

The Tax Cuts—Their Ultimate Effect

by PETER PATSAKOS

ON January 31st President Kennedy presented his tax bill to Congress, designed to eliminate "the unrealistically heavy drag of federal income taxes." Businessmen and Congressmen agree in general, but not on the specific measures.

What effect would the tax proposals have on the economy if adopted? A tax cut will leave more potential purchasing power in the hands of the taxpayers to be used for spending, investing and/or saving. This should result in a greater demand for goods and services and should increase the supply of wealth to satisfy this demand. But since the government is spending more than it is receiving, the net purchasing power is lessened because the value of the dollar is decreasing.

The tax cut would amount to about \$8.7 billion after certain loopholes had been closed. If this resulted in increased incentive for business, and higher real wages for labor, it might have a beneficial short term effect. However, any increase in the economy's growth would be reflected in higher land values and land rentals, which would tend to negate any benefits to wage and interest earners. The ultimate effect could be to spur land speculation at an even faster pace than the possible increase in production. This would result in more unemployment, decreased production and a "recession."

Part of the President's tax bill concerns tax reform. A suggested reform in the right direction would have been a large deduction in the oil depletion allowance which is presently 27.5 per cent. This means that petroleum producers can deduct this percentage of the value of the crude oil and natural gas they produce from their pre-tax gross. Instead the President recom-

mended a mere 6 per cent reduction in the allowance, along with changes in the complicated methods by which natural resource depletion is computed, which could provide \$280 million in tax revenue. This is a mild measure but is regarded by Congressmen as a "hot potato," indicating that powerful oil interests are applying pressure. The 27.5 per cent is basically land rental, but is privately collected instead of being used as government revenue.

The profits on sales of stock and other assets (this includes land which is erroneously considered capital) are now taxed as ordinary income if sold within six months after purchase—this period would be extended to one year. But the new proposal would also decrease the top rate on long term capital gains, making it 19.5 instead of the present 25 per cent. Hence the profit on land sales, if held for more than a year, would be even greater than now.

Persons inheriting stock or property which had increased in value since it was bought, would, however, have to pay a capital gains tax on the increased worth. At present such gains go untaxed, so this would result in a partial collection of increased land values for public revenue. By the error of considering as capital, both land and improvements, the government is penalizing the production of wealth and making an accurate assessment of land values more difficult.

In fact the net effect of all the reform proposals is not a major closing of the many and devious loopholes, but only a stiffening of collection procedures which applies more to earned than unearned income. This is almost unavoidable since no distinction is made between the income from land rent and that from labor and capital.