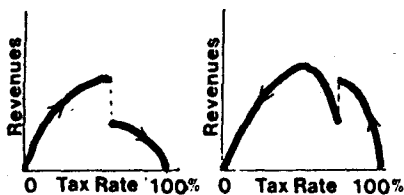


Mr. Laffer's Curve: What Is the True Shape?

Your Dec. 1 article about Arthur Laffer and his curve was both interesting and disconcerting. The current national consensus on the need for tax cuts is long overdue, and there is little doubt that large increases in productivity and prosperity will surely accompany tax cuts and in the doing inspire increased tax revenues. But that has little to do with the merits of Laffer's curve. The curve is much like the man who falls from a tenth story window, and observes as he passes the first floor that not much has changed. It is moments later that a change will occur, and it will be a sudden, immense, discontinuous change. So, too, with tax rates and tax revenues. Taxpayers do not gradually decrease their business efforts as taxes increase. Rather, they continue as before, until suddenly a point is reached at which they comprehend that the game is no longer worth the candle. The Laffer curve will look like this:



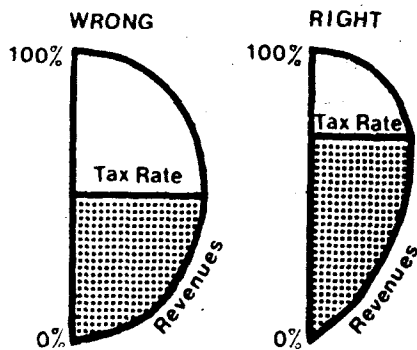
There remains now the matter of returning to a previous point on the curve, once the gap has been passed. This cannot be accomplished simply by "climbing up" again, any more than the falling man can be returned to his previous state simply by carrying his body back up to the tenth floor. There will be gaps on the Laffer return-curve too, sudden discontinuities in tax revenues even as the tax rate is decreased. This is a phenomenon familiar to all physical scientists and of apparent concern to many economist critics of Laffer. We should take such objections most seriously before basing social experiments partly on silly little curves.

ALFRED ADLER

Professor of Mathematics
State University of New York
Stony Brook, N.Y.

* * *

Your Dec. 1 back-page story on Art Laffer and his curve reminded me to pass on an important correction to the shape of the thing. The curve is usually drawn as a simple bell-shape turned on its side, but it actually looks more like a teacup handle. That is:



As can be seen, revenues are still zero at either a 0% or 100% tax rate. However, a glance at the properly-shaped curve shows that tax rates even higher than those we now have will raise more, not less, revenue. This proves that Mr. Laffer's conclusions are wrong.

The proper shape of the curve was revealed to me by a bartender in Mendocino, California, who drew it on the back of a cocktail napkin. Thus, I have as much evidence for the proper curve as Mr. Laffer does for his curve. I'm sure no one will object to using my curve as the basis for federal tax and fiscal policy, and I offer it free of charge to any U.S. Senator looking for a simple answer to our complex problems.

JOHN MICHAEL MURPHY

Mill Valley, Calif.

* * *

Alfred Malabre's perceptive portrayal on the back page of your issue of Dec. 1 of Arthur Laffer's Tax Yield Curve and the theory he derives therefrom unfortunately has the same defect as the theory and its admirers and most of its critics. All these generalize, as though all taxes were alike. But that is just not so.

Laffer's curve tells us that at rates of zero and 100% the yield of taxes will be zero, the maximum yield falling somewhere between these extremes.

This may hold in the case of the income tax, although the zero point on the top side would probably be well below 100%. It is certainly not the case with excises, where, for instance, in India in the 1870s the tax on salt almost reached 1,200%.

Nor, at the other extreme, does it hold for the property tax, where a low annual rate on the building will, over time, capture a sum whose discounted present value will be a high percentage of that present value, and where the same low rate, applied to rental property, may amount to an alarming percentage of its before-tax income.

But the most striking failure of all these theorists is their failure to analyze and describe the workings of the other part of the property tax, the part that falls on land values.

All taxes on labor and its products are harmful because they lessen incentive and, by adding to the costs of production, they lessen supply and raise prices. Likewise they are unjust as they infringe on the rightful earnings of labor and capital.

Conversely, taxes on land values are just, for land values are but the capitalization of the annual benefits from the community, net of the tax, enhanced by the expectation of future gains from the artificial scarcity created by speculation on the pos-

sibility of that rise in price of a factor, the supply of which cannot be increased by production. Moreover, the tax on land values is the only tax that encourages, that stimulates, that compels production and does that in direct proportion to the magnitude of its rate. As one of the two economists selected for special honor by the American Economic Association at its annual meeting, held in Chicago this past August, has said: "We will never have an economically efficient economy until we have recovered in taxation at least 85% of the rent of land." (In a 5% money market, this would be achieved by a tax rate of 28½%; in a 10% market, by a 56% rate on the actual market value of the land.)

It is understandable that political animals like Gov. Brown and Sen. Long should seek counsel of Laffer. The mystery is why competent economists waste their time in such distractions, instead of turning their attention to the exciting and constructive potentials inherent in the study of the economics of land value taxation, especially in these times of fiscal and monetary crises.

Somehow I am reminded of the old shell game, practiced at country fairs, where the pea was under one of three shells and the facile operator moved the shells about with such dexterity that the wagering onlooker rarely could tell which shell finally held the pea. Alas! In the ongoing controversy of fiscal vs. monetary policy, there is no third shell for land value taxation. It is not even in the game!

WELD S. CARTER

Executive Secretary
Committee on Taxation,
Resources and Economic
Development

Antioch, Ill.

THE WALL STREET JOURNAL.

Published since 1889 by

DOW JONES & COMPANY, INC.

Editorial and Corporate Headquarters:
22 Cortlandt Street, New York, N.Y. 10007.
Telephone (212) 285-5000

WARREN H. PHILLIPS
Chairman and President

RAY SHAW
Executive Vice President

DONALD A. MACDONALD
Senior Vice President

GEORGE W. FLYNN
Vice President/Development
And Affiliated Companies

EDWARD R. CONY
Vice President/News

WILLIAM L. DUNN
Vice President/General Manager

FREDERICK TAYLOR
Executive Editor

W. GILBERT FAULK JR.
Vice President/Legal

LAURENCE G. O'DONNELL
Managing Editor

FREDERICK G. HARRIS
Vice President/Finance

JOHN J. MCCARTHY
Vice President/Administration
STERLING F. SODERLIND
Vice President/Planning

ROBERT L. BARTLEY
Editorial Page Editor

WILLIAM F. KERBY, Chairman, Executive Committee

Midwest News and Sales Office:
200 West Monroe Street, Chicago, Illinois 60606
Telephone (312) 848-7600

SUBSCRIPTION AND ADDRESS CHANGES should be sent to The Wall Street Journal, 200 Burnett Road, Chicopee, Mass. 01021, giving old and new address. For subscription rates see Page 2.