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Pension plan, nearest ~~that~~
analogy to K gain.

When draw pension, pay
tax on everything above
contribution.

If you die, ~~no asset~~
~~remain~~ no step-up of basis
for widow.

Can't borrow on it.

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First, those with monetary assets and fixed incomes are the obvious, immediate, primary victims of inflation. (39); Second, most real assets, not just "capital" assets, yield phantom income. (39); Third, the ordinary	

cash flow of land, or ground rent, includes no phantom income because there is no depreciation. (41); Fourth, land is vulnerable only if title is sold, which is seldom. (41); Fifth, equities gain when inflation lowers the real value of debt. (42); Sixth is the matter of phantom recoupment, the point at which we entered this question. (42)

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among them. Let's redouble those efforts. But this "single-tax limited" is, indeed, inherently limited and limiting. It is not getting us into the larger public dialogue on the grand issues George used to inspire and move a generation.

Present at the creation: single-tax and income tax

It is a Georgist policy issue to see land pays more income tax, and earned income pays less. Many modern Georgists see the income tax as just another tax on production, and damn it whole. Cursing makes no nice distinctions. They would do better to analyze the tax: it taps a lot of land rent, and also commands the public dialogue. If you want Georgist action along Pennsylvania Avenue, it is here.

Georgists have not always held aloof from income taxation and its structuring. Let's review some history. Henry George himself called income taxation a second choice¹⁰ -- not first, but not last either. George and Georgists were "present at the creation" of the American income tax. You will be surprised at what a key role they played.

Recall that Congress enacted an income tax in 1894. There were 50 Populists in the House then, and six active Georgists (some of whom were Populists). These six all supported an amendment to the income tax act, by Judge James Maguire of California, to make it a direct tax on land rents. The constitutionality of Judge Maguire's amendment was assured by apportionment of the tax among states by population.

Judge Maguire's amendment failed. But we still owe a debt to those six: Tom Johnson and Michael Harter of Ohio; Jerry Simpson, Kansas; John de Witt Warner and Charles Tracy, New York; and James Maguire, California. We may reasonably surmise a bloc of six committed, zealous Congressmen, several within a larger bloc of 50 Populists, was what kept land rents in the base of the 1894 Act. They could block any income tax bill that excluded land income. So Congress did include land income in the base of the 1894 tax. This in turn provoked the Supreme Court into holding the 1894 Act unconstitutional¹¹, on grounds that a "direct" tax

¹⁰Charles Barker, Henry George, p. 605, n. 1.

¹¹Pollock v. Farmers' Loan and Trust Co., 157 U.S. 429 (1894); rehearing, 158 U.S. 601 (1895).

had to be apportioned among states by population. (Such apportionment was unacceptable in Congress, just as James Madison and Alexander Hamilton had planned a century earlier.)

Since they couldn't get an income tax exempting rents, income taxers were forced into engineering the 16th Amendment (1913) which removed the original constitutional roadblock (apportionment) to direct taxation of land rents. Congress has been taxing land rents ever since.

It even has the power, if it wishes, to exempt all other forms of income and limit the tax to rent. Is that an impossible dream? Not really. The maligned corporation income tax is a tax purely on property income. In the 1960s new capital achieved partial de facto exemption via fast write-off. Expensing is tantamount to total exemption. If we tax the profits of property, and relieve new capital, what is being taxed but land rent? We had a "graded tax plan" nationally, and never knew it!

Five of the six Georgist Congressmen, all but Maguire, were retired in the McKinley landslide of 1896, but that was not the end of Georgism in Congress. In the early 20th century Georgism bounced back, and was never stronger than during The Progressive Era when the income tax was molded and cast. Henry George Jr. represented Brooklyn for many terms. Newton Baker and Louis Post and Brand Whitlock and others served in Wilson's administration.

A key player was single-tax Congressman Warren Worth Bailey of Johnstown, Pa. Bailey was not just present at the creation of modern income taxation, he was the mid-wife. These excerpts from historian W. Elliot Brownlee¹² bring out the point. The underlining is mine.

...Wilson had to ask for significant tax increases. ... he supported new taxes that shifted the American tax system in a highly progressive direction. ... The boldness of the progressive shift is without equal in the history of American taxation. ...hostility to concentrations of power and wealth was politically potent. ... it was necessary for him to confront the powerful support for pursuit of social justice through redistributational taxation. The result was a commitment

¹²W. Elliot Brownlee, "Wilson and Financing the Modern State: The Revenue Act of 1916". Proceedings of the American Philosophical Society 129 (2), 1985, pp. 173-210.

to not only income taxation, but highly progressive forms of income taxation.

... with the Underwood Tariff of 1913, ... Wilson ... accepted the risk that tariff revenues might fall short. (Note: this was George's strategy in pushing free trade: substitute land revenues for tariff revenues. -- M.G.) ... Wilson firmly rejected the options of borrowing ...

... the Democratic critics of Wilson attacked the plan to broaden the income taxation to lower income groups and to add new excise taxes.

... The Democrats (abovementioned) ... were a diverse group of single-taxers, socialists, and inheritors of Populist traditions. ... For Warren Worth Bailey, for example, the war confirmed a belief in single-tax doctrine, in the necessity of taxing away economic rent not only to insure equality of opportunity but also to prevent destructive international competition.

... They wished to replace taxes serving the appetites of special privilege with taxes that would ... confiscate monopoly profits.

... The most vigorous leadership of the income tax movement rested with labor, representatives of farmers, and single-taxers. They believed that income taxation should reach only those incomes earned by monopoly power.

... Lending a powerful thrust ... was Congressman Warren Worth Bailey, from Johnstown, Pa. His personality and ideas dominated much of the early legislative activity behind the development of an alternative to Wilson's December program. ... Bailey was an articulate, energetic spokesman for single-taxation. ... he became an important liaison figure between the Wilson Administration and the single-tax movement, which, fueled by the capital of messianic Joseph Fels, gained significant strength in 1912 and 1913.

Bailey also became the leader of a small band of single-tax congressmen ... on behalf of taxes on the 'unearned increment' stemming from landownership ...

Bailey's career illustrates how the single-tax movement, reinforcing the Populist heritage, advanced the adoption of a progressive income tax. ... Louis Post ... supported income taxation ...

... Bailey wrote ... urging ... financing preparedness by wealth taxes. ... he called for 'an increase in the tax on incomes exceeding \$25,000 a year.' He advocated, as well, 'an inheritance tax levied upon

swollen fortunes,' a measure that single-tax Senator Edward Keating of Colorado had proposed to him.

...a surtax ... on incomes in excess of one million dollars. This measure surfaced as the recommendation of ... a diverse group of radical urban-progressives, single-taxers and socialists. John Dewey, Frederic C. Howe, Amos Pinchot, and George L. Record were among the founders. ...

Wilson even moved towards taxing unearned increments as they accrue, not waiting for realization in cash. This would give the income tax some of the character of a property tax. Now hear this, you who despair of professional economists. Are you ready? Most mainline tax theorists agree with Wilson. The names of Professors Haig and Simons make up the codeword. "Haig-Simons" taxable income includes land gains at the time they accrue, regardless of any sale.

The U.S. Supreme Court ruled against Wilson¹³ because Congress hadn't authorized what his Treasury officers did. But The Court then and later clearly opined Congress may tax unearned increments when and how it will¹⁴. That gives a notion how intimate is the nexus between property and income taxation.

Seven decades of creeping regress

If the capital gains exclusion is revived it will nearly complete a transformation of the income tax from its original form, including the handiwork of single-taxer Warren Worth Bailey, to a tax on work and enterprise of the median citizen. The transformation will never be literally "complete": property never sleeps. Already the road leading back to McKinley is posted

¹³Eisner v. Macomber, 252 U.S. 189 (1920)

¹⁴"...Congressional taxing power is not seriously restricted by such an implied requirement (Macomber) ... Congress is free to treat gains and losses as 'realized' pretty much whenever it chooses." Marvin Chirelstein, Federal Income Taxation (1979). 2nd Ed. Mineola NY: The Foundation Press, p. 69. Chirelstein is a Yale law professor, and this source is "the law student's bible".

and blazed with the "cash flow tax"¹⁵, and VAT. But here we just look at how Congress has changed the income tax to date.

a. Wage and salary withholding came in 1941, along with higher rates in lower brackets, converting a tax primarily on property income into a mass payroll tax. State and local public employees, previously exempt, were added to the base in 1939.

b. "Bracket creep" during inflation has pushed most workers into higher rate brackets, with no increase of real income.

c. The effect of bracket creep has been reinforced at the bottom, where most wage and salary income is found. The real value of personal exemptions has fallen, as the dollar allowances have fallen behind inflation. Labor-oriented favors to earned income have been all but wiped out.

d. The effect of bracket creep has been offset at the top, where most rents and capital gains are, by lowering the top rate from 70% to 28%.

e. Bracket creep has raised the average tax rate applied to personal income, because of the graduated rate structure. At the same time it has not raised the average rate applied to corporations, which are immune to bracket creep because the corporate rate is basically flat (with trivial exceptions at the bottom). The corporate share of total tax revenues has fallen sharply. Now, in addition, Congress has lowered the flat corporate rate from 46% to 34%.

f. The high, rising payroll tax (FICA) today raises more money than the corporate income tax, which originally dwarfed it.

g. Preferential treatment of land rents and gains has grown in several dimensions. This entails much more than the partial exclusion of gains from taxable income. The details comprise most of what follows.

The cumulative effect of those seven changes in federal taxation is totally to transform the income tax from the original

¹⁵Aaron and Galper actually propose expensing all land purchases under such a tax. This is proposing to exempt land 100%, then subsidize each successive buyer. Henry Aaron and Harvey Galper, Assessing Tax Reform. Washington: The Brookings Institution, 1985, p.76.

ideas voters had before them in 1913, and what Congress had in mind in 1916 when it passed the first important revenue measure following the 16th Amendment. A tax on the privileges of the idle rich ("idle" meaning with unearned income) has become a tax on the necessities and earnings of the working poor.

The shift of taxes off rent-yielding property is the more striking when we add in the States. In 1920 fully 50% of State revenues came from State property taxes; today hardly any. Almost all local revenues were then from property; today much less than half. Sales and income taxes have replaced them.

One bright, or at least light gray spot in this dark history is the relief of new investment from taxation under JFK, in a compact known as "business Keynesianism". Walter Heller was Chair of the CEA, perhaps the only really influential Chair that group ever had. Heller sold the idea of offsetting the effect of high income tax rates by allowing fast write-off of most new investments, plus an investment tax credit (ITC).

The policy is effective in theory, and proved so in practise. The high tax rate applies in full force to land rents; new investment gets major relief. Net result: an income tax that achieves nationally the goal Georgists chip at piecemeal from town to town. We actually had a species of national "graded tax plan", uptaxing land and downtaxing capital.

Most Georgists were watching the play on a different court. Investors who responded to the lures of accelerated depreciation, and lawyers who worked on intricate moves to exploit them, never dreamed they were responding to ideas originating with a radical reformer from the 19th century. They may not have cared, but we do: let's have a look.

The provenance of Heller's idea shows the influence of a Georgist academic, John R. Commons (1862-1945). If W.W. Bailey left his tracks on the Internal Revenue Code, Commons left his on thinking in economics at The University of Wisconsin. Commons was the leading "institutionalist" thinker; the Economics Department at Wisconsin-Madison was the leading institutionalist center. "Institutionalist" translates roughly as "relevant", from which it follows that Madison produced much more than its share of the country's practising tax economists -- including Walter Heller.

Commons views on taxing land and exempting capital and wages are set forth strongly in his Institutional Economics¹⁶. There is little difference between Commons' views and Henry George's, except the style, date, and a more tempered view of things. Here is Commons: "... the man who gets his wealth by mere rise in site-values should pay proportionately higher taxes than the one who gets his wealth by industry or agriculture. In the one case he extracts wealth from the commonwealth without adding to it. In the other case he contributes directly to an increase in both private wealth and commonwealth."¹⁷

Commons was politically active. His Georgist commitment was overt. He helped write and campaigned for the Grimstad Bill of 1921, to exempt capital from the property tax in Wisconsin, and raise the rate on land values.¹⁸ The Keller Bill, H.R. 5733, Jan. 1924, was in part modeled on Grimstad.¹⁹

Unlike George, Commons addressed the income tax. He wanted capital taxed less than land. The device he favored is fast write-off of new investments²⁰, the very idea Walter Heller put across in Washington. His purpose is overtly, explicitly to make the income tax bear heavier on land rents than on the returns to capital.

The link between Commons and Heller is Professor Harold Groves, a beloved avuncular figure who taught public finance at Madison and inspired many careers. Groves worked in tandem with Commons in the Wisconsin State Legislature, where Groves was an Assemblyman.²¹ Heller took his degree and worked closely with Groves, who launched him professionally. Groves was well disposed

¹⁶Madison: University of Wisconsin Press, 1961; first published by The Macmillan Company, 1934. Volume Two, Chapter X, pp. 815-40 expound Commons' tax theory. It is almost pure Henry George, rephrased in Commons' distinctive lexicon.

¹⁷Commons, op cit., p. 819.

¹⁸John R. Commons, "A Progressive Tax on Bare Land Value". Political Science Quarterly XXXVII (1), March 1922, pp. 41-68. Also see Harold Groves, Financing Government. New York: Henry Holt and Company, 1945, p. 380.

¹⁹Commons, op cit., pp. 823-24.

²⁰Commons, op cit., p. 833.

²¹Commons, op cit, p.841.

to Commons' views, as evidence by his writings²² and by his joining TRED, the Committee on Taxation, Resources and Economic Development. TRED at that time was fully committed to forwarding the ideas of Henry George.²³ Groves thoroughly approved, and supported us warmly. Only his failing health and early death kept him from leading the group.

Heller himself, before heading The CEA, wrote favorably (if diffusely) of using land taxation more heavily in what were then called less developed countries²⁴. Heller's striking achievement, however, was stimulating investment by applying and developing the idea of fast write-off for new capital. This is the idea that Commons saw could do through the income tax what George would do through the property tax.

Fast write-off comes and goes. Reaganites revived it for a time as part of "supply-side economics". They often cited the Heller precedent as their authority. So Heller lives; Commons lives; George lives: you just need to look in the right places.

1986: retrogression dressed as The Tax Reform Act

In 1986 Congress eliminated the most Georgist feature of income taxation, viz. the preferential treatment of new investment in real capital formation. The three changes were:

1. Repeal of Investment Tax Credit (ITC).

²²Harold Groves, Financing Government, Chapter XVII, "Taxation of Natural Resources", pp. 362-84. This chapter draws heavily on Commons. It devotes more space to George and land taxation, and treats it more sympathetically, than any other standard text. See also "The Property Tax in Canada and the United States", Land Economics 24, pp. 23-30, and 120-28, 1948. See also "Impressions of Property Taxation in Australia and New Zealand", Land Economics 25, pp. 22-28.

²³One cannot say the same of today's TRED. It has regressed toward the mean since Groves' time. Groves himself avoided that fate, in part thanks to Mrs. Groves, the former Helen Hoopes, an ardent single-taxer.

²⁴Walter Heller, four chapters in Haskell Wald and Joseph Froomkin (eds.), Papers and Proceedings of the Conference on Agricultural Taxation and Economic Development. Cambridge, Mass.: Harvard Law School, 1954. The Introduction by Stanley Surrey credits Heller with additional major contributions to the overall research.

2. Lengthening tax lives.

3. Decelerating depreciation pathways.

These changes have raised the effective tax rate on most new investment. Traditional liberals applaud them as closing loopholes. Economists, conservative or liberal, have been enchanted by "uniformity". Even Citizens for Tax Justice, a labor union tax lobby, has chimed in with praise and support for the 1986 reform²⁵. Their zest for taxing new investment seems now to override their former support of a progressive rate structure.

Uniformity is a good rule as between mutually convertible things. Land and capital are inconvertible, so incentive taxation may treat them differently. Incentive taxation is not uniform, it is -- pardon the expression -- Keynesian. Keynes always focused on the "marginal efficiency of capital", which in modern business lingo translates into the rate of return at the margin. The average rate of return includes rents; the marginal rate of return does not, it is the incentive to invest, the pure return to new capital as such. Incentive taxation distinguishes new assets from old. It takes a smaller bite from new investment and a larger bite from old, especially from land, the oldest of all.

The effect of closing these three loopholes for new investment is much the same as broadening the property tax base to include buildings, plant and equipment, etc. When combined with lowering the maximum tax rate, it is the same as shifting the tax off land and onto new buildings and other capital. Georgists see it so clearly at the local level, with respect to property taxes; we must tune in to what's happening to income taxation at the national and state level. Fast write-off (accelerated depreciation, expensing, et al.) equals tax relief to stimulate investment in, and creation of, real new capital.

Before 1986 a high-bracket professional -- physician, lawyer or actor -- could avoid the effects of high marginal tax rates by investing in certain kinds of real new capital: buildings, equipment, machines, rolling stock, furnishings and fixtures, trees, vines, or livestock. This did, it is true, make for overcapacity in certain kinds of capital, e.g. avocado trees in

²⁵Bruce Fisher, "Bush Crowd has a Plan", L.A. Times, 2 Oct 89, Section II p. 5. Fisher is research Director, Citizens for Tax Justice, Washington D.C.

California, offices in Texas. Some forms of capital received much more exemption than others. I will not defend the abuse. But today that professional is better off buying up old capital and land. Corporations are moved to join the merger-mania which creates no new wealth at all.

This poses worse problems, like overpricing land, and pricing median investors out of the market. It also tends to reduce saving and domestic capital formation. This is the message of many new economists like James Poterba²⁶, whose chapter is in these covers.

What are "capital gains"?

The 1986 tax reform was a massive shift of income tax liabilities off land (by lowering the top rates), and onto new investment (by decelerating write-off). Its only saving grace, from the viewpoint of Georgist incentive and redistributive taxation, was eliminating the preferential lower tax rate on capital gains. (Technically, it eliminates the exclusion of part of long-term gains from the base). The "saving grace" was a political bargain, to maintain some of the social compact while lowering the top rates from 70% to 28% in history's most massive shift toward a flat rate income tax. Now one side of the bargain is being reneged, "driving a stake in the heart" of the 1986 compact²⁷. The Administration is losing much goodwill with Congress on this single issue, risking its ability to govern. What are capital gains to warrant such hazards?

The term "capital gains" is a disguise, artfully contrived, growing more obfuscatory with long usage and growing complexity. It is the nature of most actual capital to depreciate, usually fast. There are few true resale gains to capital as such. It is rather land, irreproducible and limited, whose nature is to appreciate and yield unearned increments. There are exceptions, which the champions of downtaxing gains may use in debate; but exceptions are no basis for framing generalities or public policy. As a broad rule we are on the mark to read "land gains" where the world writes "capital gains".

²⁶George Hatsopoulos, Paul Krugman and James Poterba, Overconsumption. Waltham, Mass.: American Business Conference and Thermo Electron Corporation, 1989.

²⁷Tom Redburn, loc. cit.

As Lester Thurow wrote, "If lower capital gains taxes were limited to plant and equipment investment in new, high-risk venture capital situations, one could understand the proposal ... But the lower ... rates will also apply to antiques, ... land, ... assets that have nothing to do with reindustrialization. For every dollar's worth of reindustrialization incentives offered, several dollars worth of incentives will be provided for nonproductive investments."²⁸ James Poterba, as we have seen, estimates a very small share of capital gains derive from "venture capital"²⁹

Corporate shares also yield "capital" gains. What makes these shares rise is the rise in value of corporate assets. The writer has shown elsewhere³⁰ that a large share of corporate assets consist of land (in the generic sense of natural resources).

The strongest reason for favoring capital gains is this. Another source of the rise in stock prices is the plowback of undistributed profits. Some of this actually does go to create real capital. (The rest goes to acquire old capital and land.) By this indirect route, a portion of any cut in capital gains taxes does actually foster real investment, as claimed. But the portion is too small, and the productivity of the investment often low, because this captive internalized undistributed profit comes to management free of any competitive market cost or test.

When the purpose of Congress is really to encourage new investment, fast write-off of new capital is the obvious tool. The tool was highly developed and applied during the 1960s, as noted above. It would also help to allow full deduction of capital losses, a provision conspicuously missing from current proposals, and indeed all reform proposals since 1932 or so.

The main effect of untaxing land gains, on the other hand, is simply to redistribute wealth and overprice land. When tax benefits go to land, the word "incentive" takes on a new and

²⁸Lester Thurow, "Getting Serious about Tax Reform". Atlantic M? date? Thurow's later endorsement of VAT does not seem very consistent with this passage.

²⁹James Poterba, loc cit.

³⁰Mason Gaffney, "Adequacy of Land as a Tax Base". In Daniel Holland (ed.) The Assessment of Land Value (1969). Madison: University of Wisconsin Press.

lesser meaning. Land, by definition, is not created by capital formation. Incentives to buy and hold land will raise the demand, not the supply. The incentives created are not the kind that produce anything or employ anyone. They simply raise asking price and exclude marginal buyers from the market.

Loopholes for land

In 1986 Congress closed loopholes which encouraged investment in new capital, but did not close them for land. It drastically lowered the top rates, a radical redistribution in favor of landowners, as we will see in detail. Here is an comprehensive systematic list of special loopholes open to those who own or buy and sell land.

Deferral of tax

The basic preference for land gains is tax deferral. Land gains are not recognized and taxed as income when they accrue, but only later upon sale for cash. To grasp the advantage of this deferral, consider this comparison of investors A and B. Both are subject to a tax rate of 50%.

"A" puts \$1 in a savings account paying 7.2% compounded annually. (That is the rate at which money doubles every 10 years.) He gets 3.6% after taxes, and plows it back, at which rate it takes twice as long, 20 years, for money to double. After 60 years his wealth has grown to \$8.

"B" puts his \$100 in land whose value rises at 7.2% per year. After 60 years its value has doubled 6 times, to \$64. He sells it and pays taxes of 50% on the gain of \$63. He thus clears \$32.50 after taxes. B's wealth has grown to over 4 times A's wealth, although both made the same rate of return, and both paid taxes at the same rate. The difference is timing.

This is why the standard Haig-Simons concept of income says increases of wealth should be taxed when they accrue. Tax economists, sadly, have finessed this issue by agreeing with Haig-Simons in theory, but closing the matter by saying it is not practical. Thus they please both the theorist in the classroom and the landowner in the event. There are exceptions like James Wetzler, who has shown some simple practical ways to adjust

taxation for this factor.³¹ Where there's a will there's a way; the will has been too weak.

Deducting costs of buying and holding

A. Covert depreciation of land

The tax code is clear that land is not depreciable, and should enjoy none of the benefits of fast write-off, or any write-off. This is obviously part of the heritage we owe to Judge James Maguire, Warren Worth Bailey and others present at the creation. Left to their own devices standard-brand economists like John Bates Clark and Frank Knight would doubtless have said, as they maintained vehemently in their writings, that land is no different from other capital³². They would have made it depreciable.

But the Internal Revenue Code still says land is different. When an investor buys land under an old grove, or old building, the Code says he must allocate his basis between the depreciable capital and the non-depreciable land. The requirement is reasonable, since buildings and fruit trees generally do lose value with time, while land does not.

So far so good. The problem is that property never sleeps, and Georgists have hibernated. As the watchdogs dozed IRS became extremely lax and "generous" in letting buyers overallocate basis to the depreciable building or grove of trees. Thus they contrive to depreciate for income tax not just the building or trees, but part of the land value. Often that part is major.

³¹James Wetzler, loc cit. See also M. Gaffney, "Tax-induced slow turnover of capital", ...

³²Clark and Knight both attacked George and his ideas vigorously, Clark in the flesh and Knight in the spirit. See J.B. Clark, "The Moral Basis of Property in Land", J. of Social Science, containing Transactions of the American Social Science Association, No. XXVII, October 1890, Part I, The Single Tax Debate, pp. 21-28; and "Capital and its Earnings", Publications of the American Economic Association, vol. 3, No. 2, pp. 1-61. Frank Knight, "The Fallacies in the Single Tax", The Freeman, 1953, pp. 809-11; and "Some Fallacies in the Interpretation of Social Cost", in G. Stigler and K. Boulding (eds.) Readings in Price Theory. Chicago: R.D. Irwin, 1952, orig. 1924.

70%. So were expensable carrying costs. Now, if these are recouped, it is to be at 28% (or a max of 33% in odd cases). With corporations, the rate drop was from 46% down to 34%.

Unrecognized gains are basically a debt owed by landowners to The Treasury. They are a debt bearing no interest, which is outlandish enough. They are payable at the debtor's convenience, which is also worth a lot. Now, with a fall of tax rates, a debt of \$70 incurred 30 years ago may be cleared by a payment of \$28 today. That sums a lot of it up nicely. It helps one understand why landowners were willing in 1986 to trade off the exclusion of 60% of gains in return for lower rates in the high brackets.

The unpaid debt of landowners to The Treasury has its counterpart in unpaid Treasury debt to bondholders. The Treasury pays interest on its debt, and the principal is due in full at maturity. Other taxpayers make up the difference and pay the interest, from taxes on income earned by useful productive activity.

G. Recoupment in devalued dollars: indexing and all that

✓ When a landowner takes gains at a higher price level than he took earlier deductions, part of recoupment is a phantom. Learned books and scholarly articles flow like water deploring taxes on "phantom income", but who is denouncing this other phantom? A balanced treatment should consider both. We begin with the conventional case alleging overtaxation of land gains.

During inflation land rises in dollar value with no necessary rise of real value. Purely inflationary rises are "phantom income". Many apparently temperate or moderate economists, like Alan Blinder, would index land gains so as to limit taxation to only the real gain⁵⁰. "Indexing" means multiplying the unrecovered basis of a gain by a price index which is adjusted to unity in the year or years when the historical cost was incurred.

Joseph Pechman, generally a champion of taxing capital gains, calls this adjustment "essential", and knows that

⁵⁰Business Week, 1 August 1988, p. 14.

✓ "economists agree"⁵¹. When the traditional leader of capital gains taxers⁵² concedes so much to the untaxers, indexing would seem to be the consensus position. The House Bill that failed to pass the Senate in November 1989 provided for indexing capital gains, to be phased in. Indexing is a fallback position for the untaxers of capital gains; there will surely be more attempts to achieve it (although President Bush now opposes it).

It is apparently the opinion of some enthusiasts that all land gains are phantom ("my gain is illusory because my replacement cost went up just as much"). If that were the end of it, indexing would eliminate the whole tax. Let us begin by denying that. Land prices in most regions and sectors have outpaced other prices over a long period. Demand has risen while natural supply remained fixed, and available supply dropped owing to local no-growth policies. The 1986 drop in tax rates was a windfall for owners of land yielding cash flow. Property tax rates fell sharply in tax-revolt states like California and Massachusetts. Land prices rose because after-tax returns rose. That is not general inflation, but real redistribution.

If a land seller's replacement cost has risen as much as his sale price, that alone makes him better off than the entry buyer who is unambiguously worse off. Are we to believe that higher prices make entry buyers worse off, but owners no better off? If that were so (which it isn't) it then follows overall welfare would rise if land prices fell to zero - think about it. But in fact what we have when real prices rise is a redistribution from workers as such to owners as such.

Consider also that cap rates fell after 1986 because Congress decelerated cost recovery on new investments, lowering the opportunity cost of capital. There has been a massive shift of tax burdens off land onto new capital, and labor. The corresponding shift of asset values is real.

Nevertheless there is no denying much of the nominal gain when land is sold is phantom income. The problem must be faced, and indexing faces it, in what seems a reasonable way. However,

⁵¹"Tax Reform: Theory and Practise", J. of Economic Perspectives I(1), Summer 1987, p. 23.

⁵²Pechman and Walter Heller were students together at Wisconsin, both taking degrees in public finance with Harold Groves, and working closely with him. Pechman's lifelong support of capital gains taxes is not inconsistent with this background.

this seemingly reasonable proposal is in fact unbalanced and discriminatory⁵³. All assets are taxed by inflation, not just "capital assets" (read land), which inflation taxes least of all, as we will show; and which receive so many other special favors.

First, those with monetary assets and fixed incomes are the obvious, immediate, primary victims of inflation. Indexing for capital gains does nothing for them. It is unbalanced to leave this immediate loss unredressed while making special provision for unearned increments to land value. It is also regressive because the share of wealth held in monetary form falls sharply with total wealth. It is also extremely dangerous for the future, because indexing gains does more than adjust for past inflation: it creates a powerful lobby to push for future inflation, setting up savers and creditors for a total wipeout.

Second, most real assets, not just "capital" assets, yield phantom income. In some inflationary years over half of reported business earnings come from inflation-induced marking up of inventories before sale.⁵⁴ Inventories yield their phantom income early and often, compared to land. The more deferred is the tax-recognition of phantom income, the less is the real burden.

LIFO accounting abates the inventory problem in part, which leads some to dismiss the point. LIFO poses other problems, however, and is not universally used, especially by small businesses.

Land yields phantom income only when the title is sold for a "capital gain". Depreciable assets, in sharpest contrast, yield phantom income in the ordinary course of use in production or for rental. Depreciation is limited to historical cost, which is less than the true allowance required for capital consumption and replacement.

⁵³Blinder and Pechman would also tax gains at death. This partly tempers the bias of their position, but adds a major new one in favor of deathless corporations, (and a minor one against short-lived individuals). They are silent on the many other favors cited herein.

⁵⁴The U.S. Department of Commerce reports this "inventory valuation adjustment" (IVA) regularly. Many economists have noted, some with missionary zeal, the malignant tendency to overstate profits and incur excess taxation. No modern tax economist can really be unaware of this.

Consider an office building leased with inflationary escalator clauses. The owner is selling the corpus of the building to the tenants, as it were, brick by brick, as they use it and it ages. Every rental payment includes some phantom income because the owner is selling the tax basis as he depreciates the building. Likewise the UPS driver delivers us with each parcel some skin off his truck, penny by pennysworth, until the truck is retired. The customers have bought the truck bit by bit. Each layer of value delivered includes its share of phantom income because the tax basis is less than the current dollar value.

Many reformers have championed indexing depreciation bases, and rightly so. But the present proposal to index capital gains does not do so. Building rentals are ordinary income; so are delivery charges. Only by selling the assets in toto would an owner get his basis indexed. But old trucks sell for nearly nothing, and have no basis left to index anyway. Old buildings sell for something mainly because they stand on good land. Old buildings retain an undepreciated basis to index mainly because land is not depreciable. What could be more obvious? Indexing gains is mainly for landowners as landowners, not as building owners.

Congress has never defined a "capital asset" clearly. A long line of court rulings has pieced in some of the missing details. Chirelstein's long chapter⁵⁵ goes over many of those, from which one can distill this essence: a "capital asset" is something one holds as an investment, with a primary view to appreciation rather than use or income or sale to regular customers.

Harold Groves compressed it nicely. "Capital gains ... arise not as a flow of income from the fountain, but from the sale of the fountain itself."⁵⁶ Nothing fits those descriptions like land gains. The primary benefits of indexing capital gains would go to landowners.

Third, the ordinary cash flow of land, or ground rent, includes no phantom income because there is no depreciation. It is not like the building being sold to tenants "brick by brick"; or the delivery truck, "layer by layer". The cash flow of land is pure income without impairment of the corpus or tax basis of the asset.

⁵⁵Chirelstein, op. cit., pp. 270-311.

⁵⁶Harold Groves, op cit., p. 166.

Depreciable capital yields a constant flow of phantom income as the corpus and basis are sold piecemeal by use or occupancy. That is a basic difference that should be elementary and universally acknowledged, but has been entirely overlooked in the extensive literature and public comment on phantom income. To be sure no one misses the point I flag it: the cash flow from land contains no phantom income.

Land in ordinary use is therefore immune to taxation of phantom income, it just doesn't yield any. Any depreciating capital is fully vulnerable, and gets overtaxed routinely. So does capital in inventories, constantly turning over in ordinary course of sale to customers. Land is the last, not the first asset needing further special protection through indexing. But it would be the main beneficiary.

Fourth, land is vulnerable only if title is sold, which is seldom. Sale of title is the only taxable event when land yields phantom income to tax. Indexing is designed specifically to protect land from that one potential liability to share the common burden of inflation. Under indexing, it is the undepreciated basis of old assets that is to be inflated by multiplying times the index. That undepreciated basis is mostly land, because land is not depreciable.

With true capital, as we stressed above, there is constant real turnover in the normal course of sale of services to customers. With land it is entirely different. Ownership only turns over in a "sale of the fountain itself".

Selling the flow from the fountain is continuous, routine and necessary to production and exchange. Selling the fountain itself, on the other hand, is an option, one exercised rarely or never. More or less 1%-3% of land parcels turn over annually, and these average below the mean in value. Even that overstates it. Many of these turnovers are tax rollovers, as we have seen, with no taxable event.

Slow turnover creates a fallacy of selective perception. If land finally sells and is taxed after 50 years of inflation the accumulated phantom gain is large and noticeable. The same original sum invested in inventories, turning early and often, would have paid tax on the same phantom income, and paid it much sooner. Because the land gain is all bunched at the end it is conspicuous, so the very advantage land enjoys is popularly perceived as a peculiar hardship. That fallacy should not,

however, fool professional economists; the irony should not escape them.

Fifth, equities gain when inflation lowers the real value of debt. The inflationary loss by creditors is not all a hidden "tax", as sometimes alleged. It does not all inure to The Treasury. Much of the loss is a gift to debtors, a redistribution of wealth. Most debt is mortgage debt so the creditors' loss is a gift to landowners. To the extent land is mortgaged the phantom rise of land price is offset by an equal fall in the real value of debt.

The latter is "realized" immediately (but not recognized and taxed) in a fall in the real value of interest and other debt service; the phantom rise of land value is only recognized if the land is sold. James Wetzler pointed out the discrepancy years ago, in a Pechman-edited Brookings volume. A fall in the real value of debt should be taxed as current income to the equity owner.⁵⁷

Enter indexing. It offers succor to the landowners who have already gained, and nothing to those who have lost -- nothing, that is, but higher taxes needed to make up the landowners' shortfall. It is hard to see the equity of such a measure.

Sixth is the matter of phantom recoupment, the point at which we entered this question. All recoupment of excess depreciation, illegal depreciation, and expensed carrying costs is paid in depreciated dollars. Remember a landowner is a debtor not just to his private creditors but to the fisc. He has accrued liabilities on the understanding he will repay The Treasury at time of sale. These liabilities include excess depreciation, illegal depreciation of land, and expensed carrying costs. Most tax economists, following the Haig-Simons definition of taxable income, would also see them as including deferred tax liability on accruals dated long before sale.

As to the depreciation (illegal and excess), this lowers the basis which is to be indexed, and I find no fault with indexing. But expensed carrying costs, and deferred tax liability, those two are something else. They do not come off the basis. Those are

⁵⁷James W. Wetzler, "Capital Gains and Losses". Chapter 4 in Joseph A. Pechman (ed.), Comprehensive Income Taxation. Washington: The Brookings Institution, 1977, pp. 115-62, at p. 129.

liabilities accrued in good dollars, to be repaid in bad. This is "phantom recoupment", the logical counterpart of phantom income.

Accrued tax liabilities are the Treasury's basis in the land. If the owner's basis is to be indexed, so should the Treasury's basis. This would make indexing neutral and fair. However, no spokesman for indexing has made the point, to my knowledge.

Such ideas may seem novel and alien. Why? Are they logically unsound, or simply new? If they are sound (as I believe), why are they not already old? If old, why now suppressed? Tax economists are not stupid. The current one-sided approach to indexing suggests the profession is in the grip of a class bias, or is just a Washington weathervane. Something is suspending the application of superior intelligence, suppressing logical balance and fair play. That is harsh, but not intended as scolding or ad hominem. Rather, I am puzzled and deeply disturbed. I would welcome some other reason. I simply do not know how else to explain it.

More is at stake than adjustments for past inflation. The greater fault of indexation is in the future: it would add overwhelming power to the pro-inflation lobby. Now, taxes on phantom income at least generate some political force against inflation. If we exempt land from its already small share of the inflation tax, we reinforce its timeless status as the world's refuge from inflation.

Land is more than a defensive refuge from inflation: it gains what others lose. With inflation landowners not only clear their private mortgage debt, not only clear their unrecouped prior carrying costs and illegal depreciations, but also the public debt for which, as Ricardian Equivalence Theorists tell us, they might otherwise be held partly liable. Adding it all up, indexing land gains would be an invitation to disaster along the lines of Germany, 1923.

House, Grounds and Playgrounds

One reason for downtaxing gains is to spare homeowners. Indexing would be especially targeted to relieve homeownership because the capital in homes is not depreciable and is never eroded below its historical basis. Indexing, recall, means multiplying the undepreciated basis by a number greater than one, before subtracting the basis from sales price.

Use for Partiality of Indexing
and T.O.C.

1

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"The partiality of indexing capital gains"

Mason Gaffney

A consensus has emerged among centrist economists that capital gains may be taxed at ordinary rates, but only provided the historical cost is indexed for inflation to exclude phantom gains. This apparently reasonable proposal is in fact partial and discriminatory. All assets are taxed by inflation, not just what the tax code labels "capital assets."

Monetary assets and fixed incomes are primary victims of inflation. Inventories yield phantom income early and often (LIFO accounting only partly abates this problem). Third, durable depreciable capital yields phantom income in ordinary use because depreciation is limited to historical cost.

In contrast, the ordinary cash flow of land (or imputable to land) contains no phantom income (there is no turnover or depreciation). Yet land would be the asset most sheltered by indexing capital gains. Land's basis (the value to be augmented by indexing) has not been depreciated away (except illegally); and it is the asset most likely to appreciate. Land only yields phantom gains at time of sale, if ever. Ownership turnover is very slow, so land is the asset whose gains are already most sheltered by step-up of basis at death.

Equities gain when inflation lowers the real value of debt; indexing would then additionally help the debtors, who have already gained from inflation, not the creditors who have already lost. An invisible creditor that loses is the Treasury itself. Most land carries deferred tax liabilities to be recouped at time of sale. Much of the recoupment is phantom when these invisible debts are paid in depreciated dollars. These liabilities include deductions taken by expensing carrying costs on appreciating land. Such deductions do not lower the basis of property.

Under the Haig-Simons rationale these invisible debts also include taxes dated from the time of accrual of gains. When taxes are accrued in good dollars, but paid in bad, there is phantom recoupment of tax liabilities, the obverse of phantom income. Accrued tax liabilities are the Treasury's basis in appreciating assets. To index the owner's basis but not the Treasury's basis is unbalanced. It would only add to an existing bias for deferred realization.

Capital in owner-occupied residences would gain from indexing more than depreciable capital because the basis remains fully intact. This would add to the existing tax bias, already very strong, for capital in this form.

Selective lightening of taxes on new investment can be

justified on incentive grounds; indexing gains would mainly favor old assets, and assets already sheltered.

Last, selective indexing of gains would create a new pro-inflation lobby with an interest adverse to the general welfare.

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Dear Mason:

On behalf of Jim Peters, Program Chair for the 83rd Annual NTA Conference to be held November 11-14 in San Francisco, I am writing to report that he would like to schedule you to present a paper on the topic outlined in your response to the Call for Papers.

I understand from him that your paper will deal with "The Partiality of Indexing of Capital Gains". His intent is to include this in a session to be titled Persistent Trouble Spots in Federal Income Taxation, with other papers by Bruce Busta (Income Tax Averaging), George Plesko (The Alternative Minimum Tax) and Leonard Burman (The Economics of Interest Allocation). The session is tentatively scheduled for Wednesday morning, November 14.

I am sorry we are so late in letting you know of our acceptance of your paper. Please let me know immediately if for any reason you cannot give this paper.

Thanks very much for your interesting sounding submission. I am looking forward to seeing you in San Francisco.

Sincerely,



Eighty-Third Annual Conference on Taxation

San Francisco, California — November 11-14, 1990

Sir Francis Drake Hotel

Locked-in Effect?

1. If a sale is required, to shift land from use a to b, a gains tax need not delay the sale. Buyer may even buy early, hold until ready.

Most common waste is inc. a from land bought too soon — e.g. Vict. AU. groves.

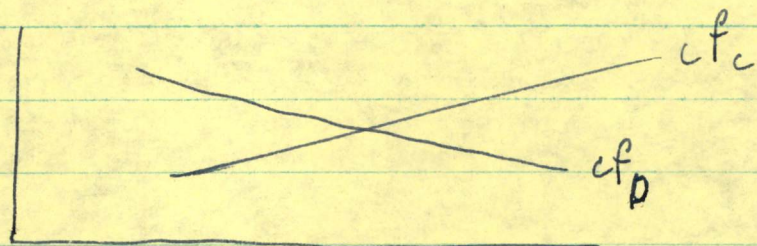
2. Develop model

$$L_0 = \text{Max} \left[\sum_i^n (a I^{-i}) - K_0 \right] + 2 \left[\sum_n^{2n} (\frac{1}{2} a I^{-i}) - K_n \right] \text{ ~~plus~~ } \frac{I^{-n}}{1 - I^{-n}}$$

$$+ \text{etc} - T$$

T is on $(L_n - L_0)$; rather, on ~~$L_n - \text{const.}$~~
 $L_n - \text{Base}$, where $B = \text{const.}$, maybe L_0 .

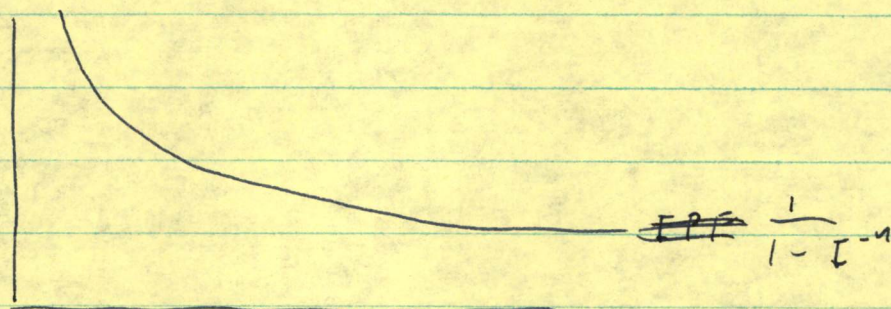
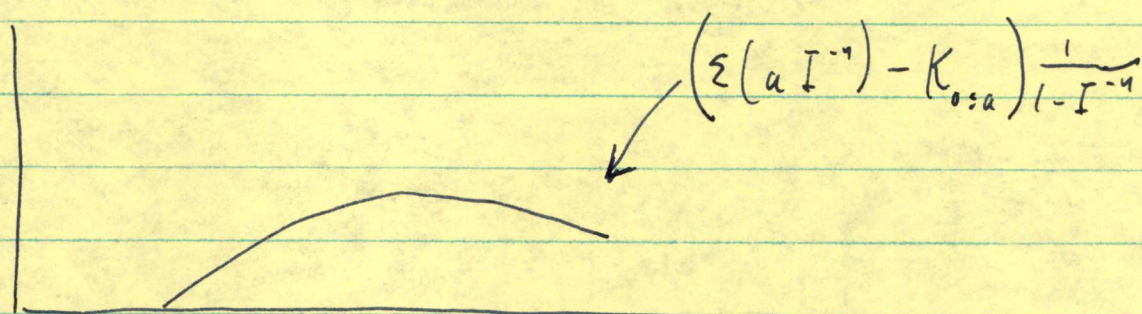
Will T affect replacement?



$$cf_c = \left[\sum (b I^{-i}) \frac{i}{1 - I^{-n}} - K_b \frac{i}{1 - I^{-n}} \right] + T$$

If gains tax is tied to act of replmt., then it defers replmt. So that becomes key gn.

3. Another basic model is PV



4. ~~And~~ To show tax effect, better to modify 3 to orange grove model.

$$L = a \frac{1 - I^{-n}}{i} + R_n I^{-n}$$

What detrs. n ?

Using regnl. approach, let R grow with n .
Condition for replacement is $R_i > a$ (ripening may alter this)

To the seller, the condition is $(R - T)i > a$
 Thus T locks seller in.

E.g., $a = \$10,000/\text{yr} = 10k$

$i = .10$

$\frac{\Delta R}{R} = .06$

$\tau = 70\%$
 $B = 0$

When R reaches $100k$, $Ri = 10k = a$

But $(R - T) = R(1 - .70) = .30 R$.

So to seller, old use looks better. He only feels 30% of the v.c. of the future.

Is true, $\frac{\Delta R(1 - \tau)}{R(1 - \tau)} = \frac{\Delta R}{R}$

But that is only part of the story. Besides, it's really

$\frac{\Delta R(1 - \tau)}{R - \tau(R - B)} = \frac{\Delta R(1 - \tau)}{R(1 - \tau) + \tau B} = \frac{\Delta R}{R + \frac{\tau}{1 - \tau} B}$

5. of course, a also pays tax.

So if a pays, + ΔR pays at same rate, that wears things out.

If a pays full rate, + R enjoys fast write-off, or tax exemption, net effect is to accelerate conversion.

6. Also consider genl. effects of inc. tax on i.

If o.c. of money falls:

a) Raises R , ^{speeding, hastening, quickening} ~~advancing~~ conversion.

("advance" means speed, ~~to~~ or make earlier, but as 2nd meaning means make later! Is $\therefore$ ambig.

("retard" is to make later. "Delay" is better

7. If tax gain, but not a, and not b, then what? Will defer conversion.

8. 7 assumes conversion requires new owner. There are several possibilities, each different.

a. a may rise smoothly, e.g. a parking lot. No new K needed. A sale wd. occur now & then, & have little effect on use.

Likewise, land w. a lease w. periodic escalator in ground rent, indep. of bldgs. R+ to receive this ground rent may change hands or not, has no effect on opus. or replnts. Is passive inc.

b. A normalized opus may stagger replnts. A sale wd. not cause any change

c. A highly land-int. opus — barley, corn grain, gas station — may replace K from

time to time, but K cost is low $\div$ cash flow.

d. One owner may convert to new use w/o tax;

conversely, owner may change w/o changing use. ~~the fact,~~

all that's locked in is ownership, not use.

e. Sometimes ownership change is of the essence, as w. o-occ. hsg., or family business.

9. ~~The~~ High rent, and ΔL under unrecovered K may pirate K recovery. To r.e. owner his asset is not depreciating, so he treats whole c.f. as inc.

10. Landowner gets ΔL . Consumes = amt.

But:

a. Can't consume ΔL itself. Consume other things - then disinvest.

b. After ΔL , higher share of c.f. is rent.

c. Owner may choose not to consume = ΔL . Then he is i) saving the inc. ii) Investing in buying ΔL . But this

inc. creates no jobs.

11. Japan has heavy tax on land gains.

R. J. Samuelson, n.d., LA Times.

Until '89, no sales tax!

12. Gains during marriage are not marital property.
Ben Line, 15 May 89.

13. Current defn of "efficiency" is, a market is efficient if no one can make further profit.

This focuses on ~~the~~ how well people buy & sell; ignores whether the basic fn. is inherently productive.

Reminds me of old argument that land is are ok bcs. owners can buy normal v.o.r.

14. "Constant land reform"
ongoing, continuing

15. J S Mill pp 504-05 on incidence of sales tax.

(On the Gen. Princ. of Taxn.)

16. Mill is often cited as an early champion of cons. taxes. (Bk V, ch. II, ¶ 4) The attribution is seriously out of context. Mill's complete train of thought ^{in ch. II} runs as follows.

1) If there is to be an inc. tax, savings shd. be exempted (he does not call it a

cons. tax).

- 2) The proposal is too easily avoidable, is impracticable.
- 3) Instead, tax perpetual incomes (i.e. from land) at a higher rate than terminable ones (i.e. salaries or life-annuities). The rationale is most relevant to our thesis here. There is no need to save if one has a perpetual income. Saving is done by those w. terminable incomes.
4. all land gains shd. be taxed 100%.
5. Existing land taxes are not really taxes but reserved rents to the sovereign. A general inc. tax shd. ~~tax them~~ be laid on top of them.
6. Paying off a nat. debt creates more K than is destroyed by any form of tax.

Ch. III, "of Direct Taxes", recaps most of the same pts, but adding ~~out~~ a stronger admonition (p. 502)

Also regards housing ~~tax~~ expenditure as the best tax base. proxy for either inc. or cons.

Ch. IV, "of Taxes on Commodities".
pp. 504 - 05. This is real double tax

17. Minsgrave p. 64 says '86 reform dealt w. inventory
guits, indexed them'. Check that.

Locked-in effect.

1. Allegation: Inc. tax is % of net gain, no effect on % gain.
2. Refutation: The tax reduces the % gain more when values are near the basis, (B).

Let: $B = \text{Basis}$

$R = \text{sales price}$

$R - B = \text{tax base}$

$R'_n = \Delta R, \text{ year } n = B(1+i)^n - i$

$t = \text{t. rate}$

n	R_n	$R_n - B$	R'	$R'_n / R_n = i$	$R'(1-t)$	$R_n - t(R_n - B)$	$q.$
0	100	0	10	.10	5	100	5.0
1	110	10	11	.10	5.5	105	5.23
2	121	21	12.1	.10	6.05	110.5	5.48
—							
10	259	159	25.9	.10	12.97	179.5	7.23
—							
25	1083	983	108.3	.10	54.17	591.5	9.16
—							
50	11,739	11,639	1,173.9	.10	586.95	5,949.5	9.91

More generally:

3. W/o taxes, current % growth = R'/R_n

$$\text{Ave. growth} = \left(\frac{R_n}{B}\right)^{\frac{1}{n}} - 1$$

4. After taxes:

$$\text{Current \% growth} = \frac{R'(1-t)}{R_n - t(R_n - B)}$$

$$\text{Ave. growth} = \left(\frac{R_n - t(R_n - B)}{B}\right)^{\frac{1}{n}} - 1$$

Gross tax

5. Now, what does this approach do to idea of gross tax's being neutral?

after gross tax

$$\text{Current \% growth} = \frac{R'(1-t)}{R_n(1-t)} = \frac{R'}{R_n}$$

But:

$$\text{Ave. growth} = \left(\frac{R_n(1-t)}{B}\right)^{\frac{1}{n}} - 1 \quad \text{becomes a}$$

powerfully increasing function of n , assuming $R_n \approx (1+i)^n$

"economists agree"⁵¹. When the traditional leader of capital gains taxers⁵² concedes so much to the untaxers, indexing would seem to be the consensus position. The House Bill* that failed to pass the Senate in November 1989 provided for indexing capital gains, to be phased in. Indexing is a fallback position for the untaxers of capital gains; there will surely be more attempts to achieve it (although President Bush now opposes it).

It is apparently the opinion of some enthusiasts that all land gains are phantom ("my gain is illusory because my replacement cost went up just as much"). If that were the end of it, indexing would eliminate the whole tax. Let us begin by denying that. Land prices in most regions and sectors have outpaced other prices over a long period. Demand has risen while natural supply remained fixed, and available supply dropped owing to local no-growth policies. The 1986 drop in tax rates was a windfall for owners of land yielding cash flow. Property tax rates fell sharply in tax-revolt states like California and Massachusetts. Land prices rose because after-tax returns rose. That is not general inflation, but real redistribution.

If a land seller's replacement cost has risen as much as his sale price, that alone makes him better off than the entry buyer who is unambiguously worse off. Are we to believe that higher prices make entry buyers worse off, but owners no better off? If that were so (which it isn't) it then follows overall welfare would rise if land prices fell to zero - think about it. But in fact what we have when real prices rise is a redistribution from workers as such to owners as such.

Consider also that cap rates fell after 1986 because Congress decelerated cost recovery on new investments, lowering the opportunity cost of capital. There has been a massive shift of tax burdens off land onto new capital, and labor. The corresponding shift of asset values is real.

Nevertheless there is no denying much of the nominal gain when land is sold is phantom income. The problem must be faced, and indexing faces it, in what seems a reasonable way. However,

⁵¹"Tax Reform: Theory and Practise", J. of Economic Perspectives I(1), Summer 1987, p. 23.

⁵²Pechman and Walter Heller were students together at Wisconsin, both taking degrees in public finance with Harold Groves, and working closely with him. Pechman's lifelong support of capital gains taxes is not inconsistent with this background.

Cap rates on land ↓. True part tax, maybe not A.T. And surely higher than in 1979 due to Reagan deficit deficits, Volcker's anti-inflation

These '91 provisions were worse!

IN L.B.

avg. land rises at same % infl, population, & productivity.

debtors

but personal debtors

this seemingly reasonable proposal is in fact unbalanced and discriminatory⁵³. All assets are taxed by inflation, not just "capital assets" (read land), which inflation taxes least of all, as we will show; and which receive so many other special favors.

First, those with monetary assets and fixed incomes are the obvious, immediate, primary victims of inflation. Indexing for capital gains does nothing for them. It is unbalanced to leave this immediate loss unredressed while making special provision for unearned increments to land value. It is also regressive because the share of wealth held in monetary form falls sharply with total wealth. It is also extremely dangerous for the future, because indexing gains does more than adjust for past inflation: it creates a powerful lobby to push for future inflation, setting up savers and creditors for a total wipeout.*

*but bondholders
try to
wealthier
have any
interest
recipient*

*This sounds
very
GOP!
See Blinder*

Second, most real assets, not just "capital" assets, yield phantom income. In some inflationary years over half of reported business earnings come from inflation-induced marking up of inventories before sale.⁵⁴ Inventories yield their phantom income early and often, compared to land. The more deferred is the tax-recognition of phantom income, the less is the real burden.

LIFO accounting abates the inventory problem in part, which leads some to dismiss the point. LIFO poses other problems, however, and is not universally used, especially by small businesses.

Land yields phantom income only when the title is sold for a "capital gain". Depreciable assets, in sharpest contrast, yield phantom income in the ordinary course of use in production or for rental. Depreciation is limited to historical cost, which is less than the true allowance required for capital consumption and replacement.

⁵³Blinder and Pechman would also tax gains at death. This partly tempers the bias of their position, but adds a major new one in favor of deathless corporations, (and a minor one against short-lived individuals). They are silent on the many other favors cited herein.

*But for
hypothetical
or deferred
consumers*

⁵⁴The U.S. Department of Commerce reports this "inventory valuation adjustment" (IVA) regularly. Many economists have noted, some with missionary zeal, the malignant tendency to overstate profits and incur excess taxation. No modern tax economist can really be unaware of this.

But you're assuming that there's some merit to the corporate tax

often

** and on the business's side, deduct only real interest, thereby making
land speculation more expensive.*

3. Phantom Income Taxation, and Land's Escape

It is true, there is taxation of phantom income caused by the money illusion during inflation. This is what some people mean by double taxation. Many apparently temperate or moderate economists, like Alan Blinder, advocate indexing capital gains so as only to tax the real gain.⁸ Joseph Pechman, generally a champion of taxing capital gains, calls this abatement "essential"⁹, and knows that "economists agree".

This seemingly reasonable posture is in fact highly discriminatory because it selects out "capital assets" for special relief, ignoring other assets taxed by inflation.¹⁰ "Capital assets" are simply an arbitrary group whose constituents have political influence to secure preferential treatment. Many "capital assets" are not capital at all, but forms of land. There are several reasons why land yields less taxable phantom income than other assets. Even wages and salaries suffer from inflation, as will be shown.

a. Most real assets, not just "capital" assets, yield phantom income. In some inflationary years over half of reported business earnings have come from inflation-induced marking up

⁵George Hatsopoulos, Paul Krugman and James Poterba, Overconsumption, Waltham, MA, American Business Conference and Thermo Electron Corporation, 1989, p.16.

⁶"Short of Euphoria", J of Economic Perspectives I (1) Summer 1987, p.69.

⁷"The 1986 Tax Reform and the Cost of Capital", J. of Ec. Perspectives I (1) Summer 1987, p. 83.

⁸Business Week, 1 August 1988, p.14.

⁹"Tax Reform: Theory and Practise", J. of Ec. Perspectives, I (1), Summer 1987, p.23.

¹⁰Blinder and Pechman would also tax gains at death. This partially tempers the bias of the position, but they are silent on the other preferences cited on p.1 of this MS.

inventories before sale¹¹. Inventories yield phantom income early and often, compared to land. The more deferred is the tax-recognition of phantom income the less is the real tax burden.

LIFO accounting abates this problem in part, which may lead some to think there is no problem. But very complex rules are involved, and LIFO is not ordinarily used by small business. LIFO gives no relief to additions to inventories: the cost of goods not sold is not deductible.

Depreciable assets also yield phantom income. Many reformers have championed indexing depreciation allowances, but the present proposal simply to index capital gains does not do so (except incidentally in special situations where ownership changes).

b. Monetary assets are constantly taxed by inflation. It is unbalanced to leave this loss unredressed while arranging indexing for land gains. It is regressive as well, because the share of wealth held in monetary form falls steeply with total wealth. How are we to explain the thinking of economists who give priority to indexing land gains while silently tolerating this most direct and obvious confiscation-by-inflation? In theory they are against it, but in practise give priority to relief for land gains.

c. The ordinary cash flow of land, or ground rent, yields no phantom income because there is no depreciation. Phantom income arises when there is a sale of the corpus of an investment at a nominally higher price. Phantom income arises when durable capital yields cash flow and depreciates; depreciation represents sale of the corpus, little by little. Ground rent by contrast is pure income without impairment of substance, i.e. without any sale of the corpus.

That is a basic point that should be elementary, and accounted for in every treatment of this subject. But it has been entirely overlooked, to my knowledge, in the extensive literature and public comment on phantom income. That is not because it is difficult or obscure. To address the point is to see it: the profession simply declines to face it, in self-imposed isolation

¹¹The U.S. Department of Commerce reports this "inventory valuation adjustment", or IVA, regularly, and many economists have noted, some with missionary zeal, the malignant tendency to overstate real profits and incur excessive taxation. No modern economist can really be unaware of this phenomenon.

from a large chunk of reality.

To forfend anyone's missing the point I flag it: the cash flow from land contains no phantom income.

d. Increments to land value do generate phantom income, if and when ownership turns over. Ownership turnover creates the taxable event. With most assets, especially inventories, there is rapid real turnover which forces ownership turnover and a taxable event. With land there is no real turnover at all, hence only little ownership turnover. Ownership turnover is an option, one normally exercised only glacially: more or less 1%-2% of land parcels turn over annually, and these average below the mean value. Even that overstates it: most turnover of owner-occupied residences is tax-deferred, and if the deferral lasts until death the gain is tax-exempt forever.

Slow turnover creates a fallacy of selective perception. When land finally changes hands after, say, 50 years of inflation, the accumulated gain is large and is noticed. Yet the same assets invested in inventories, turning early and often, would have paid tax on the same phantom income over the same period and paid it much sooner. Thus the great irony: the very advantage land enjoys is popularly perceived as a special hardship. This fallacy should not, however, fool professional economists.

e. Equities gain by declines in the real value of debt. To the extent that land is mortgaged, the phantom rise in land price is offset by an equal fall in the real value of debt. But the latter is realized immediately in a fall in the real value of interest and other debt service; the phantom rise in equity value is only recognized as taxable when and if land is sold (and often not until some time after that).

f. Some capital is expensed, or depreciated fast. Expensing eliminates the phantom income bias, and fast write-off lowers it. The deceleration of recovery in the 1986 Act added a great deal of phantom income bias against fixed capital. A reformer might well give priority to redressing that, but the present proposal to index capital gains hardly helps, except incidentally.

As noted above, some land is depreciated in practise (extra-legally but massively), resulting in effective tax-exemption in perpetuity, beginning from when the deduction is taken. There is no tax either on phantom or real income.

g. Bracket creep, reduced real value of personal exemptions, and wage withholding have worked together since 1941 to increase the share of income taxes taken from wages and salaries. Before 1941 most workers paid no income tax at all, an outcome voters clearly desired and anticipated when they passed the 16th Amendment¹².

FICA rates have leaped up to over 14%. Income taxes are based on pre-withholding income, which includes 7% or more consigned to FICA, a kind of phantom income (in a different sense, it is true) on which labor is taxed. The growing pressure to disallow deduction of state and local taxes will only worsen this bias. States already disallow deduction of Federal taxes. We are taxed not on disposable but on an increasingly phantomized, inaccessible gross income.

Corporations have not suffered from bracket creep because the corporate rate is basically flat (except for token graduation for the first few dollars of corporate income). On the contrary, the corporate rate has dropped from 46% to 34%.

While bracket creep has pushed the middle class into higher tax brackets it has spared the upper class because the top brackets have dropped from 70% to 28%, a giant step towards a flat rate tax. This has also abated any previous tendency of intermittent capital gains to push recipients temporarily into high brackets in the year of the gain's recognition (a problem already assuaged by averaging rules).

h. A goodly share of land gains are much less inflation-induced than usually perceived ("my gain is illusory because my replacement cost has gone up just as much"). The 1986 drop of tax rates was a giant real windfall for owners of old capital and land. There has also been a sharp drop of property tax rates in many states like California and Massachusetts. Land prices rose because after-tax returns rose. That is not general inflation but redistribution.

At the same time cap rates fell after 1986 because Congress decelerated cost recovery on new investments, lowering the opportunity cost of capital. That is not general inflation either. Rather there has been a massive shift of tax burdens from

¹²Elliot Brownlee, "..."

land and old capital to new capital and labor. The corresponding readjustment of asset values is real.

The upshot is, land gains accrue to an asset whose basic income is already exempt from the extra inflationary tax that erodes most other wealth, and confiscates wages. They accrue to an asset whose share of the tax burden has fallen steeply (if intermittently) over a century, and especially since 1986. Land gains are the last, not the first asset whose phantom income from ownership turnover should concern us. The overall impact of past and future inflation is to discriminate for land gains, not against them. Consideration of phantom income actually argues for heavier taxation of land gains.

CLASS OUTLINE AND LIST OF ASSIGNED READINGS

FOR

TAXATION AND BUSINESS MANAGEMENT: 15.418

Professor Daniel M. Holland

Fall, 1974

1. There is no textbook for the course. All additional required readings have been assembled in reprints and will be made available to you as a package at a charge of \$4.
2. There will be no final examination.
3. An important feature of the course is the term paper required of all students. I shall expect that all topics will be chosen after discussion with me by October 22, and all papers submitted no later than 9:00 A.M., December 16.

15,418 - TAXATION AND BUSINESS MANAGEMENT

Professor Daniel M. Holland

Fall, 1974

I am sorry to miss the first day of class, but will be here to meet with you on Monday, September 16 to describe the course and what it covers.

We are distributing now reading assignments for the first several meetings. You may obtain the readings from the Graphic Arts Department (E52-032).

<u>Class Number</u>	<u>Date</u>	<u>Topic and Assigned Reading</u>
1	Sept. 16	<u>The Government Sector</u> <ol style="list-style-type: none">1. Selections from Milton Friedman, <u>Capitalism and Freedom</u>, Chapter II2. Francis M. Bator, "Government and the Sovereign Consumer"
2	Sept. 18	<u>Principles of Taxation</u> <ol style="list-style-type: none">1. Selections from <u>International Encyclopedia of Social Sciences</u>, Volume 15, pp. 521-5452. Selections from Carl Shoup, <u>Public Finance</u>, pp. 21-31
3	Sept. 23	<u>Fiscal Facts and Folklore</u> <ol style="list-style-type: none">1. Joseph A. Pechman and Benjamin Okner, "Who Bears the Tax Burden?"2. Richard Musgrave, "Expenditure Structure"

Fall, 1974

<u>Date</u>	<u>The Income Tax Base and Structure</u>
October 2	Tables from John A. Gorman, "The Relationship Between Personal Income and Taxable Income," <u>Survey of Current Business</u> , May, 1970
October 7	<u>How Should Stockholders Be Taxed?</u> Selections from Daniel M. Holland, <u>Dividends Under the Income Tax</u> , ("Double Taxation, Differential Taxation, and Tax Relief")
October 9	<u>Some Specific Aspects of Corporate Income Taxation</u> 1. "Dividend Policy and the Tax on Accumulated Earnings" (Chapter 10 in Robert Holzman, <u>Tax Basis for Managerial Decisions</u>) 2. Richard Goode, <u>Rates of Return, Income Shares and Corporate Tax Incidence</u> 3. Citizens Utilities Company
October 16	<u>Capital Gains</u> 1. Roger Brinner and Alicia Munnell, "Taxation of Capital Gains: Inflation and Other Problems" 2. Daniel M. Holland, "Note on Capital Gains"
October 21	<u>Adjusting the Income Tax for Inflation</u> E. Cary Brown, "Allowance of Replacement Cost Depreciation for Tax Purposes: Equity and Economic Effects." (Chapter IV in <u>Depreciation Adjustments for Price Changes</u>)
November 11	<u>Effect of Taxation on Compensation: a. Trends in Top Executive Compensation</u> 1. Wilbur G. Lewellen, "An Intersectoral Analysis of Senior Executive Rewards" 2. Wilbur G. Lewellen, "Managerial Pay and the Tax Changes of the 1960's" 3. Assorted Proxy Statements

Date

October 23

Tax Incentives - General Discussion

Stanley S. Surrey, "Tax Subsidies as a Device for Implementing Government Policy: A Comparison with Direct Expenditures"

October 30

Tax Incentives - Some Specific Examples

1. Daniel M. Holland, "Note on Exploring for Mineral Properties"
2. Daniel M. Holland, "An Evaluation of Tax Incentives for On-the-Job Training of the Disadvantaged"

November 4

Tax Shelters

Paul R. McDaniel, "Tax Shelters and Tax Policy," National Tax Journal, September, 1973

November 6

Effect of Taxation on Compensation: Stock Option

1. Selections from Daniel M. Holland and Wilbur G. Lewellen, "Probing the Record of Stock Options"
2. Selections from Myron S. Scholes and Daniel M. Holland, "Taxing Options at Time of Grant"

November 11

Effect of Taxation on Compensation: a. Trends in Top Executive Compensation

1. Wilbur G. Lewellen, "An Intersectoral Analysis of Senior Executive Rewards"
2. Wilbur G. Lewellen, "Managerial Pay and the Tax Changes of the 1960's"
3. Assorted Proxy Statements

Date

November 13 & 18

November 20 & 25

November 27 &
December 2

December 4 and 9

December 11

Effect of Taxation on Compensation: b. Cost Benefit Analysis

1. George Hettenhouse, "Cost/Benefit Analysis of Executive Compensation," Harvard Business Review July-August, 1970
2. John L. Leshner, Jr., "Executive Compensation--Theory and Practice"

Effect of Taxation on Compensation: Private Pension Plans

Daniel M. Holland, "Pension Fund Growth and Economic Implications"

a. Effect of Taxation on Effort: Theory

1. Selections from Duncan Black, The Incidence of Income Taxes, Chapter II, "The Effect of the Income Tax on the Supply of Labour per Individual," pp. 157-163
2. Crawford W. Greenawalt, "The Effect of High Tax Rates on Executive Incentive"

b. Effect of Taxation on Effort: Some Evidence

1. George Break, "Income Tax Rates and the Incentive to Work and Invest"
2. Daniel M. Holland, "The Effect of Taxation on Effort: Some Results for Business Executives," all but pp. 74-93

Value Added Taxation

1. Dan T. Smith, "The Value Added Tax: The Case For"
2. Stanley S. Surrey, "The Value Added Tax: The Case Against"

Edwin S. Cohen, "Foreign Experience with a Value Added Tax"

Taxation of International Business:

Readings to be distributed later

Review

Phantom profit

Sinking fund & infln.

To replace a discrete item when scrapped, need set aside much less than its value.

b = sinking fund instalment

$$b \frac{e^{mi} - 1}{i} = C$$

$$b = C \frac{i}{e^{mi} - 1} = C \frac{c.r.f.}{e^{mi} - 1} \rightarrow 0 \text{ as } m \text{ grows.}$$

The argument is made that deprec. shd. cover replacement, at higher prices. Sounds dubious. Replacement begins immediately, i.e. mntce. of capl. does.

As to the capl. recovered later in life, it has enjoyed many years of untaxed apprec., which offsets a good deal of the phantom profit effect.

Solution: Write up value of unrecovered K each year — but charge tax on the write-up. Then let it be deprec. Well, this achieves intertemp. neutrality, but doesn't offset phantom profit effect.

3) There are the allocations about 'phantom profits' made by Joel Barlow and so on. It seems to me that the idea ~~that~~ profit is fictitious because of the rise of price level of replacement capital has been seriously overstated. Investment and liquidation is a self-contained cycle. The fact that a good purchased for \$100 can be replaced only at \$105 does not wipe out a \$5 profit because after all the new capital purchased for \$105 can be sold for \$110. The fallacy in Joel Barlow's thinking is of a peace with the idea that new investment in, let us say, drilling for oil is a current expense to be charged against income from existing wells.

Putting it another way, a 5% rise in the price level does not reduce profits by 100% or 50% as Joel Barlow would have it. Yet no-one so far as I am aware has written the definitive article spiking this fallacy which has a big head of steam behind it. All the right-wing tax avoiders are jumping into the act, you may be sure.

In terms of relevance to the conference, I think it would be interesting to demonstrate that inflation or anticipated inflation tends to increase the profitability of short-term investments more than long-term investments. This could account for some of the stimulating effects of inflation normally attributed to money illusion and so on.

Well there are obviously many other possibilities, and I leave it to you to pick your favorite. My only request is that you avoid getting into a narrowly technical issue of only limited interest and relevance. We are after all going to be discussing a reconstruction of macroeconomics.

Incidentally, Jerre Brannon has accepted along with Hans Brems, David Martin, Hyman Minsky, Rober Bezdek and possible Jack Hirshleifer.

And congratulations to you on Gillian Traer, ^{AUNT} and Traer must be very pleased as well.

I hear that George Tolley is now director of OTA. Is this so? I never thought of him as a public finance man.

If you have suggestions for people who might be worthwhile ~~my~~ considering for this conference please send them along. There is always some attrition as you go along and I want to stock pile a few spares.

Cordailly,

Mason Gaffney
Acting Director

MG/cn

Sunley

Pensioners are major victims
of infln. Cos. borrow from
their own pension funds, like
UStsy from Soc Sec fund.



Department of Finance

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Telephone: (313) 927-1160

November 2, 1989

Professor Mason Gaffney
3040 Tyler Street
Riverside, CA 92503

Dear Mason,

Your letter of Oct. 24 arrived just after Homer Fox and I presented his Detroit study and my AJES submission to our faculty colloquium!

My assessment ratios are from Musgrave and Musgrave, 4th Ed (1984), p. 467; in turn, they are from Census of Governments (1977). I haven't checked latest figures. I agree that coverage is poor (though coverage of farm land may be good, because of USDA's interest). Incidentally, I have a disk with consistent USDA data through 1981 or so; interyear comparisons were always difficult, due in part to rapid turnover of the economist in charge.

Re: your WEA paper: you argue (correctly, in my view) for a continuation of capital gains taxes on land. If this is to be an academic paper, I'd cut the tour of the nuthouse (Ture, Roberts, et al) and the obiter dicta on accounting and utilities. Your real point is on page 4: gain equals sales price minus basis.

Your point about investment in education is interesting, though limited. A large part of the student's investment in education is the time value involved. As the value of that time isn't taxed, no subsequent "depreciation" is warranted. Similarly, the (large) "investment" in nurturing of preschoolers (especially on the part of educated parents and all Japanese) is expenditure of pretax income, hence no discrimination. Fascinating as this is, it may belong in a separate paper.

More relevant is your argument about nondeductible commuting costs (top of p. 5).

P. 6, fn. 10: I'd happily settle for carryover of basis (per the 1976 Act, then killed by moratorium). No benefit to corporations: in an efficient market the rising value of the corporation's land (cf. Japanese firms) is reflected in its stock's price. Yes, deferral is of considerable value, esp. without indexation (enclosed JPM article, table 3). But carryover was killed by concern (Farm Bureau, NFIB) about continuity of family ownership.

✓ P. 7, top: the 1986 Act made LIFO usable by small firms.

P. 9: Most states already disallow deduction of Federal taxes. Exceptions: AL, AZ, KY, LA, ME, MO, DE, MT, OR. OK and KS allow optional deduction, but then impose higher state rates. Source: Tax Foundation.

P. 9: I'd downplay bracket creep, given our three-rate personal structure, and some indexation therein.

P. 10: the flows... are potentially taxable: exemption of imputed rent on owner-occupied property may be the largest single flaw in the American tax system.

Now to your model (p. 11-12): Why not motivate this with two examples: 1. Farm land on the urban fringe, where future value will arise largely from social expenditure on infrastructure.

2. Real growth of average land prices over time is largely population and productivity (as you state at the middle of p. 12).

The model itself is much like the "supernormal growth" models that were popular in business finance some years ago. The difference here is that above-normal growth results from external causes, so should be taxed.

I enclose some recent journalism. I'm starting a note on the welfare gain from indexation, and a broadbrush polemic on tax policy and saving. I'll send copies when I have readable drafts. In turn, send me the next version of the WEA paper; I wish I could have done a better job on the present one.

Sincerely,

Alan K. Severn
Associate Professor and
Research Coordinator

✓ P.S. Note Musgrave and Musgrave on real estate gains (p. 668 our fourth ed): "However, this [exemption]... extends to investments which render little addition to growth (e.g., real estate speculation).... the preferential treatment of capital gains is thus of questionable merit as an investment incentive...."

Note new mailing address -->

Mason Gaffney
P.O. Box 7998
Riverside CA 92513-7998

17 March 90

Frank Genovese
Babson College
Babson Park MA 02157

Dear Frank:

Enclosed please find "The partiality of indexing capital gains" edited in response to your pencilled suggestions. Let me have further comments if needed; after a few replications we'll have it right.

On the questions in your letter:

a. My ms does single out owner-occupied residences for special comment. It refers to capital on such land, rather than the land, because the germane point here is non-depreciability. All land is non-depreciable, but only residential-recreational capital is non-depreciable.

b. The lifetime exclusion of \$125,000 of gain on sale of residence is worth mentioning if there is space. I put it in brackets, to strike out if the thing is too long. One could also mention the non-taxation of imputed income.

c. I deleted references to inventory turnover. "Ownership turnover" of land is still there, and I hope explains itself.

d. Many land improvement costs that should be capitalized are in fact expensed. Ditching and draining are "water conservation" items and qualify for expensing. Very few land improvements (except buildings) remain undepreciated or unexpensed by time of sale, and I suggest omitting the matter from so short a statement.

Concerning the paper at St. Johns', it is not copyrighted and is available for AJES use. Let me know how you would like it abbreviated, if need be, or otherwise changed. I am delighted you like it. It seems to have good chemistry, there has been a lot of fan mail. Sometimes you get lucky and the pieces just fall together right. I suspect it would be a good piece to run.

One "fan," Peter Colton of the ORER at U of Illinois, has already run it, edited down a bit. I enclose his version in case that will help with your editorial suggestions. He got the original title, which you too may prefer. The HG School of Los Angeles has also reproduced it, using both the original title and all the original wording, including mistakes in punctuation.

I have no copies of the St. Johns' version, which is wretchedly reproduced in any event. Am sending copies of the ORER version to Warsh and Francis at your suggestion.

Re Francis, one Jon Rowe, an old friend of mine, works for the Monitor and has been filling a file on Georgism for a feature article he has been promising for two years now. If you can get Francis to encourage him ...

Sincerely,

Précis, article on Tax Revolt.

"Land Reform & the Taxpayer Revolt."

New conventional wisdom relates Prop. 13
to shift of Prop. tax burden to
residential. Caused by better assmt.

Morals: a) "bring back the crooked ass." b) Forget about
land tax as mode of land reform.

Hypothesis here is relate ~~tax~~ shift of burden
not to better assmt., but to worse. Effect of
infln., cfd. to conventional ways of assg
income prop vs. o-occ. prop.

- ~~Much inc. prop.~~ Standard way of assg
inc. prop. is cap. current income, [†] This omits:
- a) Higher future inc. in present use
 - b) " " " " higher use, future or present
 - Plottage Δ
 - e.g. of ind. land and lower than adjacent resid.
 - c) Contingency value, vert. intra.
 - d) Presumptive value
 - e.g. of covenant not to compete
 - e.g. of allowable lot cals.
 - e) Ancillary values
 - Grazing rts.
 - Water rts.
 - Rts. to pollute air & water

[†] Kuttner & Keiston mention this, p. 3, but don't develop it.

f) Underuse of land in current use.
- Neglected citrus groves

g) Value of tax shelter
- Citrus groves, dairy herds, etc.

h) Value of unripe resources
- App. coal
- Timber in large holdings

Some other r.e. is valued on historical cost.

Lag in assets, also, in infl. era, opens wide
gaps. hurting v. occ. residue of highest turnover.

acc. deprec. for inc. tax, accepted by ass.

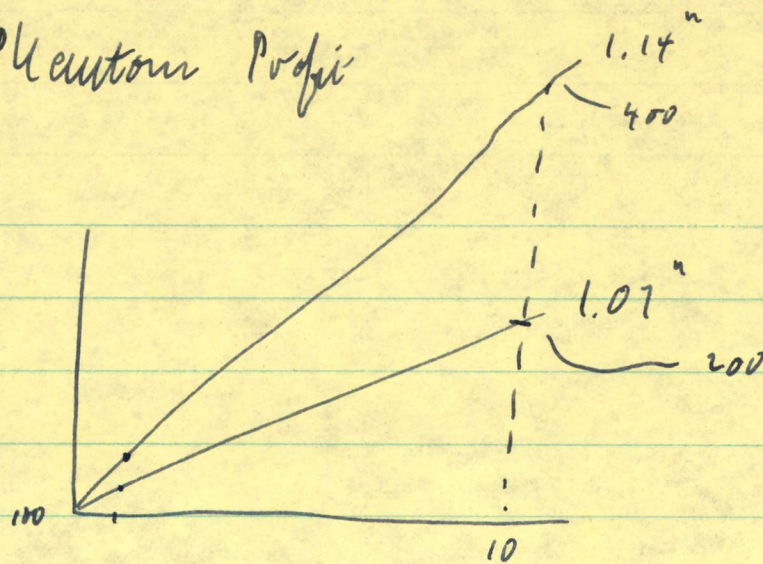
Much of this results from tech. difficulty
of assig ~~ing~~ indy. LVT better.

Much results from exempting mach. & equipment,
etc.

Much results from local desire to attract &
hold indy.

all solved by LVT -- land reform
via tax.

Phantom Profit



$t = 50\%$

✓

n	R	$R-I$	T	$T/R-I$	$R-T$	r
1	114	14	7	.5	107	.07
10	400	300	150	1/6 .5	250	>.07
20 30	1600	1500	750		850	>.07
30 40	6400	6300	31,500		32,500	>.07

