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Earners' Apparent Income Gains Cancelled by Taxes and Inflation

Americans now find themselves in the paradoxical position of being both richer and poorer than they were at the beginning of this decade. The median income of the prototypical U.S. family (one earner, employed full-time, year-round, with a non-working spouse and two children) has increased by nearly 66 percent in the last seven years. At the same time, its after-tax purchasing power has declined by more than 8 percent since 1972, according to Tax Foundation economists.

From 1972 to 1979, the median family's money income climbed from $11,152 to an estimated $18,467. After direct Federal taxes, both income and social security, and inflation take their bite, however, the family's purchasing power, measured in 1969 dollars, has dropped $700—from $8,500 to $7,800—leaving the family richer on paper but poorer at the supermarket.

During this period, Federal individual income taxes jumped 82 percent, from $985 to $1,789, while social security taxes soared 142 percent, from $468 in 1972 to $1,132, in 1979. Total direct Federal taxes have more than doubled in seven years. While after-tax incomes were rising 60 percent, prices went up 75 percent. The result is an 8 percent decline in actual purchasing power.

For the ten-year period from 1969 to 1979, the rise in before-tax median family income barely managed to keep pace with the 99 percent climb in prices. Mounting taxes, however, caused an actual drop of 2 percent ($147 in 1969 dollars).

This "richer-is-poorer" situation does not even take into account the

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Median Incomes, Before and After Federal Taxes and Inflation

Year	Median income[a]	Direct Federal taxes: Income tax[b]	Direct Federal taxes: Social security	Direct Federal taxes: Total	After-tax income: Current dollars	After-tax income: 1969 dollars[c]
1969	$ 9,277	$ 956	$ 374	$1,330	$ 7,947	$7,947
1970	9,750	964	374	1,338	8,412	7,943
1971	10,314	937	406	1,343	8,971	8,119
1972	11,152	985	468	1,453	9,699	8,500
1973	11,895	1,100	632	1,732	10,163	8,385
1974	13,004	1,271	761	2,032	10,972	8,158
1975	14,156	1,179	825	2,004	12,152	8,278
1976	15,016	1,408	878	2,286	12,730	8,197
1977	15,949	1,472	933	2,405	13,544	8,194
1978[d]	17,223	1,733	1,042	2,775	14,448	8,117
1979[d]	18,467	1,789	1,132	2,921	15,546	7,800

[a] Median for all families with one earner employed full-time year-round as reported by U.S. Department of Commerce, Bureau of the Census, for 1969 to 1977; 1978 and 1979 estimated by Tax Foundation.
[b] Married couple filing joint returns, two children.
[c] Adjusted by the consumer price index of the Bureau of Labor Statistics.
[d] Income data for 1978 and 1979 are estimated.

Congress Ups U.S. Debt Lid For 19th Time

On September 28, 1979, the Senate passed and sent to the President for his signature a bill increasing the temporary ceiling on United States government debt to $879 billion through May 31, 1980. Senate approval was by a decisive 49 to 29 majority; two days earlier, the House had endorsed the measure by a much narrower 219 to 198 margin.

This action marked the nineteenth time that Congress had approved a "temporary" addition to the $400 billion permanent statutory ceiling on U.S. government debt it enacted in 1971. The action came shortly before the October 1 deadline which would have ended the existing $830 billion "temporary" ceiling approved on April 1 of this year, at which point the ceiling would have reverted to its permanent $400 billion limit. Pending congressional action, the U.S. Treasury Department had been forced to cancel two Federal bill auctions since it lacked the requisite power to incur new indebtedness until Congress acted.

On March 17, 1971, Congress raised the permanent U.S. debt ceiling from $380 billion to $400 billion, starting with fiscal 1972. Almost every year since then, in the spring and in the fall, separate laws have given the U.S. government authority

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The Front Burner

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"A Raise by Any Other Name"

The raise-no-raise shenanigans of Congress this fall bring to the front burner two issues that have very little to do with whether our Senators and Representatives will get a raise, or whether they deserve 5.5 percent, 12.9 percent, or no raise at all. The issues are "linkage" between the pay of members of Congress and that of thousands of top-level Federal executive and career employees, and the need for action on proposed Federal pay system reforms to relieve pressures on local governments to match Federal pay levels.

"Linkage" imposes a ceiling on the salaries of top-level executive officials and career civil servants, tying adjustments in their salaries to those for members of Congress. The result is that thousands of top-level career people find themselves compressed at the same salary level. A 5.5 percent or 7 percent cost-of-living boost does little to solve this problem, which has driven some of our most experienced and effective managers to take early retirement and look for greener pastures elsewhere.

Testifying before the President's Panel on Federal Compensation in August 1975, I proposed that this "linkage" be eliminated or at least modified. My argument was based on comparability, which I felt should prevail at the top of the government pay scale just as surely as at lower levels. "If the comparability principle is sound," I asked, ". . . why should not the indicated comparability pay adjustments be made throughout the civil service grade structure?" I also pointed out that, if this meant some career employees would earn more than their political bosses or than members of Congress, enough examples existed in the private sector to justify such an arrangement.

If those at the top are squashed into an unrealistically frozen level of earnings, middle- and lower-level government workers in Federal service enjoy a far larger comparability "universe" than meets the eye. This, too, causes problems, as public employees at the state and local levels try to whipsaw the units of governments which employ them into ever-expanded pay levels and benefit programs on the grounds that such practices prevail at the Federal level. This puts potential funding burdens on local units which are difficult to meet within realistic revenue-raising perimeters.

What can be done? The Administration proposes to base the annual comparability survey on total compensation (pay plus benefits), and to include state and local government employees within the comparability "universe." This is an eminently sensible approach to a very real problem. So is the proposal to relate the pay of nonprofessional white-collar Federal workers to local area pay levels.

As for the unrealistic ceiling on salaries of top-level professionals in government service, why not simply "raise the roof" a little? Even in a time of climbing government costs and double-digit inflation, you don't solve the problems of the public sector by driving out of Federal service the men and women best qualified to deal with the issues.

Keeping salaries too low might save a few dollars. In the long run, however, the old saying runs true: "You get what you pay for." In this area being "penny-wise and pound-foolish" can be especially damaging.

Inflation Task Force Has No Quick Inflation Cure

"Full employment, a gradually rising living standard, and close to no inflation" should be the economic goals of the nation, says the House Budget Committee's Task Force on Inflation in its unofficial summary of recommendations released on August 6. The report quickly notes that "the goals cannot be achieved this year or next."

To reach them at all, the study group asserts, will require "courage on the part of the Administration and Congress, and sacrifice on the part of the American people."

The bulk of the Task Force document lists 40 recommendations for dealing with inflation which grew out of two months of hearings involving testimony by 81 witnesses. The Task Force plans to issue its official, complete report, including "dissenting views of individual members of the Task Force on specific recommendations," sometime in December.

The special study group, chaired by Congressman Paul Simon of Illinois, cautions that there are no "comfortable, easy answers to the inflation problem." It says that the 40 recommendations "are an attempt to provide answers which are realistic, which impose the sacrifices which must be made, in a reasonably equitable manner."

As statistical background for its suggestions, the Task Force points out that inflation in 1979 has averaged 13.6 percent, 8 percent per year since 1973. By contrast, the Task Force notes, inflation from 1955 to 1965 averaged 1.6 percent per year.

The Task Force also explains that, of the 1979 Federal indebtedness of $839 billion, $303 billion was accumulated in the last five years. "We will soon mark only one year out of twenty," the report says, "when the budget has been in balance, a record which is economically indefensible." Financing such indebtedness, the Task Force asserts, consumes $58 billion—about 11 percent—of all Federal outlays.

"Unless inflation is brought under control to a much greater degree than is now the case—and soon—our free system of government will be drastically altered, almost certainly for the worse," the Task Force warns, citing the example of Germany more than four decades ago.

The study group divides its recommendations into four major categories:

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Task Force

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- Fiscal and Monetary Recommendations;
- Recommended Wage and Price Actions;
- Productivity Recommendations;
- Procedural Recommendations.

The Task Force urges the government to "recognize the relationship between deficits and monetary policy," noting that there is a "fundamental, practical relationship between fiscal and monetary policy" which must be recognized or "we will never deal effectively with the inflation phenomenon."

"To continue the present policy of regular deficits—even when the economy is functioning reasonably well—metes out the punishment of inflation, often on those who can afford it least," the Task Force says.

The report also calls for "carefully paced fiscal and monetary reforms, recommending a gradual reduction in the Federal deficit with a balanced budget in fiscal year 1982. "The Administration should avoid tax cuts until the budget is balanced," the report asserts, suggesting that a cut in social security taxes would be the least inflationary if the Congress and Administration cannot show the recommended restraint.

The Task Force links high employment with low inflation, recommending a government guarantee of jobs, "when jobs cannot be provided in the private sector."

"The sizable national expenditures on defense makes budget balancing difficult," the Task Force notes, recommending that the nation ask "our friends" to "shoulder a larger share of the financial burden." The nation must choose, according to the Task Force, either higher taxes, high unemployment, or reduced defense expenditures, "if we don't want high inflation rates." "By avoiding the choice," the study says, "we choose high inflation."

The Task Force strongly opposes further indexation of either taxes or spending programs, which it calls "in and of itself inflationary." "Indexation," the report cautions, "is inflation feeding upon itself."

"There should be no standby wage and price controls at this time," the study says, and the nation must move to reduce oil dependence. The Task Force also recommends that any Administration proposals for Real Wage Insurance "should be carefully considered."

The government must not be an "inflationary example," the report contends, conceding that "too often we are." As a "minor example," the report notes that cost of postage has been rising "much more rapidly than the Consumer Price Index."

The United States ranks fifteenth of the top fifteen exporters in total 1978 sales on a per capita basis, according to the Task Force, a situation which "weakens the dollar" and promotes inflation. "A one percentage point reduction in the international value of the dollar adds between 0.1 and 0.15 percentage points to the inflation rate," the report notes.

"Resist protectionism" and "promote competition," the Task Force urges, suggesting that the U.S. also follow the example of "most nations" and enact a youth differential as part of the minimum wage law. Trucking regulations must be changed to eliminate empty hauls and lessen the impact of shipping costs on food prices.

The Task Force urges that state governments be asked to finance projects "as much as possible without issuing bonds." "Those deficits," the report notes, "cause problems in the private money market, just as Federal deficits do."

Housing costs should be reduced, the report says, and the government should move toward "simplification of building codes, work-rule standards, and other regulations." "Additional timber cutting" should also be authorized, the committee says.

Noting that a 1 percent boost in productivity brings about an estimated 1 percent reduction in the inflation rate, the Task Force points out that U.S. productivity figures "in recent years are not encouraging."

Productivity must be approached "industry by industry," the Task Force says, and the government must move to reduce the "significant inflationary pressures produced by some regulations and regulatory actions." Proposed regulations should include a cost/benefit study. "Too many regulations are too detailed, too cumbersome, lacking in common sense, and totally uncoordinated," the Task Force asserts, adding, "there is too much change." They also recommend that regulatory agencies be required to answer inquiries within 60 to 90 days.

The nation must find a way, the report says, to protect those not employed without discouraging them from seeking employment. Greater encouragement of research and development is also needed.

Stating that "government by impulse is no longer an affordable luxury," the Task Force calls for multiyear budgeting. It also recommends bringing off-budget items onto the budget to make possible "adequate monitoring and control of Federal borrowing in the private money market." The Housing Error in the CPI must be corrected since the present method of calculation distorts the stated rate of inflation by about 1.4 percent (for 1978).

The government should move toward identifying all actions and proposals by the President and Congress that would either raise or lower the price level, the report suggests.

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About Tax Features

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Debt Lid

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to exceed—temporarily—that statutory limit. The year after the $400 billion limit went into effect, Congress voted to exceed it by $50 billion. For fiscal 1973, the $50 billion temporary ceiling was enacted again. Since then, the "temporary" increments have grown increasingly larger. In April 1979, the temporary addition exceeded the permanent limit for the first time.

Congress's action on September 28 covers the first eight months of fiscal year 1980, with the temporary additional ceiling standing at $479 billion, $79 billion more than the permanent limit. If the seven-year pattern prevails, Congress will repeat the process sometime in the first half of 1980.

Many Senators and Representatives view these periodic ceiling revisions as an opportunity to go on record as opposing rapidly rising Federal spending—even though Congress itself has approved most of the tax and spending measures which necessitate exceeding the permanent debt ceiling. Also, a substantial share of recent additions to the debt represent "off-budget" deficits over which Congress has no control except through the debt ceiling legislative process.

A new and significant wrinkle was added in this fall's deliberations, when Congress legally tied future limits on the debt to the amount specified in the most recently approved congressional budget resolution, by which targets are set for Federal revenue, spending, and debt for the upcoming fiscal year.

In March 1978, the House turned down a proposal from its Ways and Means Committee providing for such linkage. This time out, however, members backed such a connection by better than two to one.

The wisdom, and even the constitutionality, of linking the two procedures is widely debated. Legal scholars have pointed out that the debt ceiling is established by statute, requiring approval by the Chief Executive as well as both Houses of Congress. On the other hand, budget resolutions are adopted by the Legislative Branch and require no action from the Executive.

Those who favor connecting the debt limit and the budget resolution contend that legislators in the past have first voted amounts of spending that would require hiking the debt limit and, then, turned around and voted against the increased indebtedness which their own spending decisions had made necessary.

Opponents counter that keeping the two procedures separate and distinct forces lawmakers to take a stand on the specific issue of authorizing deficit spending. In addition, some legislators are reported to fear that tying the debt limit to the budget resolution will increase the already serious difficulties surrounding congressional approval of such resolutions.

The accompanying table shows the permanent and temporary additional statutory debt limitations for fiscal years 1972 to date.

Statutory Debt Limitations
Fiscal Years 1972 to Date
(In Billions of Dollars)

Fiscal year	Statutory debt limitation		
	Permanent	Temporary additional	Total
1972 through June 30	400	50.0	450.0
1973 through Oct. 31, 1972	400	50.0	450.0
1973 through June 30	400	65.0	465.0
1974 through Nov. 30, 1973	400	65.0	465.0
1974: Dec. 3, 1973 through June 30, 1974	400	75.7	475.0
1975 through Feb. 18	400	95.0	495.7
1975: Feb. 19 through June 30	400	131.0	531.0
1976 through Nov. 15, 1975	400	177.0	577.0
1976 through Mar. 15	400	195.0	595.0
1976 through June 30	400	227.0	627.0
TQ[a]: from July 1 through Sept. 30, 1976	400	236.0	636.0
1977: from Oct. 1, 1976 through Mar. 31, 1977	400	282.0	682.0
1977: from Apr. 1 through Sept. 30, 1977	400	300.0	700.0
1978: from Oct. 1, 1977 through Mar. 31, 1978	400	352.0	752.0
1978: from Apr. 1 through July 31, 1978	400	352.0	752.0
1979: from Aug. 1, 1978 through Mar. 31, 1979	400	398.0	798.0
1979: from Apr. 1 through Sept. 30, 1979	400	430.0	830.0
1980: from Oct. 1, 1979 through May 31, 1980	400	479.0	879.0

[a]Transition quarter.
Source: Committee on Ways and Means, U.S. House of Representatives.

Task Force

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Finally, the Task Force says, the government must move with "visible boldness." "Speeches will not be enough," the Task Force insists. "Unless the image of action is combined with the substance of action the 'psychology of inflation' will not be broken. Solid action taken in such a way that people understand and know what is happening is the medicine our ailing economy needs."

Gains Sapped

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added burden of state and local individual income taxes. Such levies vary widely, but on the whole, they have grown more rapidly than Federal income taxes and have a significant impact on family budgets. Total state and local individual income taxes are four times as high in 1979 as they were a decade ago and have increased relative to the Federal income tax burden. In 1969, states and localities took about 10.5 percent of what the Federal government claimed. By 1979, they were taking 16.3 percent. Given the assault of taxes and inflation on the typical worker's paycheck, it is possible to be richer and poorer at the same time.

The table on page 1 shows the effect of direct Federal taxes and inflation on median income since 1969.