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FOOL'S PROFITS

by Barnard H. Bissinger

With the giveaway in full force garnished by plums such as the lowering of the excise taxes to shoot adrenalin into the heart of our economy, we wonder if the economic advisors will really succeed in getting for the country the long range success by giving the individual the immediate gain. Our wonder grows because of equally deep-seated economic theories that assure healthier gain, have a similar public appeal, but are not being used.

John Stuart Mill may have been the first one to point out that double taxation of the kind now imposed on savings by virtue of later taxing the income from the savings can work extensive destruction upon savings and spendings. The paradoxes that arise are sufficiently interesting in themselves to be told to the people who just might in turn begin an advisory campaign to our mortarboards now advising our government.

As recently as 1941 the eminent Irving Fisher expounded several frightening facts about government taxation of an individual's savings. He not only gave expertly the backfiring destructive effects but supported them with mathematics that would do honor to some of our present armchair solons.

Fundamental to derived defects, he said, was the serious effect of taxing capital-increase. A tax, levied yearly, will reduce the capital formation during a period of years more than will a tax levied at the same rate on the accumulated savings at the end of the period for a sufficiently long period of years. He gave an example of an initial capital of $1000 that has a growth rate of 40 per cent each year. If the yearly tax-rate on the yearly increase be 20 per cent, the initial investment would grow in 40 years to a sizeable amount, $66,500,000. But if it be left untaxed, it would become the stupendous $700,500,000. The imposed 20 per cent annual tax stunted the growth by over 90 per cent!

The first impression now may be "Who needs 700 million when they can have 66 million?" Another retort might be "Isn't it better it went to Uncle Sam?" That's just it, it didn't. Both parties took a licking. For the $634,000,000 lost by the taxpayer is much greater than what Uncle Sam gained in revenue, namely, a paltry $16,000,000. If the government had invested its annual tax bite at 5 per cent compound interest, it still would realize at the end of 40 years only $20,700,000, and the taxpayer still has lost the $634,000,000, the point here being the taxpayer loses considerably more than the government gains.

Now suppose the government has a final tax at death at the same rate. This gives our state 20 per cent of the $66,500,000, or $13,300,000. So the total gain is $30,000,000 and the taxpayer still records the $634,000,000 loss. If the government's 5 per cent interest prevails, the total gain is only $34,000,000. As if this isn't bad enough, we hasten to point out that less revenue is gotten from yearly taxes on capital-increase during life than from taxes at the same rate at death. In our numerical example the 20 per cent tax at death would be $140,100,000, to say nothing of other rewarding virtues. So we see one glaring loss to government of the difference between $140,100,000 and $20,700,000. Even if you add the death-tax to the life-tax, the loss in revenue is still $110,700,000. And once again bringing in the interest rate of 5 per cent, the loss maintains in excess of one million dollars.

Fisher used to say "to put *any* tax on savings is a penny-wise-pound-foolish policy, even from the narrowest fiscal point of view." Better should we reduce the tax all the way to zero. In our example this would give Uncle Sam a nice tidy 20 per cent of $700,500,000! The loss to our nation of $634,000,000 is not just that alone. This loss of earned increment might possibly represent that much capital equipment which in turn benefits labor and the general public.

So far we have said nothing of the psychological effect on people, the discouragement of saving. Obviously this makes matters worse! Hence we have less growth to insure at a later date larger spending on which a tax is healthy for all concerned.

What have we done? We have done away with an appreciable amount of revenue due to taxes on spending, a pedestrian political fanfare at best and only shortly after we had put the tax on savings. One of these moves is bad enough, but the ensemble is catastrophic. There an old Dutch saying, "It ain't what you eat what gets you the ulcers, it's what eats you." This just might help us Americans straighten out our DIET! □

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Ab Initio

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charge regardless of combined cost to the purchaser, his ability to pay, or any contributory norm.

It is a serious handicap to the activities of the Social Security Administration in rationalizing American hospital administration that they must limit their direct concern to the aged alone. This Dr. Brown thinks is a case of raising the level of a bed by lifting one of its legs. However, the person in the bed—the hospital management—has begun to realize that something is going on.

The intent of Medicare to provide a service benefit rather than an indemnity has, however, been frustrated to a marked degree by the unwillingness of American physicians to accept payment of Part B charges as determined under Medicare guidelines. Help in determining the proper levels under a variety of circumstances may be computerized.

The book winds up with a chapter on Health Care—the expanding frontier of Social Security—pointing out that we have only begun to take care of the needs of the population for basic protection.

The book is well organized and, although much of it may be well known to many actuaries, it is unquestionably worth reading. □

Actuarial Club Meetings

Nov. 15, Actuaries' Club of Des Moines

Nov. 20, Chicago Actuarial Club

Nov. 21, Actuaries Club of Philadelphia

Nov. 30, Nebraska Actuaries Club