

Building the Modern American Fiscal State: Progressive-Era Economists and the Intellectual Foundations of the U.S. Income Tax

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The ideas of economists and political philosophers, both when they are right and when they are wrong, are more powerful than is commonly understood. Indeed, the world is ruled by little else. Practical men, who believe themselves to be quite exempt from any intellectual influences, are usually the slaves of some defunct economist.”

– John Maynard Keynes

Introduction

At the turn of the twentieth century, the U.S. system of public finance underwent a dramatic transformation. The late nineteenth century structure of indirect national taxes, associated mainly with the tariff and regressive excise taxes on alcohol and tobacco, was eclipsed in the early decades of the twentieth century by a graduated federal income tax that soon accounted for more than half of all federal tax revenues.¹ A similar, albeit less pronounced, shift occurred at the state-level where the income tax soon came to challenge the dominant reliance on property taxes.² This shift in U.S. tax policy towards the direct and progressive taxation of income marked the emergence of a new fiscal polity – one that was guided not simply by the functional and structural need for government revenue but by concerns for equity and economic and social justice.

Although the early versions of the national and state-level income tax laws – with their high exemption levels and moderate rates – raised only a small percentage of total government revenues and affected a relatively small group of wealthy citizens, these early income tax laws were the thin edge of the wedge.³ Not only did exemption levels and rates change dramatically

¹ U.S. Bureau of the Census, *Historical Statistics of the United States, Colonial Times to 1970, Part 2* (Washington, D.C., 1975), pp. 1106-08 [hereinafter, *Historical Statistics of the U.S.*]; *Statistical Appendix to Annual Report of the Secretary of the Treasury on the State of the Finances for the Fiscal Year Ended June 30, 1971* (Washington: D.C.: Government Printing Office, 1971), p. 12. In 1880, 90% of federal government revenues came from the combination of customs duties (56%) and internal excise taxes (34%). By 1930, income taxes accounted for approximately 59% of all federal government receipts. Id.

² At the state and local level, the income tax was only able initially to make a small dint into government revenues. But over time, the income tax did provide state and local governments with an opportunity to diminish their reliance on the property tax. In 1890, nearly 80% of state and local government receipts were derived from the property tax, and by 1932 that figure had dropped to less than 60%. *Historical Statistics of the United States*, pp. 1106-08; U.S. Bureau of the Census, *Census of Governments, 1967 Vol. VI, No. 5* (Washington, D.C.: Government Printing Office, 1967); *Report on Wealth, Debt and Taxation at the Eleventh Census: 1890 Part II, Valuation and Taxation* (Washington, D.C.: Government Printing Office, 1895), pp. 412-3.

³ The 1913 federal income tax, which initiated the permanent national taxation of income, had a high exemption level of \$3,000 for single persons (\$4,000 for married couples), and began with a “normal” tax of only one percent that was graduated to a maximum “surtax” rate of six percent for incomes over \$500,000. This law also contained a

over the course of the twentieth century, but the revenues generated by the income tax soon became the lifeblood of the burgeoning American regulatory, administrative and welfare state. As early as the start of the 1920s, at the conclusion of the First World War, the income tax came to dominate federal revenues.⁴ Though the reach of the income tax laws was scaled back during the retrenchment of the interwar period, the larger trend towards the direct and progressive taxation of income was accelerated in response to the national emergencies of the Great Depression and the Second World War.⁵ Indeed, by the end of the twentieth century the progressive income tax had become the central foundation of modern American public finance, generating in fiscal year 2002 nearly 60% of federal receipts, and on average about 40% of state-level revenue.⁶

The dramatic transformation in American public finance occasioned by the rising prominence of the income tax raises several salient questions about the making of tax policy at the turn of the twentieth century. How and why, for example, was this radical transformation in American public finance possible? What were the historical factors at work that affected, and were affected by, this dramatic change in fiscal policy? More specifically, how and why did the direct and progressive taxation of income become the dominant source of federal government revenue? And, perhaps most importantly, what role did the emergence of this new fiscal order play in the changing status of American state-society relations?

In seeking to answer these critical questions, conventional historical accounts of the American income tax have generally focused on the state's need for revenue, contending that the rise of the income tax can best be explained as a structural-functionalist response to the growing demands of the public sector.⁷ Other common interpretations examine the role of political parties and party competition over the issue of protectionism and tariff revenue in explaining why the corporate and individual income taxes were adopted when they were.⁸ Even those

flat one percent tax on corporate net income. Pub. L. No. 63, Statute I – 1913, Chapter 16, Sections II-A, II-C *Statutes At Large of the United States of America from March 1911 to March 1913*, Vol. XXXVIII, Part 1 (Washington, D.C.: Government Printing Office, 1913). Similarly, the Wisconsin income tax of 1911, which began the effective state-level taxation of income, had high levels of exemption and low statutory rates. The 1911 Wisconsin income tax was set at a graduated rate that ranged from 1% on the first \$1,000 above the exemption level of \$800 for single taxpayers (\$1,200 for married couples) to a maximum rate of 6% on all taxable income in excess of \$12,000. *Wisconsin Session Laws 1911 Chapter 658* (Madison, WI: Democrat Printing Co., State Printer, 1911).⁴ By 1920, well over 60% of federal government receipts were obtained from income taxes. *Historical Statistics of the United States*, pp. 1106-08.

⁵ While World War II provided the impetus for transforming the income tax from a “class tax” to a “mass tax,” it was the turn-of-the-century transformation that established the intellectual and institutional foundations of the modern American income tax. On the WWII transformation, see generally, W. Elliot Brownlee, *Federal Taxation in America: A Short History* (Cambridge, 1996), pp. 89-100 [hereinafter Brownlee, *Federal Taxation*]; for more on how WWII induced a change in tax paying culture, see Carolyn C. Jones, “Class Tax to Mass Tax: The Rise of Propaganda in the Expansion of the Income Tax during World War II,” 37 *Buffalo Law Review* 685 (1989).

⁶ *Statistical Abstract of the United States: 2002* (Washington, D.C.: Government Printing Office, 2001), Table No. 464, p. 315; *State Profiles, The Population and Economy of Each U.S. State* (Lanham, MD: Bernan, 2002), Table IL-17, p. 169. These figures suggest that the American historian George Mowry was correct to claim as early as the 1950s that “the modern democratic social service state probably rests more upon the income tax than upon any other single legislative act.” Mowry, *The Era of Theodore Roosevelt and the Birth of Modern America, 1900-1912* (New York: Harper, 1958), p. 263.

⁷ John Witte, *The Politics and Development of the Federal Income Tax* (Madison, WI: University of Wisconsin Press, 1985); Bennett D. Baack and Edward John Ray, “Special Interests and the Adoption of the Income Tax in the United States,” 45 *J. Econ. Hist.* 607 (Sept. 1985).

⁸ Christopher Howard, *The Hidden Welfare State: Tax Expenditures and Social Policy in the United States* (Princeton: Princeton University Press, 1997); Elizabeth Sanders, *The Roots of Reform: Farmers, Workers, and the*

scholars who have set out to explore the redistributive potential of tax laws have generally concluded that the roots and development of the American income tax rest more with placating revenue demands than with issues of economic equity. For this last group of scholars, the income tax, like so many of the other reforms of the Progressive Era, is viewed as a form of sophisticated conservatism, a clever ploy to domesticate potentially more radical forms of wealth redistribution.⁹

This concentrated focus on the revenue-side of taxation tells us only part of the historical story. Taxation has always been about *both* revenue and equity; about effectively raising government funds and fairly distributing fiscal burdens. The accepted narratives and interpretations that view the ascendancy of the income tax as simply a revenue-generating process, or more cynically as a conservative ruse to forestall more radical calls for economic redistribution, have marginalized the reallocative potential of taxation. Put simply, the preoccupation with revenue has elided how the early development of income tax laws was driven by the need to reallocate more fairly the burden of financing a modern nation-state.¹⁰

This paper, by contrast, contends that the income tax had its roots in social concerns about justice, fairness and the equitable distribution of fiscal burdens. More specifically, this paper claims that the income tax was the product of calls for economic justice and a response to social democratic claims made upon the state. Common historical accounts that have focused on the failure of the income tax system to redistribute wealth have obscured our understanding of what the rise of the direct taxation of income did, in fact, accomplish. The new fiscal order that emerged at the turn of the century was by no means a radical system of wealth redistribution, nor was it merely a conservative bulwark against more radical reform.

Instead, the modern American fiscal state that emerged in the early twentieth century dramatically altered the distribution of fiscal burdens, both along class and regional lines. By replacing the nineteenth century structure of regressive indirect consumption taxes with a direct tax on income and other forms of wealth, the new fiscal polity shifted the burden of financing a modern, industrial state on to those segments of society that had the greatest tax paying ability, namely wealthy citizens in the North and Northeast. This move – this transition towards a more transparent and fairer system of taxation – was a qualified achievement. Although it did not go

American State, 1877-1917 (Chicago: University of Chicago Press, 1999); Richard F. Bensel, *The Political Economy of American Industrialization, 1877-1900* (Cambridge: Cambridge University Press, 2000).

⁹ As the tax historian, Robert Stanley has put it, the income tax “represented not an expression of real economic democracy,” but rather “a rejection of the far more fundamental institutional change advocated by intellectuals and street dissidents of both left and right.” Robert Stanley, *The Dimensions of Law in the Service of Order: Origins of the Federal Income Tax, 1861-1913* (New York, 1993), p. 12. Similarly, Morton Horwitz has claimed that limits placed on the state’s taxing powers exemplify how “the impermissibility of redistribution embodied one of the central tenets of the nineteenth-century idea of the liberal state.” Morton J. Horwitz, *The Transformation of American Law, 1870-1960: The Crisis of Legal Orthodoxy* (New York, 1992); see also Gabriel Kolko, *The Triumph of Conservatism: A Reinterpretation of American History, 1900-1916* (New York, 1963), pp. 112, 129; for more general monographs in this vein, see, Mark Leff, *The Limits of Symbolic Reform: The New Deal and Taxation, 1933-1939* (Cambridge, 1984); James R. O’Connor, *The Fiscal Crisis of the State* (New York, 1973); Albert L. Ellis, *The Regressive Era: Progressive Era Tax Reform and the National Tax Association – Roots of the Modern American Tax Structure* (Ph.D. Diss., Rice University, 1991).

¹⁰ While there is an older historiography of the income tax that celebrates the achievements of the income tax, this literature is often infused in a tone of liberal triumphalism that sees the creation and development of the income tax as part of a teleological march towards democratic progress. See, for example, Sidney Ratner, *American Taxation, Its History as a Social Force in Democracy* (New York: W.W. Norton, 1942); Roy G. Blakey and Gladys C. Blakey, *The Federal Income Tax* (New York: Longmans, Green and Co., 1940); Randolph E. Paul, *Taxation in the United States* (Boston: Little Brown and Co., 1954).

as far as some progressive reformers had envisioned, this new fiscal polity laid the foundation and held out the promise of a new, more progressive American tax regime.

Among the forces that helped forge this modern American fiscal state, none was perhaps more important than the intellectual movement supporting the direct and graduated taxation of income. To be sure, there were several other factors, including popular social movements and institutional changes, that helped usher in this new fiscal order. Intellectuals alone could not build a new fiscal polity. Nonetheless, the turn-of-the-century structural transformation in American public finance was guided mainly by a paradigm shift in the legal and economic theories that undergirded tax policy.¹¹ It was academic political economists, trained predominately in Germany, who responded to the social and political circumstances of the times by leading the intellectual charge for a permanent, progressive income tax.

This paper explores how these key American intellectuals, responding to their historical conditions, were able to apply their social and political theories to the development of American tax laws and policies. More specifically, this paper contends that a particular group of academic political economists played a pivotal role in supplanting the “benefits theory” of taxation, and its concomitant vision of the state as a passive protector of private property, with a more equitable principle of taxation based on one’s “faculty” or “ability to pay” – a principle that promoted a more active role for the positive state in the distribution of fiscal burdens. In so doing, these thinkers were able to use the growing concentration of wealth, moments of national emergency, and the ascendancy of new economic theories during the Gilded Age and Progressive Era as justifications for using a progressive income tax to redistribute more fairly the fiscal burdens of financing the emerging regulatory, administrative, welfare state. Led by the likes of Richard T. Ely, Henry Carter Adams, and Edwin R.A. Seligman, these economists were at the forefront of the battle not only to dismantle the orthodox theories of laissez-faire, but also to advance the adoption of new, more effective and equitable forms of taxation.¹²

This historical shift in the economic and legal ideas that undergirded tax policy was reflective of a much larger change in American social thought at the turn of the century. For the move from “benefits” to “ability to pay” was part and parcel of what American intellectual historians have referred to as “the revolt against formalism” – a revolt that included a transformation in American liberalism away from a focus on negative liberties towards a more active role for the positive state.¹³ Spurred by the modern forces of mass immigration,

¹¹ The larger project, from which this paper is derived, explores the multitude of idealistic and material forces that affected the emergence of the income tax at the turn of the twentieth century, including the influence of the legal profession and the popular movements for tax reform. See, Ajay K. Mehrotra, “Creating the Modern American Fiscal State: The Political Economy of U.S. Tax Policy, 1880-1930” (Ph.D. Diss., University of Chicago, 2003).

¹² In charting the role that these economists played in laying the intellectual groundwork for the new fiscal order, this paper is not meant to be a traditional history of disembodied ideas or a philosophical explication of the truth claims made by these historical figures. Rather, this paper seeks to historicize the ideas that underwrote the emergence of the modern income tax by placing these theories within their social, political and economic context. The empirical aim is to show how idealistic and material historical forces combined to facilitate the paradigm shift in tax theories at the turn of the twentieth century. The more normative task of uncovering the philosophical underpinnings of progressive income taxes, and revealing the tensions within tax theories is left to other papers published in this symposium and elsewhere. Marjorie Kornhauser, “Political Philosophy and the Tax Progressivity Debate,” *UCLA L. Rev.* (2005); Liam Murphy & Thomas Nagel, *The Myth of Ownership: Taxes and Justice* (Oxford, 2002); on the inherent tensions within the tax theory of ability to pay, see Stephen Utz, “Ability To Pay,” *23 Whittier L. Rev.* 867 (2002).

¹³ See generally, Morton White, *Social Thought in America: The Revolt Against Formalism* (Boston, 1957). For a more detailed account of the changing face of American liberalism at the turn of the twentieth century, see, Mary O.

urbanization and industrialization that created a much more interdependent world, this change in American liberalism embodied in the Progressive Movement, had a profound impact not only on tax policy, but on nearly every aspect of state-society relations. In the realm of tax law, as the historian James T. Kloppenberg has noted, “the graduated income tax, based on the idea that everyone owes a debt to society proportional to his ability to pay was perhaps the quintessential progressive reform.”¹⁴ Protective labor legislation, the emergence of antitrust laws, and numerous other reforms were all representative of this progressive re-orientation of the relations between society, economy and the state.¹⁵

A century or so has passed since that dramatic transformation in American liberalism facilitated the Progressive economists’ intellectual charge for a graduated income tax. Though much has changed since then, some alarming similarities appear to have reemerged. As the subtitle of this symposium suggests, the turn of the twenty-first century has brought with it a new era of rising inequality in wealth and opportunity; a new era that has placed into bold relief what some contemporary commentators see as the possibility of a New Gilded Age in the United States.¹⁶

Amidst these circumstances, this paper on the intellectual foundations of our modern income tax is meant to be a cautionary tale and a modest reminder. It is meant to be a cautionary tale both for those scholars who mistakenly assume, however implicitly, that the income tax was originally meant to redistribute wealth and income in a dramatic way,¹⁷ and for those tax scholars who have recently embraced a return to benefits theory as a way to bolster our current tax system.¹⁸ On a more positive note, given the current desires for tax reform, this paper is meant to be a modest reminder of the historical beginnings and social context that gave birth to a system of taxation that admittedly was based not on radically redistributing wealth, but was driven by the need to reallocate, in a more transparent and progressive manner, the fiscal burdens of financing a modern nation-state. This paper thus attempts to tell the story of how one group of socially-engaged and reform-minded academics tried to provide the intellectual support for an historic change in the American system of taxation.

This paper is divided into three parts. To comprehend the significance of the transformation in American public finance occasioned by the establishment of the federal income

Furner, “Knowing Capitalism: Public Investigation and the Labor Question in the Long Progressive Era,” in Mary O. Furner and Barry Supple, eds. *The State and Economic Knowledge: The American and British Experience* (Cambridge, 1990); on the transatlantic aspects of this new form of liberalism, see James Kloppenberg, *Uncertain Victory: Social Democracy and Progressivism in European and American Thought, 1870-1920* (New York, 1986); Daniel Rodgers, *Atlantic Crossings: Social Politics in a Progressive Age* (Cambridge, 1998); for a recent and rather unconvincing reinterpretation of this period of American liberalism, see Nancy Cohen, *The Reconstruction of American Liberalism, 1865-1914* (Chapel Hill, 2002).

¹⁴ Kloppenberg, *supra* note [X], at 355.

¹⁵ See, generally, Morton Keller, *Regulating a New Economy: Public Policy and Economic Change in America, 1900-1933* (Cambridge, 1990);

¹⁶ For more on the rise of New Gilded Age in the late twentieth century, see Kevin P. Phillips, *The Politics of Rich and Poor: Wealth and the American Electorate in the Reagan Aftermath* (New York, 1990); David Remnick, ed. *The New Gilded Age* (New York, 2001); Paul Krugman, “For Richer” *New York Times Sunday Magazine* Oct. 20, 2002; Thomas Pinketty and Emanuel Saez “Income Inequality in the United States, 1913-1998” *Quarterly Journal of Economics* 118:1 (February 2003), pp. 1-39; “Ever Higher Society, Ever Harder to Ascend,” *The Economist*, December 29, 2004, p [x].

¹⁷ Stanley, *Law and the Dimensions of Order*; Witte, *Politics and Development of the Federal Income Tax*.

¹⁸ Deborah A. Geier, “Time to Bring Back the ‘Benefit’ Norm?,” *Tax Notes*, March 1, 2004, p. 1155; Herwig J. Schlunk, “Double Taxation: The Unappreciated Ideal,” *Tax Notes*, Feb. 16, 2004, p. 893.

tax, this paper begins in Part I with a description of the nineteenth-century system of indirect taxes and an explanation of the historical factors that led to the decline of this old order. Part II, then, provides a brief genealogy of the notions of “benefits” and “faculty.” This genealogy illustrates how the Progressive economists were operating as part of a longer tradition in the history of tax concepts and economic ideas. Part III focuses on the political economists of the late nineteenth and early twentieth centuries and their efforts to use the logic of “ability to pay” rationale to underwrite the movement for a progressive income tax. Finally, the conclusion explains why, at the dawn of the twenty-first century, an historical tale about the intellectual foundations of the modern, American income tax remains poignant and pertinent.

I. The Gradual Demise of the Nineteenth-Century, Indirect Tax Regime

The extent to which indirect taxes, particularly import duties, dominated federal revenues throughout the nineteenth century is often underappreciated. In fact, revenues from the tariff accounted, on average, for approximately 85% of the annual federal budget during the antebellum period.¹⁹ Although the crisis of the Civil War introduced, on a temporary basis, a successful national income tax in the North, indirect excise taxes on imports and everyday commodities such as sugar, alcohol and tobacco remained the cornerstone of federal receipts throughout the last decades of the nineteenth century.²⁰ Of course, the federal budget at this time was relatively small, with spending limited to the military, and the legacy of the Civil War.²¹ Nevertheless, as federal government spending increased at the turn of the century, the indirect system of taxation continued to dominate, at least until the First World War.

These indirect taxes affected nearly every aspect of daily consumption. The breadth of goods that fell under the tariff’s duty list in the late nineteenth century was indeed astonishing. The Tariff Act of 1883, for instance, placed a levy on fourteen different categories of products including “Chemicals;” “Earthenware and Glassware;” “Metals;” “Wood and Wooden Wares;” “Sugar;” “Cotton and Cotton Goods;” “Hemp, Jute, and Flax Goods;” “Wool and Woolens;” “Silk and Silk Goods;” “Books and Papers,” and the catch-all category of miscellaneous “Sundries.” The schedule for “Provisions” listed in the 1883 law alone consisted of such everyday necessities as “Beef and pork; Hams and bacon; Cheese; Butter; and substitutes thereof; Lard; Wheat; Rye and barley; Oats; Corn-meal; Oat-meal; Rye-flour; Potato or corn starch; Potatoes; Rice; Hay; Honey; Hops; Milk; Salmon and other fish; Pickles and sources, of all kinds; Vegetables; Vinegar; Chocolate; Dates, plums and prunes; Oranges; Lemons; Raisins,” and a large assortment of nuts. Although the “duty charges,” or rates, were relatively low, ranging from “one cent per pound of beef and pork” to “four cents per pound of cheese,” they had a significant impact in increasing the daily cost of living in America.²²

¹⁹ *Historical Statistics of the United States*, p. 1106. During the antebellum period, proceeds from the tariff fell below 75% of federal income only during the Jackson and Van Buren administrations when federal land sales contributed significantly to the federal treasury. Hansen, “Taxation and the Political Economy of the Tariff,” p. 529.

²⁰ As late as 1890, more than 90% of federal government revenues came from the combination of customs duties and internal excise taxes. *Historical Statistics of the United States*, p. 1107-8.

²¹ In 1890, for instance, the federal government spent more than a fifth of its budget on the military, 11% on servicing its debt, much of which was acquired during the Civil War, and over a third on Civil War pensions – that quintessential proto-welfare state measure. *Historical Statistics of the United States*, p. 1115.

²² Schedules A - N, Section 2502, Chapter 121, Tariff Act of March 3, 1883, *The Statutes at Large of the United States of America*, Vol. XXII (Washington: Government Printing Office, 1883).

For many policymakers and economic commentators, inflationary pressures were just one of the adverse effects of the indirect tax regime. A revenue system based on customs duties and excise taxes also proved to be unstable, inflexible and unfair. It was unstable because receipts varied with the vicissitudes of international trade and social consumption patterns. It was inflexible because it gave government actors little leverage over the source of funds, and it was considered unfair because the bulk of the burden fell on those with limited economic resources. These drawbacks became particularly pronounced during times of national stress and strain, when crises often required governments to access revenue quickly and effectively. Writing in the wake of the Panic of 1893, during the last great recession of the nineteenth century, Robert Hoxie, the University of Chicago labor economist, observed that “the customs revenue system, through inherent inflexibility and instability, is incapable of serving as an adequate source of public revenue in times of emergency.” Since moments of national crisis were crucial testing grounds, “no nation could be found willing to base its finances on a system that must fail it in time of stress,” Hoxie continued. “This conclusion then is really equivalent to a general condemnation of the customs revenue system as the main source of a national income.”²³

The tariff was criticized not only for its internal defects, but because its protection of domestic industries undermined the economic ideals of free-trade. For those economists who were weaned on the treatises of Adam Smith and John Stuart Mill, the benefits of comparative advantage had made free-trade an obvious choice. There were, of course, many American economic thinkers who favored protecting “infant industries.” Henry C. Carey, the Pennsylvania publisher and economic writer, trained generations of antebellum students to believe in the virtues of a high protective tariff.²⁴ But after the Civil War, when the inherent flaws of the tariff and indirect consumption taxes became readily apparent, free-trade thinking came to dominate.²⁵

Yet despite this seeming convergence around free-trade ideas, the protective tariff remained a central part of American economic and foreign policy throughout the last decades of the nineteenth century. The political and economic powers behind protectionism were not only able to muffle the voices of some economic thinkers; they also had access to the ears and pockets of influential lawmakers. Even the foremost authority on the tariff, the Harvard economist F.W. Taussig, was hesitant in completely repudiating protectionism.²⁶

Economic ideas alone were not enough, however, to erode the traditional reliance on the indirect system of taxation. Material factors, namely changes in political and economic conditions, helped to hasten the demise of the *ancien* tax regime. Foremost among these factors was the deterioration of the Republican Party’s coalition supporting protectionism. The tariff had long been an endemic issue in American politics, pitting Northeastern Republican interests who favored protectionism against the more agrarian political base of the Democratic Party. After the Civil War, Republicans were able to widen and tighten their hold over the protective tariff by appealing to new sets of constituencies. By including such items as wool, hides, and grains on to the duties list, Northeastern Republicans were able to bring western and mid-western farming interests into the protectionist fold. Similarly, Republicans used revenues from the tariff to underwrite the nation’s first proto-welfare provisions, Civil War pensions. Since only

²³ Robert F. Hoxie, “Adequacy of the Customs Revenue System,” 3 *Journal of Political Economy* 39 (Dec. 1894), p. 71.

²⁴ Henry C. Carey, *Principles of Political Economy* (1837 – 40); *The Public Debt* (Philadelphia, 1866), pp. 11-15; Joseph Dorfman, *The Economic Mind in American Civilization, Vol. III, 1865-1918* (New York, Viking Press, 1949), pp. 5-7.

²⁵ Douglas Irwin, *Against the Tide, An Intellectual History of Free Trade* (Princeton, 1997)

²⁶ F.W. Taussig, *The Tariff History of the United States* (1892); Dorfman, *supra* note X, at 270-1.

Union Army veterans were eligible for these pensions, Republicans were able to solidify their support for the tariff in the North and West, while further marginalizing the resistance of Southern Democrats.²⁷

The Republican coalition supporting protectionism began to erode in the early years of the twentieth century. Increasing federal government surpluses, an aging population of Civil War veterans, a mature industrial economy and other factors contributed to the skepticism surrounding protectionism. Democrats and Progressive Republicans began questioning whether the protective tariff created more detriments than benefits. The rising cost of living and the increasing concentration of wealth and corporate capital, opponents of the tariff claimed, were directly tied to the Republican agenda of high import duties. Southern Democrats, after all, had long identified the tariff as “the mother of trusts.” The growing consolidation of holding companies at the time, and the increasing fortunes of their owners, seemed to ratify that the protective tariff had outlived its usefulness.²⁸

As support for the tariff waned, other pressures compelled the federal government to consider alternative forms of financing. Though the need to provide Civil War pensions was decreasing over time, as the population of veterans declined, the federal government was becoming increasingly active, both at home and abroad, in the decades straddling the turn of the century. The Spanish-American War, and the beginnings of an overseas military empire required increased funds, as did the maintenance and rise of new regulatory and administrative agencies.²⁹

These two issues – the increasing demand for federal revenue and the decreasing supply of import duties – combined with a third factor, the growing disparity of wealth, to spur the turn-of-the-century transformation in American public finance. As modern economic historians have demonstrated, the distribution of wealth became increasingly concentrated in the late nineteenth century.³⁰ Commentators at the time were not unaware of this trend in inequality. Many critics even went so far as to attribute the visible poverty and class conflict of the times to this growing disparity of wealth and opportunity. Indeed, the Panic of 1893, which triggered the ensuing depression, exacerbated the visibility of growing poverty and class conflict. It was against this backdrop of growing dissatisfaction with the tariff, increasing pressure for more government revenue, and concern over rising inequality that the Progressive-Era economists made their mark in helping build the modern American fiscal state.

II. A Brief Genealogy of the Benefits and Faculty Principles

When American political economists set out to construct the theoretical blueprints for the new fiscal polity, they were able to rely on a long tradition of equitable tax principles. Neither

²⁷ Paul Wolman, *Most Favored Nation: The Republican Revisionists and U.S. Tariff Policy, 1897-1912* (Chapel Hill: University of North Carolina Press, 1992); Joanne Reitano, *The Tariff Question in the Gilded Age: The Great Debate of 1888* (University Park: Pennsylvania State University Press, 1994); John Mark Hansen, “Taxation and the Political Economy of the Tariff,” *International Organization* 44:4 (Autumn, 1990), 527-51.

²⁸ Elizabeth Sanders, *The Roots of Reform: Farmers, Workers, and the American State, 1877-1917* (Chicago: University of Chicago Press, 1999).

²⁹ By 1900, spending on the Department of Army and Navy constituted the single largest category of federal spending, amounting to almost 40% of total spending. *Historical Statistics of the United States*, p. 1115.

³⁰ Richard H. Steckel and Carolyn M. Moehling, “Rising Inequality: Trends in the Distribution of Wealth in Industrializing New England,” 61 *J. of Econ. Hist.* 160 (March 2001); Simon Kuznets, “Economic Growth and Income Inequality,” 45 *Am. Econ. Rev.* 1 (1955).

the benefit principle nor the notion of “faculty,” which was used synonymously with tax paying capacity and the ability to pay, was unique to the historical development of the American income tax. Both of these rationales had coexisted throughout the western world for centuries. Frequently, the two were conflated into one general justification for a diverse set of levies. The coterminous development of these disparate ideas over time shows how neither theory was ever able to completely replace the other. The task of the Progressive-Era political economists was thus two-fold. They needed, first, to delineate the divergent social theories that undergirded each of the two tax principles; and, second, they needed to demonstrate why a progressive income tax supported by the notion of faculty was the historically appropriate form of taxation for a modern, industrial nation-state. In seeking the first objective, economists at the turn of the century were able to draw on a long, though often undifferentiated, intellectual tradition.

Taxation, of one form or another, has existed since human societies first began to mobilize and allocate resources. But the development of self-conscious and systematic theories supporting taxes appears to be of a more recent vintage. The ancient Athenians and Romans appeared to justify their taxes implicitly based a combination of principles, without precisely elaborating on the theories that supported these principles. The liturgical burdens and property taxes borne by wealthy Athenians, for example, were viewed as civic obligations justified by the superior resources of the aristocratic class. These burdens, in other words, were premised on the capacities and endowments created by birth and rank. At the same time, ancient Greek aristocrats used their enhanced wealth and power, and the fiscal sacrifices that such wealth and power entailed, to argue for a more active role in government. According to this logic, the contribution of taxes were justified not only as a civic duty, but also as a political benefit enshrined in the positive rights of the ruling class.³¹

The Romans similarly fused the principles of benefits and faculty in their tax systems. From roughly the third to the sixth centuries, taxes throughout the Roman Empire were also based mainly on the passive context of land ownership, where property tax payments were deemed to be an indirect discharge of the emperor’s debts to the army and civil service, and occasionally on the active liturgical context, where taxes were part of the requirements of citizenship.³² The former resembled the modern theory of benefits, especially since property tax payments ultimately financed the protection provided by the Roman army, while the latter was akin to the principle that citizens should contribute to the commonwealth according to their abilities.

In the medieval towns of Western Europe, taxes based on both the capacities of individual citizens and the benefits they received from the government persisted. The general property tax of French, German and English towns was usually levied proportionally according to the amount of real property owned by a resident. The medieval property tax itself was premised on a dual set of principles: on the one hand, taxes were based on social rank, determined by one’s status in the feudal system, suggesting that taxes were a function of the benefits bestowed by the sovereign upon his subjects. On the other hand, the medieval “corporate levy,” which was extracted from the urban freemen who lived outside the feudal ranks, was premised on the obligations of membership in organizations such as guilds or towns.³³

³¹ Maureen B. Cavanaugh, “Democracy, Equality, and Taxes,” 54 *Ala. L. Rev.* 415, 461-3 (2003) A.H.M. Jones, *Athenian Democracy*, (1957), p. [x]; M.I. Finley, *The Ancient Economy* (1973), p. [x].

³² Goffart, *Caput*, pp. 105-6. A.H.M. Jones, *The Later Roman Empire, 284-602* (Oxford, 1964), pp. 462-9.

³³ Dennis Hale, “The Evolution of the Property Tax: A Study of the Relation between Public Finance and Political Theory,” 47 *J. of Politics* 382 (1985).

As a supplement to this source of revenue, income taxes, occasionally set at graduated rates, were also evident throughout Europe during this period. Generally limited to income derived from labor, these wage taxes were founded on the more democratic spirit that “individual faculty or ability to pay taxes were supposed to be in some manner fixed by individual income.”³⁴

The process of analytically differentiating between the two principals of taxation began with the seventeenth and eighteenth century social contract theorists. From Hobbes and Locke to Grotius and Pufendorf to Montesquieu and the Physiocrats, classical liberal thinkers concerned primarily with defining the relations between state and society started to privilege the benefits rationale. Locke succinctly summarized how the benefit principle was fundamentally based on the state’s role in protecting private property: “everyone who enjoys his share of the protection [of the state] should pay out of his estate his proportion for the maintenance of it.”³⁵ In advocating the superiority of benefits theory, many of these theorists concluded that property, in fact, was an inadequate measure of the benefits received from the state because too few citizens who received public benefits actually owned land. Theorists such as Hobbes and Locke, thus, used the benefits theory to support a tax not on property but on consumption.³⁶

While the early Enlightenment witnessed the initial ascendancy of benefits theory, the concept of faculty remained critical for many other theorists. There was perhaps no better example of how the theories of benefits and faculty remained intertwined during this period than Adam Smith’s well known and often-cited first axiom on taxation. “The subjects of every state,” wrote Smith, “ought to contribute towards the support of the government, as nearly as possible in proportion to their abilities, that is in proportion to the revenue which they respectively enjoy under the protection of the state.”³⁷ Subsequent political economists, mostly notably J.S. Mill, would depart from Smith’s conflicting use of the two theories to argue for a variant of the faculty theory, namely that “equality of sacrifice” – measured in terms of diminished individual utility – should be the touchstone for modern tax policies.³⁸ Still, for most of the nineteenth century, tax policy discourse remained wedded to justifying taxes in terms of both faculty and benefits.

Indeed, the continuous coexistence of these concepts over time illustrates how the history of ideas is seldom about the victory of one concept over another. As the legal historian, Neil Duxbury has noted, “Ideas – along with values, attitudes and beliefs – tend to emerge and decline, and sometimes they are revived and refined. But rarely do we see them born or die.”³⁹ Thus, neither the benefits principle nor the faculty theory was created or destroyed at the turn of the twentieth century. Rather, American tax theorists, building on the path breaking work of J.S. Mill, attempted to delineate between these rationales in effort to reveal, what they believed, was an antiquated social theory underpinning the benefits principle.

III. The Progressive-Era, Public Finance Economists

The professional economists who led the campaign for an income tax at the turn of the century were part of a larger cohort of academic social scientists who were seeking to dismantle the orthodox theories of laissez-faire that dominated classical and neo-classical visions of law

³⁴ Seligman, “The General Property Tax” PSQ (1890), pp. 47-52. .

³⁵ John Locke,

³⁶ Kaldor, Expenditure Tax

³⁷ Adam Smith, *Wealth of Nations*, Book V, Chap. II, p [X].

³⁸ John Stuart Mill, *Principles of Political Economy*, Book V, Ch. 11, p. [x]. Stephen Utz, “Ability To Pay,” 23 *Whittier L. Rev.* 867 (2002).

³⁹ Neil Duxbury, *Patterns of American Jurisprudence* (Oxford, 1995), pp. 2-3.

and political economy. Responding to the material forces of modernity that had eroded notions of self-reliant individualism, this rising class of professional social scientists sought to demonstrate, through their writings and teachings, the mutual interdependence of modern social relations. With the establishment of the American Economic Association (AEA) in 1895, the economists were among the first group of social scientists to sever their ties to the general antebellum field of moral philosophy, and place their discipline on a more professional standing.⁴⁰

From the beginning, the young generation of economists who founded the AEA sought to use their training to address the social concerns of the day. Calling themselves the “new school” of American political economy, these young maverick intellectuals challenged the reigning system of economic thought.⁴¹ Eschewing timeless universalisms, these academics resolutely believed that economic relations were embedded in a larger social and institutional matrix – a matrix that was often constituted by law and legal processes. Although seeds of this institutionalist strand of American economic thought would not fully blossom until the 1920s and early ‘30s, many of the leading “new school” economists were eager to use the law to exercise the “ethical agency” of state power. In this way, many of these ethical or proto-institutionalist economists were, indeed, part of what legal historians have identified as the “First Great Law & Economics Movement.”⁴²

Among this first generation of professionally-trained economists, there were several who were interested in public finance. Occupying influential teaching posts throughout the country, thinkers such as Henry Carter Adams, Richard T. Ely, and Edwin R.A. Seligman dedicated much of their careers to the empirical and theoretical study of taxation. Others, of course, contributed to the emerging American literature on public finance. But it was Adams, Ely and Seligman who were representative of their generation of economic thinkers, and who proved to be the pivotal historical figures guiding the paradigm shift in tax theory that pushed faculty to the fore.

Common Bonds

What united Adams, Ely, Seligman and many of the other ethical or institutionalist economists were their personal backgrounds and the experiences of coming of age during the turbulent decades of the late nineteenth century. Though Ely, Adams and Seligman were each reared in rather different environments, they all shared at an early age an interest in social reform. Ely was raised in the agricultural region of upstate New York by a family of ardent Presbyterians, who had hoped that young Richard would one day join the ministry. Similarly, Adams was born and raised in Iowa, the son of a Congregational minister and abolitionist leader, who also had aspirations of turning his son into a minister. Seligman, by contrast, was the child

⁴⁰ For more on the professionalization of the social sciences, see generally, Thomas L. Haskell, *The Emergence of Professional Social Science: The American Social Science Association and the Nineteenth Century Crisis of Authority* (Urbana, 1977). Mary O. Furner, *Advocacy & Objectivity: A Crisis in the Professionalization of American Social Science, 1865-1905* (Lexington: University of Kentucky Press, 1975); Dorothy Ross, *The Origins of American Social Science* (Cambridge, 1991).

⁴¹ For more on the “new school” of American political economy, see generally, Furner, *supra* note [X], Chapter 3; Sidney Fine, *Laissez Faire and the General-Welfare State: A Study of Conflict in American Thought, 1865-1901* (Ann Arbor: University of Michigan Press, 1964); add coates.

⁴² Herbert Hovenkamp, “The First Great Law & Economics Movement,” 42 *Stan. L. Rev.* 993 (April 1990); Barbara H. Fried, “The Progressive Assault on Laissez Faire: Robert Hale and the First Law and Economics Movement (Cambridge, 1998).

of an affluent, New York City German-Jewish family that was active in civic and social reform organizations.⁴³

If their upbringing inclined these three men towards social change, their experiences with the harsh material realities of late nineteenth century life fortified their reformist tendencies. Not only did the forces of rapid industrialization and urbanization heighten the disparity of wealth, it also fueled class conflict and labor unrest during this period.

The prevailing importance of the “labor question” was not lost on these budding academics. After searching for work in the streets of New York, Ely resolved himself as early as 1880 to become an advocate for the working class.⁴⁴ When Adams began his graduate training at Johns Hopkins he was also struck, as he walked the streets of Baltimore, by the extent of urban poverty.⁴⁵ Although Seligman was the scion of a prestigious banking family, he too was empathetic to the needs and wants of the working class, as his early scholarship on the cooperative movement and Christian socialist suggested.⁴⁶ Indeed, nearly this entire generation of American academics struggled with the long-standing dilemma of attempting to “bridge the world of educated opinion and that of the working masses.”⁴⁷ For those who became interested in public finance, the distribution of fiscal burdens was an ideal topic to help close the chasm between high brow theories and the material world of the masses.

The German Influence

Above all else, the most important common bond that united Ely, Adams, Seligman and the other Progressive economists was their economic training abroad in Germany. Following the path of their American mentors, a whole host of aspiring American academics made a sojourn to Germany to complete and often complement their graduate school training. As one of the oldest of the group, Ely helped initiate this trans-Atlantic transference of ideas and pedagogy by not only attending Heidelberg to complete his doctorate, but by also bringing the German seminary model of teaching back to Johns Hopkins, where he began his teaching career.⁴⁸ Adams, who received one of the first doctorates granted by an American university (Johns Hopkins), also completed his graduate studies at Heidelberg and Berlin, where he studied with Adolf Wagner,

⁴³ Historians of economic thought have written at great length about how this generation of political economists, including Ely, Adams, and Seligman, were united by a religious fervor for social reform. While all three of these thinkers were reared in an environment where religion was important – for Ely and Adams the evangelicalism of Protestantism, and for Seligman reformed Judaism – they also shared the common trait of turning their backs on the religious desires of their families. Ely and Adams attempted but eventually gave up on careers in the ministry, and Seligman at a relatively early age turned his back on Judaism. Furner, *Advocacy & Objectivity*; Ross, *Origins of American Social Science*; [add cite to Eustace Seligman oral history].

⁴⁴ Richard T. Ely, *Ground Under Our Feet, An Autobiography* (New York, 1938), pp. 164-5; Benjamin G. Radner, *The Academic Mind and Reform* (Lexington, 1966), p. 16; Ross, *Origins of American Social Science*, p. 105.

⁴⁵ Henry Carter Adams to Mother, 29 October 1876, “Correspondence 1876 Jan. – June,” Box 1, Henry Carter Adams Papers, Bentley Historical Library, University of Michigan, Ann Arbor, Michigan. Ross, *Origins of American Social Science*, p. 106.

⁴⁶ Seligman, *Two Chapters on the Mediaeval Guilds of England*; “Owen and the Christian Socialists,” *PSQ* Vol. 1 No. 2 (June 1886), pp. 206-49.

⁴⁷ Leon Fink, *Progressive Intellectuals and the Dilemmas of Democratic Commitment* (Cambridge, 1997).

⁴⁸ Rader, *Academic Mind and Reform*, p. 18; William J. Barber, “Political Economy in the Flagship of Postgraduate Studies: The Johns Hopkins University,” in *Economists and Higher Learning in the Nineteenth Century*, ed. William J. Barber (New Brunswick, NJ: Transaction Publishers, 1993).

one of Germany's leading authorities on public finance.⁴⁹ Seligman, who had family ties in Germany and often visited Europe during his childhood, also studied in Heidelberg and Berlin, under the tutelage of Wagner and other well-know German economists.⁵⁰

This common intellectual connection to Germany was more than just a coincidence. Unlike some of their more conservative colleagues, Ely, Adams, Seligman and many other members of the "new school" were deeply indebted to the training they received in Germany. The more radical American students became great admirers of the scholars who made up the German Historical School of Economics. Ely, Adams and Seligman each studied under some of the leading figures of this so-called school of thought, and Seligman, who had the greatest affinity for German culture, corresponded with his teachers long after his days as a student.⁵¹

Not surprisingly, historians of economic thought have disagreed about the coherency and legitimacy of the so-called German Historical School; they have questioned whether it was really a "school of thought," whether it was, in fact, "historical," and even whether it was truly "German."⁵² Still, most commentators agree that German academics such as Wilhelm Roscher, Gustav Schmoller, Karl Knies and Adolph Wagner – to name only a few – coalesced as a group of intellectuals who during the second half of the nineteenth century came to question the metaphysical laws of classical political economy. Led by Roscher, who in the 1840s began the assault on deductive, a priori systems of economic thought, the subsequent generation of German academics contended that universal economic laws were incoherent outside of their social, political and economic context.

Like the German school of jurisprudence, which Roscher explicitly sought to emulate, the German historical economists believed that there were no natural laws of political economy. Instead, they contended that social and economic relations were contingent upon historical and institutional contexts. These scholars used the term "historical" in its broadest sense to highlight not only the significance of the past, but to renounce generalizing theories in favor of a fidelity to the particularity of actual events.⁵³ From this vantage point, scholars such as Schmoller critiqued the tenets of classical and neoclassical theory, and took a normative position on the role of the state in guiding the economy and society. In contrast to the laissez-faire bias of classical theory, the German historical economists argued that the increasing complexity and interdependence of modern society required a changing and more active role for the positive state.⁵⁴

⁴⁹ Joseph Dorfman, "Introductory Essay – Henry Carter Adams: The Harmonizer of Liberty and Reform," in *Two Essays by Henry Carter Adams*, ed. Joseph Dorfman (New York: Augustus M. Kelley, 1969); Rodgers, *Atlantic Crossings*, p. 97; William J. Barber, "Political Economy in the Flagship of Postgraduate Studies: The Johns Hopkins University," in *Economists and Higher Learning in the Nineteenth Century*, ed. William J. Barber (New Brunswick, NJ: Transaction Publishers, 1993), pp. 203-24.

⁵⁰ Carl S. Shoup, "Seligman" in David L. Sills, ed. *International Encyclopedia of the Social Sciences* (New York, 1968); Frank Rozwadowski, "From Recitation Room to Research Seminar: Political Economy at Columbia University," in *Economists and Higher Learning in the Nineteenth Century*.

⁵¹ Joseph Dorfman, "The Role of the German Historical School in American Economic Thought," 45 *Amer. Econ. Rev.* 17 (May 1955); Jurgen Herbst, *The German Historical School in American Scholarship: A Study in the Transfer of Culture* (Ithaca: Cornell University Press, 1965); Rodgers, *Atlantic Crossings*, Ch. 3; Ross, *Origins of American Social Science*, p. 104.

⁵² Heath Pearson, "Was There Really a German Historical School of Economics?" *History of Political Economy* 31:3 (1999), 547-562; Joseph Dorfman, "The Role of the German Historical School in American Economic Thought" *American Economic Review* 45:2 (May 1955), 17-28; Jurgen Herbst *The German Historical School in American Scholarship: A Study in the Transfer of Culture* (Ithaca: Cornell University Press, 1965).

⁵³ Pearson, "Was There Really a German Historical School of Economics?" p. 548

⁵⁴ Rodgers, *Atlantic Crossings*; Ross, *Origins of American Social Science*; Furner, *Advocacy & Objectivity*.

It was this methodological emphasis on contingency and the normative appeal to state action that had the greatest influence on the young American political economists who were trained at the foot of the German historical school. As historians have demonstrated, the generation of American scholars who traveled to Germany in the last decades of the nineteenth century came back to the United States with a more radicalized and fervent desire for reform.⁵⁵ In their role as academics, these progressive intellectuals adopted the pedagogical seminar style of the German universities, and absorbed the substantive lessons of their German teachers. In the process, they helped forge not only a new view of economics but a distinct form of American new liberalism that advocated using the powers of the state to address the numerous social dislocations of modern industrial society.⁵⁶

Nowhere was the influence of German historicism on American new liberalism more apparent than among those American scholars who were interested in public finance. Ely, Adams and Seligman, in particular, returned from their post-graduate experiences in Germany with a sincere interest in understanding public finance, or what their German teachers referred to as *Finanzwissenschaft*, the “Science of Finance.” Having read Schmoller’s historical tracts and Adolph Wagner’s calls for the need for a redistributive tax policy, Ely, Adams and Seligman began to build the intellectual foundations of American public finance. But first they had to translate the general philosophy of the German historical school for an American audience.

From Berlin to Baltimore

Ely was one of the first Americans to transplant the ideas of his German teachers across the Atlantic, identifying the German historical school as the model for the American “new school” of heterodox economists. Although he was careful not to dismiss completely the contributions of Adam Smith and the classical political economists, Ely described their ideas as outdated, as he proclaimed that a historical and institutional approach was now carrying the day.⁵⁷

Seligman soon followed Ely’s lead. In one of his first published essays, Seligman claimed that German scholars, such as Roscher, Knies and Hildebrand, were the first thinkers to place economic ideas on a “truly scientific basis” by proclaiming “the necessity of treating economics from the historical stand-point.” It was these German thinkers, and now their American counterparts in the new school, Seligman contended, who discarded “the exclusive use of deductive method” and called for the “necessity of historical and statistical treatment;” it was they who denied “the existence of immutable natural laws in economics, calling attention to the interdependence of theories and institutions, and showing that different epochs or countries require different systems.” It was the German historical school, Seligman continued, that abandoned any “belief in the beneficence of the absolute laissez-faire system,” and maintained “the closer interrelation of law, ethics, and economics,” while refusing to accept “the assumption of self-interest as the sole regulator of economic action.” Finally, and most importantly for Seligman, the new school shared with its German counterpart the need to address contemporary problems. Once it was free from the reigning orthodoxy of laissez-faire, “the new school, devoid of all prepossessions, devoted itself to the task of grappling with the problems which the age had

⁵⁵ Id.

⁵⁶ See supra note [X].

⁵⁷ Ely, “The Past and Present of Political Economy,” *2 Overland monthly and Out West Magazine* 225 (Sept. 1883).

brought with it.” These were the main principles, Seligman argued, that their German mentors had bequeathed to the new school of American political economy.⁵⁸

The American new school, according to the Progressive economists, was not, however, a simple imitation of German historicism. Both “schools of thought” were rather a function of changing material circumstances. Ideas were not the engines of change, material economic conditions were. Thus, the message of the German historical school was a manifestation of an industrial era, and similarly “the new school,” Seligman explained “is the product of the age, of the *zeitgeist*, not of any particular country; for the underlying evolutionary thoughts of a generation sweep resistlessly throughout all countries whose social conditions are ripe for change.” Even English economists – those most ardent supporters of timeless economic and legal doctrines – Seligman argued, could not resist the force of the *zeitgeist*, as John Stuart Mill “himself had gone through an evolution and was sincere enough to express his disbelief in the old economy, and to a certain extent in his own work.” This commitment to the relativity of economic and legal doctrines – a relativity that Ely, Adams, and Seligman acquired mainly during their European education – would be an essential part of their overall fiscal vision.⁵⁹

Applying the New Political Economy to Tax Policy

In applying their theories to the “needs and wants” of the state in a rigorous and scholarly manner, these American economists were operating on relatively new ground.⁶⁰ Though the tariff remained a politically charged topic in the U.S. and elsewhere throughout the turn of the century, there was little scholarly discussion about the general economic principles of taxation beyond the political controversy surrounding the tariff. Throughout the nineteenth century, the taxing powers of state and local governments in the U.S. were, of course, necessary in promoting a “well-regulated society,” and local and state sales and property taxes were topics of discussion among some social commentators.⁶¹

Yet, few contemporary scholars emphasized the political and economic power that lay behind the federal government’s ability to levy taxes. As late as 1880, Francis A. Walker, Adams’s mentor at Hopkins and a leading authority on political economy, could confidently claim, “The body of English literature in finance is shabby in the extreme.” The main explanation for the “febleness and emptiness of the English literature in this department,” according to Walker, was the lack of serious scholarly attention given to taxation. “Most of our political economists have not dealt with the subject at all, or have done so very perfunctorily.”⁶²

The young reform-minded economists set out to change all that. Proceeding from two different origins, Ely and Adams began the American engagement with the “Science of Finance.” Adams had always had an interest in issues of taxation and public finance. His dissertation was a historical analysis of the protective tariff, and his first treatise was focused on public debts. In his thesis, Adams illustrated how although the taxing powers of the new republic were originally instituted for the purpose of securing revenue, political pressures at the

⁵⁸ Seligman, “Change in the Tenets of Political Economy with Time,” *Science – Supplement* April 23, 1886, p. 381.

⁵⁹ Id.

⁶⁰ Adams, *Public Debts*, p. [X].

⁶¹ William J. Novak, *The People’s Welfare: Law and Regulation in Nineteenth-Century America* (Chapel Hill: University of North Carolina Press, 1996). For more on the political charged nature of the tariff see, Richard F. Bense, *The Political Economy of American Industrialization, 1877-1900* (Cambridge: Cambridge University Press, 2000).

⁶² Francis A. Walker, “The Principles of Taxation,” *The Princeton Review* 2 (July-December 1880), pp. 93-4.

time dictated that the tariff be used for protectionist objectives.⁶³ Adams's historical research demonstrated that this initial justification for protectionism subsequently cloaked the proper purpose of the tariff. Lawmakers continued to renew the protectionist tariff even though its initial political justifications disappeared. In the end, the main contention of Adams's thesis was that the early manipulation of tax policy led directly to the late nineteenth century abuse of the tariff to protect domestic industry. Adams's normative goal was to insure that "tariff reform means tariff for revenue only." From the start, then, Adams was attempting to use his scholarship to affect the making of tax policy.⁶⁴

This desire to influence policymaking continued with Adams subsequent work on public debts. Preoccupied by the enormous national debt created by the Civil War, Adams wrote a thorough and detailed analysis on public borrowing – arguably the first American treatise on public finance – in which he argued that modern nation-states had become overly reliant on debt financing. With the American Civil War in mind, Adams emphasized how the flexibility and accountability inherent in taxes made them superior to public debt. Moreover, the unequal distribution of wealth that was a by-product of industrial capitalism was supported, Adams argued, by a state's reliance on loans, as opposed to taxes, to fund its needs.⁶⁵

Not only did public borrowing, in Adam's estimation, insure that the moneyed classes controlled the "machinery of government," but it also ossified class distinctions. The legal institution of private property already assured that "the citizens of a state are divided into two classes – those who pay taxes for the support of the debt, and those who receive interest payments out of the proceeds of the taxes." And given the fact that "industrial leisure, rendered possible by proprietorship in fixed investments of any sort, is a habit easily acquired, we may discern," Adams concluded, "how the funding system readily lends its influence to the permanency of class relations." Simply put, Adams believed that public debts exerted an adverse social influence on class relations by reifying the disparity of property possession.⁶⁶

Yet despite these drawbacks, Adams recognized that during emergencies nation-states had little choice but to rely on public borrowing. As a constructive and realistic reformer, his theoretical preference for taxation over public debts gave way in the face of empirical and pragmatic circumstances. By no means did Adams advocate that taxation by itself could be an adequate substitute for government bonds; such a policy would jeopardize that most important source of all state revenues: industrial society. A well-balanced fiscal policy, thus, meant a taxing system that could both mitigate some of the anti-democratic tendencies of public debts without threatening industrial productivity – a sound fiscal policy, according to Adams, included a system of taxation that respected "the mechanisms of production."⁶⁷

An Early Salvo Against the Property Tax

⁶³ Because Britain after the Revolutionary War was attempting to reestablish its economic dominance over the new republic through the Navigation Acts, the U.S. tariff was used not simply to raise revenue, but rather as a protectionist tool to combat British naval imperialism. Adams, *Taxation in the United States, 1789-1816* (Johns Hopkins University Studies in Historical and Political Science, 1884).

⁶⁴ *Id.*, at 19.

⁶⁵ Henry Carter Adams, *Public Debts: An Essay in the Science of Finance* (New York: Appleton and Co., 1892 [1887]) p. 9. Even though one of the aims of the book was to advance the study of public finance in the United States, the treatise gained an international audience, including an edition translated into Japanese.

⁶⁶ *Id.*, pp. 42-3.

⁶⁷ *Id.*, p. 109.

Unlike Adams, Ely came to study taxation later in his career and without any grand conception of how taxes constituted a sound system of public finance. Rather, Ely approached tax issues from a more bottom-up, inductive method when he was appointed as an economic expert to the Baltimore and Maryland tax commissions in the mid-1880s. In pioneering the empirical study of municipal and state-level finance, Ely used his official position to gather data on numerous North American cities and several American states. Ely was left appalled, from this work, by the “worthless” system of state and local taxation that he observed. Struck by how unfair the process of assessing property was on the ground, Ely dissented from the rudimentary recommendations of the commissions to enforce the existing laws more stringently, and issued his own supplemental report calling for a radical overhaul of the state and local system of taxation.⁶⁸

At about the same time that Ely was evaluating the Maryland and Baltimore tax systems, Seligman was conducting his own international analysis of property taxation. Although the two scholars were working independently, their evaluations of the general property tax were remarkably consistent. Indeed, the property tax had become the favorite whipping boy of nearly every economic commentator during the end of the nineteenth century. Still, what set Ely and Seligman apart was how they applied historicism in their analysis of the property tax. Their examinations focused on how the property tax no longer corresponded to modern industrial conditions – how the property tax because of changing historical conditions no longer adhered to what they saw as the touchstone of modern taxation: the principle of “ability to pay.”

To be sure, Ely and Seligman did not invent the “ability to pay” principle; as we have seen, it had a long lineage dating back at least to the classical period of antiquity. But “ability to pay” aptly captured the proper relation, in their minds, between the state and society, between the sovereign and the people. In addressing the problem of the property tax, Ely advocated the innovative idea of separating state and local government revenues. He recommended that local governments apply the property tax only on real estate, which could not be easily hidden, while state governments resort to a graduated income tax to fund their needs.⁶⁹

Seligman provided a more detailed critique of the property tax and its departure from the principle of “ability to pay.” In his early salvo against the property tax, Seligman made three principled points. First, he demonstrated that the property tax was not exceptional to American conditions, as many commentators had claimed. And because it was not unique, the American property tax was susceptible to the forces of historical change. Second, and perhaps most importantly, Seligman illustrated how the property tax was now flawed “because property is no longer the criterion of faculty or tax-paying ability.” With the changes in economic conditions, Seligman asserted, “the standard of ability has been shifted from property to product.” Put simply, Seligman believed that the emergence of modern, industrial society meant that wealth could no longer simply be equated with property. “Not the extent but the productivity of wealth constitutes the test.” Revenue, or the flow of wealth – not its mere physical embodiment – was the true measure of one’s ability-to-pay.⁷⁰

⁶⁸ Ely, “Supplementary Report on Taxation in Maryland,” in *Report of the Maryland Tax Commission to the General Assembly* (Baltimore, 1888). Rader, *Academic Mind and Reform*, supra note X, at 85-6.

⁶⁹ Id. In a review of Ely’s work, Seligman commented that Ely had underestimated the support for a move to an income tax. “It will be found on examination that many business men, especially in those localities where any attempt is made to enforce the taxation of personal property, are in reality not at all inimical to the income tax.” Seligman, “

⁷⁰ Seligman, “The General Property Tax,” *PSQ*, 5:1 (March 1890).

Finally, Ely and Seligman indicted the general property tax on administrative grounds. It was a levy that could not be effectively collected because it could not get at the increasing forms of intangible or “invisible” wealth, such as bonds, stock and mortgages, and because it “puts a premium on dishonesty and debauches the public conscience.” But most importantly, for Seligman, the property tax was no longer practical because “it presses hardest on those least able to pay.” In light of these problems, the income tax, Seligman believed, was “infinitely superior in practice.” From all this, Seligman passionately concluded “the general property tax is so flagrantly inequitable that its retention can be explained only through ignorance or inertia. It is the cause of such crying injustice that its abolition must become the battle cry of every statesman and reformer.”⁷¹

In advocating for an income tax based on the notion of ability to pay, the reform-minded economists needed to address the defects of the then dominant tax theory of benefits. In their estimation, the idea that taxes should be levied according to the amount of government benefits that a citizen/taxpayer received was linked to the classical, “night watchmen” view of the state. Thus, just as they had attacked this obsolete notion of limited government, they set out to dismantle the benefits theory. In so doing, they faced resistance from both the political left and right.

The Conservative Opposition to Income Taxes

From the right, conservative commentators such as William Graham Sumner, the Yale sociologist, and David A. Wells, the former commissioner of Internal Revenue, argued that an income tax violated the benefits principle and the notion of human equality. Sumner was one of the old guard defenders of laissez-faire, who denounced the protective tariff as a form of state capitalism; he also similarly believed that income taxes aimed at reallocating fiscal burdens was an example of unnecessary state intervention in the natural struggle for all “to get capital.” The only thing that one could expect from government was a minimal amount of protection of historically-based rights; this, of course, implied that citizens only had a limited responsibility to pay for such protection. Sumner passed along this belief in libertarian individualism to one of his best students interested in taxation, Irving Fisher.⁷²

During some of the earliest discussions of income taxation, David Wells joined Sumner in opposing such a levy. Wells was no stranger to the importance of using taxes to fund an army and build a nation, but he, like many of the old guard academics, was adamantly opposed to the use of progressive income taxes. As early as 1880, when there were discussions among some lawmakers to revive the Civil War income tax that was allowed to expire in 1872, Wells spoke out against graduated income taxes. Except for the extreme cases of war, Wells argued, there was no place in a free republic for any form of a graduated income tax based on the ability to pay.

Nearly all income taxes in the western world had some sort of exemption level, and most had graduated rates. But for Wells, exemptions and progressive rates spelled the worst sort of government discrimination. “Any government, whatever name it may assume, is a despotism, and commits acts of flagrant spoliation,” Wells intoned, “if it grants exemptions or exacts a greater or lesser rate of tax from one man than from another.” It was not only the “entirely

⁷¹ Id., p. 24.

⁷² W.G. Sumner, “Protective Taxes and Wages,” *North American Review* 136 (March 1883), pp. 270-277; *What Social Classes Owe Each Other* (1883). Ross, *Origins of American Social Science*, p. 88.

unpractical” administration of an income tax that troubled the former federal tax administrator; it was the fundamental principle that any discrimination in taxation was by definition “purely arbitrary,” and hence “an act of charity which every American ought to reject upon principle and with scorn.” Demonstrating how he believed progressive income taxes were indeed a form of emasculating charity, Wells concluded that “equality and manhood, therefore, demand and require uniformity of burden in whatever is the subject of taxation.”⁷³

The Populist Opposition: Henry George’s Single Tax

Although Wells and Sumner were certainly not alone either in opposing the leveling effects of a redistributive income tax, or by associating such levies with a gendered view of masculinity, other popular voices were not so reluctant to call on the state’s taxing powers to address the growing disparity of wealth in the nation. But even these voices were causes for concern among the reform-minded economists. The most strident of these voices was Henry George, a journalist turned economic commentator, who proposed his own type of tax system that was at odds with the income tax and the principle of ability to pay. In a hugely popular book, George advocated that the government impose a levy only on the increase in land values, a single tax on the “unearned increment” of appreciated land. When Henry George’s *Progress and Poverty* burst onto the social scene in 1879, it was only a matter of time before many social movements took up the calls for a single tax. During the 1880s and well into the early twentieth century, the single tax became a popular movement demanding a tax on land, specifically rent, as the exclusive source for all government revenue.⁷⁴

George’s single tax on land was a simple, if not simplistic, idea aimed at curbing land speculation and forestalling more radical attempts at tax reform. Because George believed that land was the source of all of wealth, he argued that it should be taxed as common property. Combining the teachings of the Bible and Aristotle, George concluded that the “unearned increment” on land came from the growth of populations, from society itself, rather than individual effort, and thus the state had an obligation to reclaim such unearned increment on behalf of society.⁷⁵

The rhetoric of reclaiming the value created by society had a socialistic ring. But George was no socialist. Instead, he held a rather conservative view of individualism in arguing that the fruits of individual labor did indeed belong to the individual, and that the state had very little role to play in economic or social matters beyond levying a single tax on land. With a very limited role for the state, George believed that there was little need for any tax beyond the unearned

⁷³ David A. Wells, “The Communism of a Discriminating Income Tax,” *North American Review* 130 (March 1880), pp. 238-9, 246. Ironically, while Wells was linking tax equality and uniformity with masculinity, women were already using their status as taxpayers to fight for full citizenship. Carolyn Jones, “Dollars and Selves: Women’s Tax Criticism and Resistance in the 1870s,” 1994 *University of Illinois Law Review* 265 (1994); Linda Kerber, *No Constitutional Right to Be Ladies: Women and the Obligation of Citizenship* (New York: Hill and Wang, 1998), Chapter 3.

⁷⁴ Henry George, *Progress and Poverty: An Inquiry into the Causes of Industrial Depressions and of Increase of Want with Increase of Wealth ... The Remedy* (New York: Robert Schalkenback Foundation, 1960, [1879]). For more on George and his times, see Charles A. Barker, *Henry George* (New York: Oxford University Press, 1955); Stephen B. Cord, *Henry George: Dreamer or Realist?* (Philadelphia: University of Pennsylvania Press, 1965); John L. Thomas, *Alternative America: Henry George, Edward Bellamy, Henry Demarest Lloyd, and the Adversary Tradition* (Cambridge, Mass.: Belknap Press, 1983).

⁷⁵ George, *Progress and Poverty*, pp. 299-394.

increment of rent. It was only the people's natural share in wealth that he sought to tax for the purposes of government revenue.

Most professional social scientists ridiculed George's ideas when they did bother to address them. Throughout much of the 1880s, most professional economists ignored George's writings, especially after Francis Walker's biting criticism of "George's Social Fallacies" seemed to provide the final word against George. George's own caustic style and obstinate nature certainly did little to endear him to the emerging academic professionals. In 1890, George came into direct contact with his critics when the American Social Science Association devoted a session to the single tax. As part of that session, Seligman exhibited his youthful exuberance by purporting to speak for the entire profession, as he poignantly attacked George and the single tax. In future years, Seligman would publish a more careful and calmer analysis of George's single tax, but at the conference he followed Walker's earlier lead by denouncing George and his "schemes" as "repugnant to our moral sense and repellent to our logic." Other academic political economists joined Seligman at the conference in berating the ideas of the "amateur" economist.⁷⁶

Though George's idea of using such a single tax to address nearly all the ills of modern capitalism caught on with many grass-roots movements at the turn of the century, it did not fit neatly into either of the contending views of governance. Neither the laissez-faire proponents – who abhorred almost any kind of taxation, particularly one on the most sacrosanct of private property – nor the advocates for a more robust positive state could see much merit in George's ideas. At its core, though, George's single tax idea was a narrow application of the benefits principle. Landowners owed a duty to the state because it was the state that protected the private property rights of landowners; this reciprocal relationship captured the essence of benefits theory. While George appealed to many among the producing classes – more to labor than farmers – because of his populist appeals attacking land speculators and monopolists, the single tax itself was premised on a conservative, if not reactionary, view of individualism, hence many socialists spurned it.

Navigating Between the Two Extremes

Faced with these critiques from the political right and left, the reform-minded economists attempted to navigate between these poles in pushing for the progressive income tax. Building on the work of J.S Mill, their solution was to concentrate on how an equality of sacrifice could be melded with the notion of ability to pay. In this way, they wanted to move away from the reciprocal notion of taxation, away from the idea that taxes reflected a *quid pro quo* between government and the people. The progressive economists preferred to view taxes as a "contribution," as Adams pointed out in his early treatises, because contributions did not imply any form of reciprocity, but instead suggested that taxes were part of the obligations of citizenship.

Some economists carried this notion one step further. Thomas N. Carver, a professor of political economy at Oberlin College and later Harvard, used a version of the "minimum sacrifice" theory to support a "moderately progressive system of taxation." Carver argued that it was neither notions of "benefits" nor "contributions" that captured the essence of an effective

⁷⁶ Barker, *Henry George*, pp. 565-7. On the history of the American Social Science Association, see Thomas Haskell, *The Emergence of Professional Social Science: the American Social Science Association and the Nineteenth Century Crisis of Authority* (Urbana: University of Illinois Press, 1977).

and fair tax system, but rather “the least evil to the least number.” This theory, which Seligman would build upon and refine, was an application of neoclassical marginal utility analysis to the notion of minimum sacrifice. By turning the utilitarian principle of “the greatest good to the greatest number” on its head, Carver deduced that “the evils of taxation are two-fold – the sacrifice to those who pay the taxes, and the repression of the industry and enterprise which they occasion.” Policymakers needed to be aware of both of these evils, and balance the two against each other, when they structured a tax system. They needed to realize that, on the one hand, an equality of sacrifice among individuals meant that each taxpayer would pay a proportional yet varying amount of taxes, insuring that the proper work incentives remained intact. At the same time, a minimum amount of total aggregate sacrifice suggested that the wealthy should pay more taxes because they received less utility from their last dollar. In Carver’s words: “The minimum amount of repression is secured by imposing an equal sacrifice on all members of the community, but the minimum amount of sacrifice is secured by collecting the whole tax from those few incomes which have the lowest final utility.” A similar theory of minimizing aggregate disutility was emerging in Britain at about the same time with the writings of F.Y. Edgeworth.⁷⁷

In his writings on progressivity, Seligman contrasted his support for progressive taxes, based on the principle of faculty, or ability to pay, with other prevailing theories. Unlike the “socialistic” theories of Adolph Wagner and the more moderate “compensatory theory of progression” forwarded by Francis Walker, Seligman contended that the theory of ability combined with “the marginal utility theory of value” furnished “an irrefragable proof of the necessity of progression.”⁷⁸

Wagner’s justification for progressivity was too radical for Seligman’s moderate ways. Seligman admitted that his former instructor appropriately identified the social aspects of fiscal policy – that taxes were used for much more than just government revenues. But he warned that this was a far cry from what Wagner and his socialist disciples advocated. “From the principle that the state may modify its strict fiscal policy by considerations of general national utility, to the principle that it is the duty of the state to redress all inequalities of fortune among its private citizens, is a long and dangerous step,” Seligman warned. “It would land us not only in socialism, but practically in communism.”⁷⁹

The problem for Seligman and other more moderate proponents of progressive taxes, however, was that many commentators and political economists erroneously assumed that “progressive taxation necessarily implies socialism and confiscation.” Citing explicitly to the work of David Wells, Seligman argued “it is quite possible to repudiate absolutely the socialistic theory of taxation and yet at the same time advocate progression.” This then was Seligman’s aim: to show his readers – social commentators, lawmakers and professional academics alike – that one could defend progressive taxes without being a socialist.⁸⁰

⁷⁷ T.N. Carver, “The Ethical Basis of Taxation and Its Application to Taxation,” *Annals of the American Academy of Political and Social Science*, 6 (July 1895), pp. 97, 99; F.Y. Edgeworth, “The Pure Theory of Taxation,” *Economics Journal* 7 (1897), p. 550. For a comparison of Carver and Edgeworth and their views on progressive taxation, see Herbert Hovenkamp, “The First Great Law & Economics Movement,” *Stanford Law Review*, 42 (April 1990), pp. 1002-8.

⁷⁸ Seligman, “The Theory of Progressive Taxation,” *Publications of the American Economic Association*, 8:1 (Jan. 1893), 52-55; “The Theory of Progressive Taxation,” *PSQ* 8:2 (June 1893), pp. 220-51; *Progressive Taxation in Theory and Practice* (Baltimore: American Economic Association, 1894).

⁷⁹ Seligman, “Theory of Progressive Taxation,” p. 222,

⁸⁰ *Id.*

This was no small task. As Seligman and many other academics had learned from H.C. Adams's harsh dismissal from Cornell, the "socialistic" tag often blinded people to the logic and reasoning behind any plausible reforms. This tension between academic freedom and the confining political climate of the times was heightened when Seligman was writing about the need for progressive taxation. Just when Adams's brush with the Cornell alumni seemed to be receding into the past, other academic economists, including those who pushed for progressive taxes, were coming under increased scrutiny by the administrators and alumni of their institutions. Ely, who by 1894 was teaching at Wisconsin, endured a public trial of his ideas, before he was eventually exonerated. Amid this environment, it was incumbent upon Seligman and other supporters of progression to create some distance between their ideas and the conventional impressions of socialism.⁸¹

In addition to separating his views from Wagner, Seligman also had to demonstrate that other theories such as Walker's compensatory view of progression were equally inadequate. French writers had made a claim similar to Walker's, that the state had a duty to use progressive taxes to counterbalance or compensate for the inequality of wealth that resulted from "the state's own acts of omission and commission." The compensatory theory, more specifically, held that the state should use progressive taxes to counter the adverse effects of tariffs, wars, currency legislation, and the like. This theory, as Walker himself admitted, and Seligman emphasized, provided "no practical standard" for economic policymaking. According to Seligman, the ideas of Wagner, Walker and the French writers were, in the end, tangential to the real issue behind progressive taxation. The vital tension was between progressive and proportional taxes, and the resolution of this choice turned on "the fundamental tension as to the basis of taxation – the theory of benefits or the theory of ability."⁸²

As we have seen, Seligman was an ardent supporter of the theory of ability, and he used the debate over progressivity as yet another opportunity to demonstrate the theoretical, if not practical, superiority of progressive taxes based on the faculty theory. For Seligman, "the elements of faculty [were] twofold: (1) those connected with acquisition or production (2) those connected with outlay or consumption." On the production side, it seemed rather self-evident that those with large fortunes or incomes had "a decided advantage in augmenting their possessions." In these cases, faculty "may be said to increase faster than fortune or income," suggesting the need for something "more than [a] proportional rate of taxation."⁸³

The analysis from the consumption perspective was a bit more complicated. Here, the faculty or ability to pay theory rested on a version of equal sacrifice, which itself was based on the notion of diminishing marginal utility. Building on the work of European theorists, such as Stanley Jevons, Seligman illustrated how the individual benefits received from the consumption of different items dictated the need for a progressive system of taxation:

Since the intensity of our wants and therefore their final utility decreases as we ascend from the lower or more pressing to the higher or less urgent wants, and since larger incomes supply the means of satisfying these less intense wants, a strictly proportional tax would involve small sacrifices in the case of the larger

⁸¹ Rader, *The Academic Mind and Reform*, Ch. 6; Furner, *Advocacy & Objectivity*, Ch. 7; Ross, "Socialism and American Liberalism," pp. 64-79.

⁸² Seligman, "Theory of Progressive Taxation," pp. 223, 224.

⁸³ *Id.*, pp. 245-6.

incomes. Strict equality of sacrifice in the sense of relatively proportional diminution of burden thus involves progressive taxation.⁸⁴

At the national level, Seligman had long been a strong proponent of a direct progressive income tax as the best method of equitably capturing a citizen/taxpayer's ability-to-pay. Like many of his historically-minded colleagues, Seligman eschewed the general notion that taxation should be based on a *quid pro quo* ideal of "benefits theory" – the notion that the level of taxes paid by a citizen should be based on the benefits conferred upon that citizen by the state. For Seligman and his ilk, benefits theory, like the property tax, was based on an outmoded conception of political economy.

It is now generally agreed that we pay taxes not because the state protects us, or because we get any benefits from the state, but simply because the state is a part of us. The duty of supporting and protecting it is born with us. In a civilized society the state is as necessary to the individual as the air he breathes; unless he reverts to stateless savagery and anarchy he cannot live beyond its confines. His every action is conditioned by the fact of its existence. He does not choose the state, but is born into it; it is interwoven with the very fibers of his being; nay, in the last resort, he gives to it his very life. To say that he supports the state only because it benefits him is a narrow and selfish doctrine. We pay taxes not because we get benefits from the state, but because it is as much our duty to support the state as to support ourselves or our family; because, in short, the state is an integral part of us.⁸⁵

The major paradigm shift that the progressive economists like Seligman initiated was, thus, this move away from benefits theory towards a concept of taxation based on faculty or ability to pay.

A Self-Reflexive Historicism

Seligman augmented his support for the ability to pay argument by applying a historicist analysis to the global development of the income tax. In one of his best-known treatises, which was published in several editions and translated into numerous languages, Seligman set out to demonstrate that a progressive income tax was the historically appropriate form of taxation for a modern urban industrial nation. Seligman had already attempted unsuccessfully to influence the constitutional case that struck down the federal income tax in 1895. After that experience, he set out to write his treatise on the income tax with the aim of insuring that his ideas would not be ignored.⁸⁶

⁸⁴ Id., p. 239.

⁸⁵ Seligman, *Essays in Taxation* (New York: MacMillan Co, 1895), p. pp. 70, 72. Seligman was one of the few academic political economists, after Francis Walker, who carefully and extensively analyzed George's writings. In fact, Charles Bullock, the Harvard economist confided to Seligman that "in opposition to the single tax, I should not know what to reprint for students of finance, if your discussion was not available." Bullock to Seligman, June 2, 1905, Cataloged Correspondence, ERASP.

⁸⁶ Seligman, Edwin R.A. *The Income Tax: A Study of the History, Theory, and Practice of Income Taxation at Home and Abroad* (New York: The MacMillan Company, 1911).

Applying his historical perspective on political economy to the issue, Seligman argued in his treatise that theories of taxation had evolved over the centuries to meet the changing functional needs of society. What remained constant during this historical evolution was the criterion used by the state to determine the basis of taxation. Seligman identified this criterion as the well-known “principle of faculty or ability to pay,” and he tied this principle to an on-going search for social justice. “Amid the clashing of divergent interests and the endeavor of each social class, we discern the slow and laborious growth of standards of justice in taxation, and the attempt on the part of the community as a whole to realize this justice,” Seligman proclaimed. “The history of finance, in other words, shows the evolution of the principle of faculty or ability to pay – the principle that each individual should be held to help the state in proportion to his ability to help himself.”⁸⁷

According to Seligman, the criterion of faculty had undergone several manifestations from its origins in preliterate society to modern times. Using an evolutionary theory of historical change, Seligman illustrated how different types of taxes embodied the “ability to pay” metric. More specifically, Seligman set out five stages in the historical development of Western taxation, with the income tax as the fifth, and perhaps final, stage of fiscal evolution.

Seligman, however, went to great pains to emphasize in his treatise that the income tax should not be viewed as the only accurate measure of “ability to pay.” The income tax, for him, was not without its faults. It left unanswered many thorny questions, such as what constituted income, could all sources of income be treated equally, and the all-important issue of “whether different amounts of income present identically the same criteria of ability to pay.”⁸⁸ In addition to these substantive questions, the income tax also posed a whole host of administrative concerns, not the least of which was whether it could be executed without being overly intrusive. This administrative challenge in time would become Seligman’s strongest claim against state-level taxation. In the end, Seligman admitted that, although a tax based on income was perhaps the final stage of fiscal evolution, a system of taxation that accurately gauged an individual’s faculty or ability to pay would remain an ideal beyond the reach of practical politics.

Seligman’s theory of fiscal evolution was, therefore, not a teleological one with the income tax as some sort of whiggish culmination of progress. Seligman recognized that the income tax by itself was no panacea for the complexities of a modern, industrial society. Pinning all his hopes on the income tax would only make him as “unscientific” and unsophisticated as Henry George. Instead, he saw the income tax as a vital component in a larger matrix of economic and social justice – a component that remained tied to Seligman’s criteria of “ability to pay.” Seligman acknowledged the idealistic aspects of his theory when he wrote: “While the system of taxation should endeavor, roughly at all events, to adjust itself to income in general, the income tax as such can form only a part, even though it may be a permanent part, of the system, the other elements of which must be based upon the remaining criteria of faculty in order to reach as close an approximation to justice as may be possible.”⁸⁹

Writing at a time when the future fate of the American income tax was still unclear, Seligman did not lose sight of his historical methods. The income tax had come into its own as the necessary policy for an industrialized nation. But that did not mean that an income tax was or should be sacrosanct. For Seligman to give it such timeless, transhistorical prominence would be to betray his own historicism. Instead, because the income tax corresponded with the level of

⁸⁷ Id., p. 4.

⁸⁸ Id., p. 16.

⁸⁹ Id., p. 18.

political and economic development that existed in early twentieth century America, Seligman became a vocal advocate for the implementation of a permanent federal income tax. Yet he recognized that conditions elsewhere and at other times might dictate other forms of fiscal policies. His academic publications as well as his writings for the popular press at the time focused on how a federal income tax was the historically and socially appropriate form of taxation for a modern society.

In facilitating this shift from benefits theory to the ability to pay, Seligman did not limit his advocacy for the income tax to his writing. He also played a significant role in New York State's ratification of the Sixteenth amendment, as well as an important part in bringing the state-level income tax to New York.⁹⁰ But Seligman's most lasting legacy was within the fragile yet essential arena of ideas where his historicist theories of taxation were passed on to the next generation of tax scholars.

Conclusion

All throughout their efforts and achievements, the reform-minded public finance economists were concerned, first and foremost, about the equitable distribution of tax burdens, with what Seligman referred to as rounding "out the existing tax system in the direction of greater justice."⁹¹ Through their scholarship, teaching and public lectures, these Progressive-Era economists guided a paradigm shift in the theories that undergirded American taxation – a paradigm shift away from benefits theory towards the principle of faculty or the "ability to pay."

In so doing, they helped inject a sense of redistributive reasoning into the prevailing fiscal order. Though they did not go as far as some of their German mentors in advancing radically redistributive, progressive taxes, they did bring a vigorous defense of justice and equity to an otherwise anemic American dialogue about taxation. In their unyielding support for tax reforms, they demonstrated that historical, political, social and economic contexts all dictated that the American system of fiscal governance required a permanent progressive income tax. In this way, these political economists who pushed for the direct and progressive taxation of income became the visionaries or architects of the modern American fiscal state – they drew the blueprints from which a new more equitable fiscal polity could be built.

⁹⁰ John D. Buenker, *The Income Tax and the Progressive Era* (New York: Garland Publishing, 1985).
and R. Rudy Higgins-Evenson *The Price of Progress: Public Services, Taxation, and the American Corporate State, 1877-1929* (Baltimore: Johns Hopkins University Press, 2003).

⁹¹ Seligman, "The Income Tax," *PSQ* 9:4 (Dec. 1894), p. 610.