated with him. Still, Adams described the Canadian general sales tax in glowing terms, indicating that perhaps it was time for the United States to experiment with a broad-based national consumption tax.[156] The anti-income-tax publisher William Randolph Hearst went even further in his support for a general sales tax as a replacement for the income tax. He financed a trip to Canada for U.S. policymakers to show them how the levy operated in that country. And he followed up his generosity with a publicity campaign in his newspapers "against the . . . Bolshevist system of income taxation."[157]

The powerful U.S. House Ways and Means Committee appeared persuaded by the sales tax proponents. In late 1932, it recommended a

---

154 THORNDIKE, *supra* note 118, at 123–30. For a different interpretation of New Deal tax policy, see generally MARK H. LEFF, THE LIMITS OF SYMBOLIC REFORM: THE NEW DEAL AND TAXATION, 1933-1939 (1984), depicting New Deal Tax Policy as insufficiently progressive.

155 THORNDIKE, *supra* note 118, at 28–30; BROWNLEE, *supra* note 22, at 66–69.

156 Revenue Revisions of 1932: Hearings Before the Comm. on Ways & Means, 76th Cong. 239–41 (1932).

157 THORNDIKE, *supra* note 118, at 39.

"manufacturers' sales tax" of 2.25% on all items except food.[158] But once again, "the great political and social forces which control the evolution of tax systems," as Adams noted, shaped tax policy.[159] A fractured business community remained divided on a general sales tax. Retailers staunchly opposed it. Manufacturers tentatively supported it. And those in specialized industries that were potentially impacted by the proposed excise taxes much preferred a general sales tax over the long list of particularized commodity taxes.[160]

Organizations representing everyday Americans, such as organized labor and agrarian associations, strongly opposed the general sales tax proposal, just as they had in 1921. In language reminiscent of the 1921 battles, the American Federation of Labor declared the sales tax an unfair burden on working citizens.[161] Similarly, the American Farm Bureau Federation reiterated its consistent objection. "A general sales tax is constantly opposed by the Farm Bureau for the broad reason that it is based on the necessity to consume rather than the ability to pay," declared one agricultural leader.[162]

Ultimately, the argument that a general sales tax—as opposed to particular excise taxes—affected the "necessity to consume" convinced most lawmakers to reject the 1932 proposals for a "general sales tax." Rank-and-file Democrats as well as a group of progressive Republicans came out against the sales tax, much to the chagrin of Senator Reed Smoot, who once again voiced his support for broad-based federal consumption taxes.[163]

Yet it was not simply the regressive incidence of consumption taxes that won the day. Instead, lawmakers focused on the element of volition that undergirded the difference between excise taxes and a general sales tax. They reasoned that a comprehensive national sales tax would affect nearly all goods and thus force all Americans to pay the levy in one way or another. By contrast, a series of isolated excise taxes, even a growing list of them, allowed people to choose whether to consume taxed goods. Excise taxes were, to be sure, regressive. But tax incidence was only one element of tax equity. In this sense, consumer choice became a touchstone of tax fairness. Similar calls to balance consumer choice against the need for greater revenue would be seen a decade later when another crisis hit American fiscal policy.

158 H.R. REP. NO. 72-708, at 8–10 (1932).
159 Adams, *Fundamental Problems*, *supra* note 138, at 554.
160 THORNDIKE, *supra* note 118, at 38.
161 *Id.*
162 H.R. REP. NO. 72-708, at 137, 206–09.
163 THORNDIKE, *supra* note 118, at 41.

In the early 1940s, the United States once again considered adopting a general national consumption tax. Crisis once again became the crucible for a possible fiscal transformation. In fact, just as the end of the First World War and onset of the Great Depression provided the historical plasticity to reconsider the federal government's primary tax base, so too did the start of World War II.

Led mainly by Republican legislators in Congress, and backed by business interests, the idea of a general sales tax once again gained momentum in the early 1940s.[164] Many supporters wanted a widespread and flat sales tax to replace the existing array of excise taxes on specific goods—an administratively simple and efficient tax scheme, similar to the one Adams had proposed. Others hoped that a general sales tax might still replace the progressive income tax entirely. Once the United States formally entered World War II, the tremendous need for government revenue and concerns about rising inflation led to increased interest in a general sales tax. Although President Franklin D. Roosevelt remained staunchly opposed to any type of broad-based federal consumption tax, his Treasury Department attempted to strike a compromise between congressional and business leaders on the one hand and Democratic lawmakers on the other.[165]

On September 3, 1942, as Congress was considering a new tax bill, Treasury Secretary Henry Morgenthau proposed what was arguably the most innovative proposal since Adams's proto-VAT: a progressive sales tax.[166] The Treasury recommendation was hardly simple or straightforward. Designed to supplement rather than replace the income tax, Morgenthau's complex proposal combined a flat 10% tax, refundable after the war, on all spending with a graduated spending tax that ranged from 10% to 75%. The proposal built upon earlier Treasury studies, including those conducted by T.S. Adams.[167]

Morgenthau's attempt at a compromise was futile and fleeting. Reminiscent of Adams's remarks, Morgenthau's proposal offered neither equity nor simplicity. Like most flat rate consumption taxes, it had a regressive bent. And with a complicated refund scheme, Morgenthau's plan was hardly a model of administrative simplicity.

Without any support from President Roosevelt and few advocates in Congress, the progressive spending tax was set to fail. Indeed, the Senate Finance Committee rejected the proposal almost immediately. *Washington Post* reporter Robert C. Albright summarized the ill-fated proposal when he

[164] *See generally* Zelenak, *supra* note 118, at 151–54.

[165] *Id.* at 159–60; THORNDIKE, *supra* note 118, at 38–43.

[166] THORNDIKE, *supra* note 118, at 241.

[167] *Id.* at 238–41.

wrote that the spending tax was "Morgenthau's morning glory — It opened Tuesday morning and it folded before noon."[168] Like its predecessors from the 1920s and 1930s, the failed 1942 national consumption tax foreclosed a possible path of fiscal development. Although it is impossible to predict what might have happened if President Roosevelt had supported Morgenthau's progressive spendings tax proposal, some scholars have suggested that it is possible that the United States might have emerged from World War II with a two-tax structure: a progressive income tax imposed mainly on the wealthy, and a comprehensive national consumption tax, perhaps even a VAT, levied more broadly on nearly all spending.[169]

If the two world wars and the Great Depression provided the crisis context for the early considerations of a national consumption tax, a third seminal moment came during a different type of crisis—a perceived crisis in educational financing. During the early 1970s, the presidential administration of Richard M. Nixon proposed a national VAT to fund education.[170] Once again, legal and economic experts played a pivotal role in both advancing the national consumption tax idea and in some cases opposing it. But unlike the past when crude forms of a proto-VAT or a progressive spendings tax were recommended, Nixon administration economists, led by Paul McCracken and lawyers such as Treasury official Edwin S. Cohen, favored a fully formed VAT that could raise sufficient revenue to underwrite a variety of social programs. Some of Nixon's aides were attracted to the idea of a national VAT. In an attempt to address growing social concerns about the financing of K–12 education, and to build his electoral base, Nixon proposed replacing local property taxes with a federal VAT to finance education.[171]

The origins of Nixon's education VAT began in 1969 with some initial discussions about adopting a VAT to help close a widening federal budget deficit.[172] Those discussions were quickly tabled, but not forgotten. Over the next two years, President Nixon created task forces and advisory

---

168 Bank, *supra* note 118, at 2249 (quoting Robert C. Albright, *Gallery Glimpses*, WASH. POST, Sept. 6, 1942, at B3).

169 For a description of such an alternative history, see Zelenak, *supra* note 118, at 173–74.

170 JAMES, *supra* note 20, at 344–47; Alan Schenk, *Prior U.S. Flirtations with VAT*, *in* THE VAT READER, *supra* note 18, at 52–63; ISAAC WILLIAM MARTIN, THE PERMANENT TAX REVOLT: HOW THE PROPERTY TAX TRANSFORMED AMERICAN POLITICS 82–83 (2008); Monoka Venters, Meghan V. Hauptli & Lora Cohen-Vogel, *Federal Solutions to School Fiscal Crises: Lessons from Nixon's Failed National Sales Tax for Education*, 26 EDUC. POL'Y 35, 44–46 (2012).

171 Venters et al., *supra* note 170, at 44–49 (discussing President Nixon's idea to replace property taxes with a national consumption tax for education).

172 ALLEN J. MATUSOW, NIXON'S ECONOMY: BOOMS, BUSTS, DOLLARS AND VOTES 51–53 (1998). *See generally* LEONARD SILK, NIXONOMICS: HOW THE DISMAL SCIENCE OF FREE ENTERPRISE BECAME THE BLACK ART OF CONTROLS (1972).

commissions to explore the details of a possible U.S. VAT, including one linking a VAT to revenue-sharing grants to states and local governments.[173] By 1971, his administration was working on a proposal that sought to replace local property taxes with a federal VAT to finance K–12 education.

The revolutionary idea of using a broad federal consumption tax to fund education, like its predecessors, was short-lived. Within a year, the growing opposition to Nixon's VAT undermined the proposal. Many of the same elements that had weakened support for earlier broad federal consumption taxes were evident in the 1970s. A skittish business community and a hostile Congress once again posed familiar, formidable obstacles. Liberal analysts and lawmakers continued to object to the regressive incidence of consumption taxes. Businesses remained nervous about a consumption tax's effect on consumption and, hence, their ultimate profits. And Congress continued to hesitate at the prospect of new taxes on its constituents.[174]

What's more, by the 1970s, there was a new barrier—one that exemplified the path-dependent structure of U.S. opposition to the VAT. By the post-World War II period, many state and local governments had come to rely on sales taxes as their central source of revenue. A federal tax dependent on the same tax base, namely consumption, appeared to be a challenge to subnational governments. The vertical competition of fiscal federalism appeared to be a serious threat. Consequently, many governors, mayors, and state and local treasury officials lined up against a national VAT, even though its revenues would have assisted state and local educational spending.[175]

Nixon's VAT was not the last attempt by a national leader to adopt an American VAT. In 1979, U.S. House Ways and Means Committee Chairman Al Ullman formally proposed a 10% national VAT. Ullman's proposal not only failed, but he also lost his subsequent reelection bid. And many politicians thereafter became reluctant to recommend any type of national consumption tax, let alone a VAT.[176]

While the United States continued to reject the VAT, other developed countries that were also VAT laggards began in the 1980s to reconsider their historical resistance to value-added taxes. Indeed, throughout the 1980s,

---

[173] Edwin L. Dale Jr., *Nixon Weighing Revenue Sharing Linked to 'Value-Added' Tax*, N.Y. TIMES, Dec. 21, 1970, at 17.

[174] Venters et al., *supra* note 170, at 49–52.

[175] JAMES, *supra* note 20, at 346; MARTIN, *supra* note 170, at 82–83.

[176] MICHAEL J. GRAETZ, 100 MILLION UNNECESSARY RETURNS: A SIMPLE, FAIR, AND COMPETITIVE TAX PLAN FOR THE UNITED STATES 72 (2008); Schenk, *supra* note 170, at 58; Joseph J. Thorndike, *Tax History: Is the VAT a Career Killer for Politicians?*, TAXANALYSTS (Dec. 12, 2013), [https://perma.cc/G7ZG-TDGM].

several affluent nations, including Australia, Canada, and Japan, adopted a national VAT.[177] Each of these countries had its own particular historical, social, and political reasons for rejecting VATs earlier. But each was able to overcome the lock-in effect of decisions made at earlier critical junctures to put its tax system and society on a new and different path. Path dependency seemed to have its limits in explaining their reconsideration of a VAT. Thus, by the dawn of the 1990s, the United States was squarely an outlier as the only advanced, industrialized country without a VAT.

CONCLUSION AND CODA

It is well-known by now that income and wealth inequalities have been soaring for the past half-century across the globe. Although some developing countries have seen a decrease in poverty and a rising middle class during that period, much of the world has experienced dramatic increases in within-country economic disparities. In the United States, the growing concentration of wealth has been particularly pronounced, especially at the top end of the socioeconomic spectrum. While the details of this increase have been debated recently by experts, most agree that both income and wealth inequality have increased significantly.

One prominent obstacle to addressing U.S. inequality has been the fractured nature of the modern American fiscal and social welfare state. The combination of a highly salient federal system of direct and progressive taxation and a more shrouded social welfare state has led to a unique type of political cognitive dissonance that, in turn, has helped perpetuate the myth of the "overtaxed" American—a myth that has been exploited by anti-statist politicians and lawmakers for decades.

This fable has, in part, prevented the United States from joining the rest of the developed world in adopting a comprehensive national consumption tax such as a VAT. Whereas most other affluent nation-states have a VAT that underwrites robust social spending, the United States remains an outlier in terms of both its fiscal and its social policies. As a result, the United States is constrained in its ability to generate the large-scale revenues necessary to fund robust social welfare programs and thus address inequality. Dispelling the myth of the "overtaxed" American might be the first step toward a profound restructuring of American fiscal policy—a restructuring that could include a U.S. VAT to fund new social spending and expand existing anti-poverty efforts.

Many of the existing VATs in the developed world gradually emerged from other cruder forms of consumption taxes that were adopted earlier in

[177] JAMES, *supra* note 20, at 170, 241.

the twentieth century. On several occasions throughout the twentieth century, the United States had its opportunities to experiment with similar rudimentary, broad-based consumption taxes. In fact, there were at least three pivotal periods of historical contingency when the United States could have adopted a comprehensive federal consumption tax but chose not to.

This Essay has begun the process of examining why there is no U.S. VAT by identifying three critical junctures in the path-dependent process of fiscal policymaking. By focusing mainly on the first period of the early 1920s, this Essay has shown how the political, economic, and social conditions of the post-World War I period provided the backdrop to the ideas of one prominent tax expert who became the intellectual progenitor of the VAT. As a pragmatist and political realist, Thomas S. Adams anticipated that his proto-VAT would have little chance of adoption. It was, as he predicted, doomed to failure.

Still, there were lessons to be learned from failure—lessons, as Adams noted, about the "the great political and social forces which control the evolution of tax systems."[178] Similar lessons might be drawn from the other historical periods—those moments of similar national crises—when the plasticity of U.S. fiscal policymaking could have permitted national experimentation with a comprehensive federal consumption tax. Future research on the broad forces, seminal events, and key historical agents in each of these unsuccessful attempts will likely shed further light on the critical question: why no U.S. VAT?

* * *

Yet even if these history lessons can help us prepare for the next fiscal crisis or critical juncture, there is no guarantee that embracing a U.S. VAT would mitigate inequality. A U.S. VAT would not be a panacea for addressing existing economic disparities. Many other countries that have a VAT and expansive social spending have also witnessed increases in inequality over the last four decades. Moreover, the current distribution of tax expenditures suggests that U.S. social spending is not always aimed at alleviating poverty or combating inequality. Most importantly, the United States has a particular history, one that is coded with a general skepticism about centralized authority and a particular racialized view of social spending, that might prevent it from using a muscular VAT to fund new and existing social welfare benefits. Thus, adopting a VAT might be just one necessary but insufficient step in combating the growing concentration of wealth.

---

[178] Adams, *Fundamental Problems*, *supra* note 138, at 554.

To be sure, there are many ways to address growing inequality. Numerous scholars and policymakers have focused mainly on reducing the top end of inequality by taxing the rich.[179] They have recommended, among a variety of proposals, bolstering the existing system of direct and progressive taxes by increasing top marginal tax rates, removing the preference for capital gains, and even adopting new types of wealth taxes. These are sound ideas. Taxing the rich is, indeed, one way to mitigate high-end inequality. But there are other ways to tackle inequality beyond "soaking the rich," including elevating more people out of poverty and into the middle class and addressing the longstanding stagnation of middle-income wages and post-tax earnings. If one of the goals of progressive reforms aimed at greater human flourishing is to provide more material support and social rights for the middle and lower classes, then perhaps we should look beyond "soaking the rich" to elevating those below. Finding the missing U.S. VAT might just be one way to begin that process.

179 *See, e.g.*, Piketty & Saez, *supra* note 24, at 1–41; Scheuer & Slemrod, *supra* note 34, at 207; Batchelder & Kamin, *supra* note 44, at 2; David Leonhardt, *Taxing the Rich: Americans Strongly Favor Raising Taxes on the Rich. Why Are Democrats Struggling to Do So?*, N.Y. TIMES (Oct. 7, 2021), https://www.nytimes.com/2021/10/07/briefing/corporate-democrats-taxing-the-rich.html [https://perma.cc/X2UJ-DB2L]; Jason Furman, *Biden's Better Plan to Tax the Rich*, WALL ST. J. (Mar. 28, 2022, 6:24 PM), https://www.wsj.com/articles/bidens-better-plan-to-tax-the-rich-unrealized-capital-gains-assets-treasury-distortion-11648497984 [https://perma.cc/RH5H-7CW6].