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Panel 2: Tax Reform: Purpose and Policy

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P R O C E E D I N G S

MR. MURRAY: Can we get started? My name is Alan Murray and I am having a hard time figuring out exactly what my role is on this distinguished panel. I know all these people and I that none of them needed to be prodded to speak. And I also know that most of them are very good at ignoring the questions I ask and answering whatever question they choose to answer. And furthermore, Jason Furman told me what questions to ask to that they can then ignore them and answer the questions that they choose to answer.

(Laughter)

MR. MURRAY: But I was asked to say a few words to set a little historical perspective here about the 1986 Tax Reform Act which was my political education in Washington, and I can see from looking out at the audience that there are a number people here who were involved in that. I can also see that there are a few people who probably weren't born in 1986, so I try and gear my comments to both.

It was an extraordinary accomplishment because it managed to marry the desires of the two parties in an unusual way. At the time, the Republicans were completely focused on lowering the top marginal tax rate which come to think of it they still are 20 years later, and the Democrats were very focused on the sort of burgeoning tax shelter industry that had grown up particularly after 1981 and the unfairness caused by it where you had sort of severe horizontal equity issues where two people making the same income or two companies making the same income could lay vastly different rates of tax depending on their investments in tax shelters and various other breaks that were available to them. What happened in 1986 was a decision to wipe out a bunch of those tax breaks and use that to bring down marginal tax rates.

But what was most extraordinary about it you could have made an awful lot of money in 1984, 1985, and 1986, by betting that this was going to happen because everybody would have taken the other side of that bet. Nobody thought it could happen because the number of special interests lined up against it were so huge. As a matter of fact, the only reason I was allowed to cover it at the "Wall Street Journal" as a cub reporter because the big guys didn't want to. They said this is a complete waste of time. Those of you who remember watching Ronald Reagan give his State of the Union address in 1984, he brought this up and he said he was asking Don Regan at the Treasury Department to do a study of tax reform and report back to him in December after the election which prompted an audible guffaw from the entire Congress because that signaled to them that this was just a gambit to get it out of the election campaign, there had been rumors that Walter Mondale was going to adopt some sort of tax reform plan, in fact, he never did and never intended to, but that was what drove it.

And you had a similar kind of dynamic that kept it going for 2 years as one player after another tried to make sure that as someone put it at the time the dog didn't die on their doorstep, get it out and let it die at the next step in the process, but it's not going to happen. My favorite story was in Christmas of 1985 the House is debating the bill on the floor, it's very close, looks like it might pass, might fail. Bob Packwood's office was having its Christmas party that night and Senator Packwood who was chairing the Senate Finance Committee didn't go to the party, and this by the way is a man who enjoyed his Christmas parties and became somewhat infamous for that. But that night wouldn't go to the party because he was glued to the television watching the House debate this bill hoping upon hope that they would kill it so he wouldn't have to deal with it. And so it was that kind of negative dynamic that kept it all running and led to this extraordinary bipartisan accomplishment where nobody thought it was going to happen and neither side really wanted it to happen, but they also didn't want to be responsible for killing it.

I don't know how you ever recreate that kind of dynamic again, but before we go on I just would cite two things about 1986 that are very different than today and relevant to the discussion we're about to have. One is a big a mess as the tax code may be, it's not as big a mess as it was in 1986. Rates were much higher, clearly abusive tax breaks and deductions were much larger, so the possibilities for cleaning it up were much greater. Second, Washington in my view is not nearly as good a place, as productive a place as it was in 1986. One of the extraordinary things about 1986, you had great partisanship. You had Ronald

Reagan over here, you had Dan Rostenkowski over here as far apart as anybody on the scene today in terms of their politics. But you had a professional tax staff on both sides of the aisle, some of whom who are in this room, who were really not partisan, who were really devoted to trying to figure out how you take these partisan impulses and shape them into something useful and something productive, and talk to each other all the time. In fact, one of the reporting tactics we used in covering the bill was we would talk to the people on the Hill about what the Treasury was doing and talk to the people at the Treasury about what the folks on the Hill were doing because they were talking to each other all the time. I remember watching over the years how that changed to the point where they started calling us to find out what the other was doing because they weren't talking to each other.

I'll finish with this. The greatest example of how different it was is sitting back in the fifth row, Ron Pearlman, who went to being the Assistant Secretary for Tax Policy in the Reagan Administration, to being Dan Rostenkowski's choice to head the Joint Taxation Committee. I would argue that that would be almost impossible if not completely impossible in today's environment and I think that makes the enterprise we're about to talk about here much more difficult assuming one party doesn't sweep the election and have ultimate authority to do what it wants without consulting the other party.

Having said all that, let me turn to Rob Rubin and ask what to me has always been the most difficult question in these conversations. Everybody has a different notion of what they mean by tax reform. Larry gave us his six principles. I would argue those principles are frequently if not always in conflict with each other. Some people want to simplify, some people want to improve economic efficiency, some people want to, to use a Larry Summers phrase which I hope now the statute of limitations on your off-the-record comment has now expired and I can use it, some people want to turn the tax code into a theme park.

(Laughter)

MR. MURRAY: So what I want to ask Bob Rubin is, when you look at this, and of course all the questions of progressivity and inequality, when you look at this what is the one goal, the one goal, that you think is preeminent in thinking about how to fix the tax system?

MR. RUBIN: I think my answer to that, Alan, would be that my one goal would be to achieve multiple purposes.

(Laughter)

MR. MURRAY: Which proves my point.

MR. RUBIN: I'm no tax expert and there are other people who will be much more interesting on taxes than I will be, but let me just tick off --

MR. MURRAY: You've probably paid more than anyone else on this panel.

(Laughter)

MR. RUBIN: That is probably true, and I'm probably treated more unfairly by the tax code than anybody else on this panel. That's another and different set of issues.

I guess, Alan, if it were me and I were back at Treasury which I will not be no matter what happens, and if there were a chance to do tax reform, and I actually think there could be some precipitating event because don't forget the current tax cuts expire in 2010 and that may give you an environment, and you've got this AMT problem which is going to have to be dealt with not just on a year-by-year patch basis, so you do have two forces that could create an environment. Les Samuels who was our assistant secretary said to me the other day that he thought that the kind of discussion we're having now, and this by the way is what Hamilton was set up to do. The Hamilton Project was set up to have exactly these kinds of very serious discussion about important issues on the theory that if you have these discussions, you have a lot of people involved and you're involving the media and they're involved in the substance, that helps create the kind of energy that then can at some point effect what actually happens in our political system. What Les said was we've got to have these kinds of discussions now to create the predicate so that later something can happen.

I guess what I would do, Alan, my number-one priority would be to strengthen progressivity. These recent tax cuts obviously have damaged it, inequality has increased very greatly. I think that's an enormous social and economic harm. I think it's highly disadvantageous both socially and economically that has increased inequality, so greatly progressivity. Along the same lines, I'd go into base broadening probably because it contributes to fairness and to progressivity and probably because you can raise revenue that way. And as Larry said, tax reform may be largely about the internals of the tax code, we are going to need more revenue, so that's another way to try to get it.

I think there is a real issue as Larry pointed out around corporate taxation and focuses a lot on transfer pricing with respect to international activity. Simplification which is probably hard to do because whatever you do as Les used to tell me you have losers as well as winners, but nevertheless, if nothing else, you can try to bring different programs together, as say in our paper, that serve the same purpose and try to get a simpler view of them. And one more, when the IRS Reform Bill was done, I was still Secretary. There clearly were problems that needed to be addressed. And I think it is equally clear, and I felt that way at the time and we did everything to try to mitigate this, that the bill went too far in terms of inhibiting or limiting or constraining enforcement. And I think we need much improved enforcement, and as Larry said in his remarks, it needs to be aimed at the people with respect to whom he can do the most good which is the high-bracket taxpayers and corporations.

MR. MURRAY: Thank you. Since I seem to have had limited success in getting you to --

MR. RUBIN: My one purpose would be those multiple purposes.

MR. MURRAY: But the point on progressivity is interesting because of course in 1986 progressivity was put off the table from day one. The goal was to not change the distribution of the tax burden.

Let me try and get Larry to answer the same question. If you accept that there are all kinds of conflicts in your six principles, is there one of them that you think you would hold above all others? And is it the rising inequality and progressivity goal or is it something else?

MR. SUMMERS: Again I have to maximize many things and functions with many variables.

MR. MURRAY: The equation has to be solvable.

MR. SUMMERS: Progressive full funding of an adequately strong government has to be the top priority and that means that the two imperatives of 1986 are both wrong in thinking about tax reform today. Distributional neutrality is wrong. A lot of the objective is correcting the inequities of what's taken place in the last 5 years. And it is a little complicated to know what you mean by revenue neutrality, whether you mean revenue neutrality to the 2010 tax code or whether you mean revenue neutrality to the tax code after the cuts are all taken off. But certainly if revenue neutrality is taken to mean revenue neutrality to the

Bush tax cuts when they're phased in, that is surely an inappropriate standard as well because that clearly leaves the country with an inadequate amount of revenue. So I think it's really a quite different context and indeed the reason in my earlier remarks that I distinguished between the internal imperatives of the tax system and the external imperatives to the economy was in a way when you take off the question of overall distribution and you take off the question of overall revenue, what you're left with is improving the internal imperatives of the tax code. When you put those two questions back as central, inevitably they become very large relative to the internal imperatives to the tax code.

MR. MURRAY: Please jump in, Bill. You've just heard a kind of consensus here of the Summers-Rubin axis, and anyone who wants to challenge that consensus should jump in at this time. I'm not sure Bill is going to do that, but I'll let you go first.

MR. GALE: I want to give a slightly different answer or a slightly different question but still only come back with one thing, and that is if you want progressivity or anything else, how do you get it. The key to all of this is a coherent and comprehensive tax base. Once you've got that, you can make the system progressive because it's harder to avoid the tax. You can raise the revenue that you need with relatively low rates for the same reason. You can enact intelligent social policy because you've cleaned out all the junk in the social policy in the base. You can simplify the tax system because you're taxing everything rather than having a series of exemptions. And you reduce avoidance and evasion. Regardless of the one goal that anyone thinks is important, the one operative thing that needs to be done is to make the base comprehensive and coherent.

MR. MURRAY: Bill, I have a hard time understanding the difference between what you call the junk and what you call intelligent social policy because if you're going to use the tax code to deal with our health care problems, to deal with our environmental problems, to deal with our energy problems, to encourage homeownership, before you get very far down the road you're back to Larry Summers's theme park.

MR. GALE: There is a different. No doubt there is potential for a theme park, but there are also much more intelligent, less costly, more efficient, more equitable ways to subsidize health care or housing or whatever we want to do than the way we actually do it in the current tax code.

So, yes, the current social policy in the tax code is a mess, but that does mean that social policy in the tax code has to be a mess. Jason has written about this a lot.

MR. MURRAY: Let me ask you one quick question before we go to the comments over here. In revenue terms, what is the biggest hole in the base, or the one or two biggest holes in the base that you see right now?

MR. GALE: I'm not sure I can pick one. It's sort of like death by a thousand pinpricks.

MR. MURRAY: But many of them are tiny.

MR. GALE: But there are a lot of big ones. There's health, there's mortgages, there's the way we treat savings, there's tax exempt. You can go on down the list.

MR. MURRAY: So you would spend less revenue on health, mortgage, savings? I'm not talking about rationalizing the way you do it. I'm talking about less revenue, narrowing the base, or broadening the base.

MR. GALE: I think you could do that. I think more importantly you could restructure the way we subsidize those activities. For example, with housing we don't subsidize homeownership, we subsidize the debt that people acquire when they buy homes. That's a ridiculous policy. Subsidizing homeownership would be when somebody buys their first house they get a subsidy. You can make that subsidy very progressive by limiting it, by saying a $10,000 tax credit, end of story. I understand there are political issues here, but the idea is that is a perfectly --

MR. MURRAY: Your timing in going after housing right now is particularly propitious.

MR. GALE: Le's pick health care.

MR. MURRAY: Perhaps subprime housing would be a particular area.

MR. GALE: Let's take health care. The president's proposal, the tax subsidy for health care, a fixed amount for the purchase of health insurance is the analog of the housing situation I just gave. It's a much more efficient, equitable, could be less costly approach to subsidizing health care and more effective in getting people in health insurance than the current system.

MR. MURRAY: Efficient and equitable, but is it less costly? It's not clear to me.

MR. GALE: I say it could be. You don't have to set the limit.

MR. MURRAY: Does somebody want to challenge the notion that the preeminent goal here is more progressivity in the tax system?

MR. DESAI: Sure, I'll try, which is I think this emphasis on inequality is a little puzzling and could be dangerous I think for three reasons. First, the politics of this are complicated. My understanding of the polls and people who have done research on this is that the United States is exceptional in its distaste for redistributional policies. It always has been and it's something that's there in the data and it's hard to rebut. So people will say I want a fair tax system, but what seems to be being talked about is I want a tax system that's going to rectify unfairness somewhere else, and that is a very different statement.

I think a winning ticket is a fair tax system. Rectifying other unfairnesses is a very different thing to me.

The second reason I get a little puzzled by it is part of what is being suggested is beating up on capital by changing capital tax rates or corporate tax rates. The available theory on this and the available empirical evidence on this is when you do that, part of that gets borne, maybe a whole bunch of it gets borne, by labor. And I think in some sense people get that, noneconomists can get that idea. If that's the case then beating up on capital is not necessarily going to have the effects that we think.

The final reason I'm puzzled by it is because I guess the strategies that were employed during the Clinton Administration were taxes increases were justified on a message of optimism and growth which is a very different way to sell a set of tax increases as opposed to selling a set of tax increases as we got to go after some other social goal.

MR. MURRAY: Let's take them one at a time. Take the three points one at a time. I want to have Bob do the danger of trying to rectify inequalities which are much greater than the tax system can deal, and then I want Larry to deal with capital taxation because if my memory serves me correctly, some of the empirical research you're talking about might have been done by an economist by the name of Lawrence Summers.

MR. RUBIN: Let Larry go first. Go ahead. I am a slightly different interpretation I guess of 1993.

MR. SUMMERS: I'm sure yours is better than mine.

MR. RUBIN: No, not necessarily. These are things reasonable people can disagree upon. It doesn't mean they're both right.

(Laughter)

MR. RUBIN: President Clinton was very consumed and rightly so in 1993 with the fact that in the 1980s we'd had pretty good growth until for a whole host of reasons including in my judgment most importantly fiscal matters and this thing came apart in the third, no, the fourth quarter I guess of 1989. But he was very focused on the fact that during the 1980s even though you had had growth and middle-class incomes had lagged and he was very focused on restoring fiscal discipline but doing it in a way that reflected the fact that there had been this increase in inequality and that middle-income people had not fared as well as everybody else, and that's why what we did was to increase the income tax rates on the top 1.2 percent. There is no question that that focus which I think was totally right and is right today on trying to redress what had happened in the natural economy was part of our thinking. Of course when we did it, everybody, not everybody, there were a number of critics who said that it was going to lead to the end of the world, recession and one thing and another, instead we had the longest economic expansion in the country's history, so it's hard to argue that it did economic harm. Maybe that's the response to that if that's what you wanted.

MR. SUMMERS: I think you raise fair questions. With respect to the question about quality, you're certainly right that it appears that when sociologists study ethical attitudes toward equality there are some differences between the United States and Europe. I never thought I would pushed to the point of challenging Bob McIntyre, but I don't think that there is any constituency in America for the concept that dozens of corporations should pay less in taxes than the people who clean their floors. When you pay negative or collect revenues, that's what you're doing. So I think we're at a point as your work on the tax gap between book income and profits illustrates where you really have something that's very different than what's going on.

When I was in graduate school there was a term economists used for things that people believe that are more or less true which is stylized fact. One of the stylized facts when I was in graduate school in the late 1970s was that the income distribution remains relatively constant and that what you have to do is grow the economy faster therefore if you want to make things better for middle-income people. That stylized fact and the correlated stylized fact that productivity and average wages move together have been blown apart over the last 20 years and that's why the prevailing opinions about what should be done have changed.

I am worried about the question you raised which is there is a certain amount of analytic support that can be given for what might be called the trickle-down theory of tax incidence, that if you really hammer capital too hard, since capital can easily move, it all does move, and so it gets the same return it did before and all you're left with is the workers have fewer machines to work with and therefore they're less productive and get lower wages and so taxes on profits are really taxes on workers which is essentially the argument you're making. I think it's a fair question. I think what is missed in the vast majority of the modeling that's done around these issues is the very substantial part of profits that in one way or another represents rents that firms have achieved in some way that are relatively fixed and therefore they and their shareholders are the beneficiaries of those taxes.

And I would make the point from a political economy point of view that it's possible that all those corporations who resist measures that would raise their taxes are really not acting in their own interests because they don't understand economic theory and that it's not going to cost them anything because it will ultimately be pushed onto their workers. That is a possibility but I'm inclined to give more weight to the possibility that they have correctly calculated their interests and that the taxes are for a variety of reasons much more heavily borne by corporations.

MR. MURRAY: Let's stick with that for a minute because we have a current issue of taxation that's very hot and these are these poor gentlemen in the back who have been standing there for 2 hours hoping to get some sort of a video clip that they actually use on their cable news channels. So let's take a stab at giving them that.

SPEAKER: Over to Bob.

MR. MURRAY: No, I'm going to start with John. I'm going to make John go first. There is this issue right now that gets right at the heart of what we've just been talking about, about the conflict between capital taxation and progressivity of the tax system, and that is how do you tax the carried interests that private equity partners --

MR. FURMAN: Alan, can you just clarify, I did not ask you to ask this question.

MR. MURRAY: I'm actually pretty good at not asking the questions that you asked me to ask. In the name of encouraging investment we tax capital gains at a lower rate than we do income. We have a 15-percent capital gains tax. Private equity firms earn most of their income as capital gains. It was in the paper this morning I believe that Stephen Schwarzman made $395 million last year. Do I have that right? And that's going to be I presume primarily taxed at a 15 percent tax rate while somebody making $50- or $60,000 a year will pay a significantly higher rate. Jon Talisman, tell us why that makes sense.

(Laughter)

MR. RUBIN: Aren't you glad you came, Jon?

MR. TALISMAN: I think you've raised an interesting question, and let me first of all disclose that actually I have client interests on this matter so I want full disclosure that I do have client interests.

MR. MURRAY: Do you want to disclose which side of the matter they're on or is that obvious by now?

MR. TALISMAN: Probably that's fairly obvious. Most people don't pay for me to argue for them to raise their taxes. But that being said, I do think --

MR. FURMAN: I’ve been known to do it pro bono.

MR. TALISMAN: That's that? Oh yeah. I do think that this raises interesting policy questions that frankly I think are very difficult to parse. I think that the notion of the taxation of carried interest is frankly dependent on two features of our system which is, one, if you're going to provide a favorable rate, preferential rate for capital gains to encourage entrepreneurial activity, I do think that carried interests are consistent with that. I do think that what they're doing is very similar to what other entrepreneurs are doing in taking either new ventures or existing businesses and turning them around and making them work better. So from a capital standpoint I think it's consistent with once you have a preferential rate for capital gains, it's consistent with that.

It's also tied into the fundamental notion of partnership taxation which is the only reason a carried interest gets capital gains treatment is because of the flow-through nature of partnerships and if the enterprise is investing in something that is capital in nature and holds it for a long-term basis, then what they get is capital treatment. If they are investing in something that is ordinary or held for a short-term basis, then the carried interest gets ordinary treatment.

Let me throw out this example because I think it sort illuminates the discussion. If a sole proprietor borrows money on a nonrecourse basis and puts in a very limited amount of capital but because of his expertise is able to take that venture and build a clientele around that venture, then when he sells the venture even though he did not contribute the bulk of the capital, the bulk of the capital is contributed through nonrecourse debt, he gets capital gains treatment and I think it is very hard to parse that principle and the principle of carried --

MR. MURRAY: There is definitely merit to that answer, on a sound bite basis when you have to stand up there with Andy Stern and he says why should Stephen Schwarzman only have to pay 15 percent of his income in taxes, what do you say? How do you sell that to the public?

MR. TALISMAN: Again, I am not a proponent of capital gains differentials so you'd better ask someone else who is.

MR. MURRAY: I happen to know that the Summers-Rubin axis is not in complete alignment on this issue. Which of you wants to go first?

MR. RUBIN: Larry does.

MR. SUMMERS: I think Summers and Rubin prefer to think of themselves as the alliance, the allies rather than the axis. Though there are no doubt some in Washington and at Harvard who would prefer the term axis to refer to the two of us.

(Laughter)

MR. SUMMERS: I think the right view on this is that there are surely some abuses that are involved with stuff that gets capital gains taxation that no one would want to defend, that beyond that there are very difficult questions of line drawing if you're going to have a capital gains treatment and you're going to have partnership structures in how the tax law should be written and designed if you're going to have fairness, and I'm not enough of an expert to know just where those lines should be drawn.

MR. MURRAY: Bob?

MR. RUBIN: Alan, of all the people in the panel, I'm the one who knows least about taxes and I certainly do not have a definitive view, but I have a slightly different cast on this than Larry may have. I think, Jon, and I've thought about your example, I think that you can think of a lot of examples and try to distinguish one thing from another thing and it does get complicated but I don't think that should be what drives the answer to this question. I think this should be very seriously considered, it seems to me that what is fundamentally happening is, and again I don't have a definitive view, I am not an expert in this, I haven't even given it a lot of thought, frankly, but it seems to me that what is happening is that people who run a large fund are basically performing a service and the service is running the capital and as a consequence they get paid a fee in the form of a performance fee. You can characterize it as a performance fee, you can characterize it as a carried interest, you can characterize it any way you want, but basically I think what they're doing is getting paid a fee for running other people's money and if that is essentially what's happening, while you can certainly create all kinds of analogies that are complicated and if I were arguing against this I think I would try to develop a lot of complicated analogies and use that as my way of trying to prevent something from happening, I think at the core there is a very good argument to be made for treating this as ordinary income.

If somebody works for a very large public financial institution and they take a pool of capital and they invest it in stuff and after 5 years they have a little formula deal so they get paid based on what happens to that stuff, I believe it would be treated as ordinary income and rightly so because that's what they're getting paid to do. As I say, I do not have a definitive view.

MR. MURRAY: How about Jon's suggestion of just abolishing the capital gains differential, which by the way happened in 1986?

MR. RUBIN: Again, if I were arguing against that I'd say the same thing Jon did because that's not politically possible. When I was in the administration I was against cutting the capital gains tax. I have lived around capital markets for some number of decades, I actually know something about them. I don't think that cutting the capital gains tax contributed one iota to our economy. There is nothing that I have seen anywhere in my entire experience of some decades that suggests to me it increased our savings rate by one iota or increased our investment rate by one iota, and I am told that there's a lot of academic research that would tend to support that, but leaving the academic research aside, that's my experience. So I obviously would not have the preferential tax cuts we have had today. But independently of that, I think this is a problem that you can address independently of that. I want to say once again that I'm not a tax expert. I am not saying definitely that that's where it should come out. But I am saying I think this is worth very serious consideration by the kinds of people who are engaged in these activities which are the tax writing committees.

MR. MURRAY: Mark, you wanted to say something on this?

MR. PRATER: Yes, thank you. I think that it's pretty much as Secretary Rubin was saying that you could see some of these things that are definitely abusive looking in character that look a lot like compensation. It's pretty easy to see some cases where there really isn't much capital in play, there isn't much time, much risk, well, there's a lot of risk, I'll pull back from that, but it doesn't look like capital, it doesn't like a capital transaction.

How do you write a rule that captures that notion? We have analogues, we have rules that deal with broker dealers and mark to market and notions in the securities laws and securities taxation that are well settled, but this is kind of a new animal, it's a new animal in a lot of ways, and there is a lot of impact on the markets that we would have to worry about. We have to get this right. So for that reason I'm not going to tell you exactly where we come down on it.

MR. MURRAY: But it underscores the thing that always gets lost in these conversations after they've been going on for about 15 minutes or so is simplicity. As soon as you get 5 minutes into the conversation, simplicity is gone.

MR. PRATER: And Alan, there are a lot of different features to private equity and hedge fund issues that we've discovered in our examination. You've got entity issues. Jon talked about partnership questions. You've got foreign versus domestic issues. You've got the basic how do you treat the carry issue, both pieces of the carry, and all of those things require a lot of adult research and activity. Some things are easier to identify, a more limited universe than others, but it is something that we always struggle with in the policy area because markets evolve, business practices evolve, things get more complicated, and legislative and administrative machinery has to catch up to it.

MR. MURRAY: So what do you think is going to happen?

MR. PRATER: I think we'll continue to look at it. I think you may see some piecemeal responses to these different issues. It's not just one issue. There are a lot of different subissues and related issues that are involved. And I think I would agree with Jon too that the distinction between capital and ordinary is a political question right now that I think is there. As Secretary Rubin and Secretary Summers said, we're going to be visiting all of this stuff in 2011.

MR. MURRAY: But these people don't want to know that you're going to be visiting it. They want to know what you're going to do about it.

MR. PRATER: I will say that you got to be careful about this. We do not want to make a preliminary call one way or the other.

MR. MURRAY: Will anything happen before the next election, anything substantial?

MR. PRATER: Like I said, Alan, I think you'll definitely see features or prices of the issue addressed. I can't tell you exactly when, and I don't want to get out in front of my bosses and other people. But we are taking it very seriously. I'll tell you that.

MR. SUMMERS: I don't have any political prophesy on this. In the 20th century people decided that matter and energy were really manifestations of the same thing. At a somewhat less fundamental level, debt and equity, they're both like parts of what comes out of capital income and in the same way there is no air-tight distinction between what's returned to labor and what's returned to capital. So it seems to me anybody who tries to treat this theologically by saying this really is a capital gain and this really is ordinary income is engaged in a somewhat false exercise just as how do you classify a bond that has an interest rate that varies with the relative performance of a company's stock? Is it a bond? Is it a stock? Who the hell knows.

So it's almost certainly the case that emphasis on simplicity is a passport to abuse, and the people who engage in these transactions are not without sophistication so it would be a mistake to view these issues through the prism of maximizing simplicity. What you have to do give the distinctions we've chosen to use is to find the right kind of balance to strike and my guess is that the right kind of balance is not captured by a slogan on this subject. There certainly is some abuse that absolutely should be corrected, but I don't think that anybody is likely after thinking hard about it to decide that all profit-sharing arrangements should be treated as ordinary income and how you find the right rule is why we have a Congress.

MR. MURRAY: Pam, let me go to you, but I hope in your comment you'll get back to the original question which is what is the preeminent goal of a tax reform effort.

MS. OLSON: So you can I can set aside the others? I was going to say that one thing you could do if you're concerned about this flowing through at 15 percent rates is to go back to the President's dividend exclusion proposal to throw some real complexity on the table because if you went back to the President's dividend exclusion proposal what you would find in these situations is that what passes through at a 15 percent rate is only that which has already been taxed at the corporate level in which the funds have invested. So if it hasn't been taxed once already, it gets taxed at the higher rate at the level of the owners. So that would be one way to address that issue and it would have been a better way I think for us to go in 2003 but for the fact that there were a lot of concerns about the complexity. But obviously just a 15 percent rate on dividends and capital gains is not a very good substitute for ensuring that you've got income taxed once and only once.

In terms of looking at the goals for tax reform, I guess one of the things I just wanted to visit for a minute is the question of whether the elimination of income inequality, which certainly the growing income inequality concerns me a lot, should be an end in itself, or whether what we ought to be focusing on is whether we have created an economy in which the lowest earners are constantly doing better. I think if we look for example at the situation in Europe where there is less income inequality, we also have the people at the bottom doing much worse than the people at the bottom in the U.S. So I don't think that it makes sense to focus on sort of laser like fashion on eliminating income inequality.

I also question the connection between higher tax rates and lower income inequality because, I know we've got the statistics of what's happened between 1960 and 2007, but in 1960 I think we had 91 percent rates which I suspect we're not going back to, but if we look for example at a U.S. economy and where the concentration is of income inequality what we find is that it's on the coasts in particular in California and New York where tax rates are highest when you add in the state rates. So I'm not sure that there is necessarily a relationship between higher tax rates and less income inequality.

In terms of one of the things that it seems to me we ought to be looking at, on the corporate side I think we ought to be looking at Mihir's idea of some book tax conformity or at least eliminating some of the differences between book and tax reporting. I think that we ought to go back and take another look at the President's dividend exclusion proposal complicated as it was because it is a way of addressing a lot of the shelters. It also goes a long ways to eliminating the disparities in different kinds of entities and different kinds of instruments in terms of how we tax them. I think we ought to take a serious look at worldwide taxation. I wouldn't as the last panel discussed go in the direction of formulary apportionment, but it seems to me we could look at worldwide without deferral with a fully functioning foreign tax credit system and much lower rates as a way of both collecting more revenue and establishing a more rational basis.

On the individual side, I do think we need to spend some time reforming the individual income tax and I think we asked the IRS to administer too much in the way of public policy and they really don't do a very good job of administering energy policy or environmental policy or for that matter education policy, health policy, and so I think we ought to look at reform and deciding whether or not we really want the IRS in there. If we do want the IRS in there, then maybe we ought to look at having two IRSes, one that collects revenue and one that hands out benefits because maybe the one handing out benefits could do a better job of it.

And we ought to look as I think the Hamilton Project has suggested in a couple of places at converting a number of individual income tax features from deductions to credits and credits perhaps at a 15 percent rate. This is one of the things that was proposed by the tax reform panel with respect to home mortgage and I think it's something that really deserves more look. We ought to look at it on the education front and health care front. I think the President's health care proposal does go a long ways to eliminating the disparities that the current system creates in the health care area but it doesn't reach down into the lowest income and we really need to think about a refundable tax credit if you're going to accomplish that.

Then the last thing I'm going to mention is reforming Social Security. Right now we have a system that is very progressive if we assume that benefits will be paid, and I think that's probably a questionable assumption at this point. The reality is that we have a pay-as-you-go system and we're looking to the lowest income and moderate income in this country to fund that. So let's recognize the fact that we have a pay-as-you-go system and look for another revenue source to pay it and then let's individuals set that amount of money aside that's currently going into Social Security to fund savings and to begin to build assets.

MR. MURRAY: I want to get back to the revenue point in just a minute, but before we do, Pam doesn't like the theme park. She doesn't like the theme part at all. That's the source of a lot of the complication and a fair amount of the unfairness in the tax code. Do you want to respond to that, because you made a case for smart social policy being done through the tax code.

MR. SUMMERS: I promise you as one who was involved in supervising rules and writing in both of these areas that any complexity associated with the HOPE Scholarship is as nothing compared to the complexity associated with the rules on debt and equity, the rules on capital gains, or the rules on anything else. So I find the spectacle of those who are speaking heavily on behalf of the most fortunate attacking complexity in the code by turning to the credits that are oriented to middle-class families to be a surprising one.

MS. OLSON: Not that I suggested support for them, not attacking them, and that those who have the capital gains probably already have the college educations while those who need the education credits are trying to get one.

MR. SUMMERS: Pam is arguing for simplification of capital taxation as well.

MS. OLSON: Yes. That may be more complex.

MR. SUMMERS: I'm not sure how your two comments fit together. What Jason and I defended in our paper was properly structured use of the tax system to support families of middle-income doing things that were crucial in their lives like preparing for retirement, taking care of an aging relative, sending a child to college. At a certain point justice as on the expenditure side that kind of thing can get ridiculous. I think my use of the term theme park came in response to a suggestion that there be a walking shoe credit to as to achieve parity with the commuting tax credit and the mass transit tax credit. So at a certain point those too can become ridiculous. But I think it is very important to distinguish between complexity that comes to a minor extent out of the achievement of social objectives the tax code, and complexity that comes out of trying to distinguish the fundamentally indistinguishable in the capital income parts of the code and that the right policy responses to the two of them are very different.

MR. MURRAY: Bob?

MR. RUBIN: Just one comment, Alan. When I was at Treasury it seemed to me that there was an awful lot we do in the code that we shouldn't do, but the problem is a political problem because I think these programs that help middle-income and lower-income people are very important and if you then went to those who want to simplify the tax code and say we don't to do any of those and you say to them okay then support us and we want to have these as spending programs and we want to have them on the spending side of the budget, they of course don't support those. So I think the first question is do you support the purposes and the programs in terms of substantially what they do. I did and would do a lot more of that actually I think, and these are underaddressed problems rather than overaddressed problems.

The second question is how should you do it, and I think it would be preferable in many cases to do it on the expenditure side but the politics of that are impossible and therefore they get done in the tax code as tax expenditures.

MR. MURRAY: Jason, we talked a lot about inequality and we've talked a lot about simplicity, but let's go back to the first of Larry's six principles which is fiscal responsibility which may come to override everything else when this comes to a head in a couple of years. In crude numbers, I think I have this right, correct me if I'm wrong, the federal government collects something like 18 percent of GDP in taxes, spends something like 20 percent of GDP, and is headed toward something like 30 percent of GDP if you look at trends in health care spending, et cetera. So does everything we've been talking about here get overwhelmed by the simple need for revenue to run the huge demands of government on its current course?

MR. FURMAN: First of all, that's not unrelated to the progressivity question because what we care about is not the progressivity of the tax code, but the progressivity of the fiscal system as a whole. So if you dramatically cut taxes and that results in dramatically cutting Medicaid, food stamps and Medicare, you are making the fiscal system as a whole much more regressive than it is today. And then the converse is able true, that if you are able to adequately fund the types of health insurance that we think that you should have, you can make the system more progressive and I also think that's part of the answer to the point Mihir had raised earlier. I don't think you go out and phrase this as Robin Hood stealing from the rich to give to the poor, or maybe you do. I think you phrase it to some degree as providing adequate health insurance for everyone and then paying for that adequate health insurance and that itself is progressive.

To get back to this fiscal question, I think part of the solution will come when everyone understands the basic idea that I think Larry said which is if you're running a deficit, most likely it means you're raising taxes on people in the future, you're not telling people who you're raised them on. So what we have seen in the last several years is not so much of a tax cut, but a tax shift, and shifting taxes to a set of generations and a set of people who don't know whether or not they're going to bear them and who they are and some of whom don't even vote and that's why you've been able to do it politically. I think once you understand that and then understand a corollary of that which is there is a starve the beast theory that, sure, we may have shifted taxes, but at the end of the day we'll end up with lower government spending as a result the theory would go.

My observation of the last 15 years is that if anything the opposite is true, that in the 1990s you had a culture of fiscal discipline and it involved mutual restraint. So you did have higher taxes on the most fortunate, but you also had spending restraint in areas like Medicare as well as room for targeted investments and that you actually saw spending go down and revenues go up. In this decade you've seen that culture fall apart and with the pay go rule not applying to the tax side, it's very hard for people to say it should apply to the spending side. So if anything, we have seen higher spending and lower taxes. So I think we'll come to a solution to this when people understand that working together there is a budget constraint.

MR. MURRAY: But then let's take it up to 10,000 feet from there and say does it matter how large the government is as a percentage of the economy? We've lived at roughly 20 percent spending for a number of decades now. We may be headed to 30 percent. Should we be concerned about that? Has there been a benefit to the U.S. economy that we've been one of the lowest taxed nations in the world or not? Is it okay to head onto the same path that many European nations have?

MR. FURMAN: I think some of that is you don't want to look at the size of government as measured by what the government accountants label government spending and divided that by GDP. You want to look at what the government does to affect our economy in terms of reallocating and redistributing. Dan Shaviro, an NYU law professor, wrote an important paper in which he pointed out that for instance cutting taxes today and raising taxes in the future is many ways an identical form of redistribution to expanding a pay-as-you-go Social Security program. It looks like smaller government but it actually redistributes between generations in a way that is akin to a larger government. Tax expenditures are another example of where the size of government isn't measured by tax revenue.

Going in the other direction, Social Security arguably shouldn't be counted as part of the big government. We pay 12.4 percent of our income in payroll taxes, you get back a bunch of that mathematically in a formula that links to your Social Security benefits, so that tax, actually much of it shouldn't be distortionary.

MR. MURRAY: But there is a very legitimate argument here. The starve the beast theory may not have worked, but there is a legitimate argument here that there needs to be a constraint. There was a lot of research in this area that the bureaucratic imperative of government is to grow and at some point that becomes counterproductive. Bob Rubin and Larry Summers, will one of you jump in on this?

MR. SUMMERS: I'll give you my view. Just because Bill Kristol says something doesn't make it wrong.

(Laughter)

MR. SUMMERS: And says that he doesn't see how you can love your country and hate its government. I don't think the attitude that all government is bad makes any sense. I think all of us should be ashamed that there was a significant period when the richest country on Earth could not afford to buy body armor for people fighting in Iraq. I think it's an act of spectacular national imprudence that we do not have a larger reserve force that is available to respond to a contingency than we have today. So the notion that the central problem of American democracy right now is that the government is too large is I think absurd.

We all talk about the central importance of education and we tell our kids that the most important thing they can do is get an education, but if as is true in many parts of this country today the paint is chipping off the classrooms that they're studying in, how are they supposed to believe that we mean it that it's the most important thing to our society? There is a kind of category of fiction here. If there's a wedge between the amount of money that my employer pays and the amount of money that I get and it is accounted for by a tax, that's called the end of the world, deadweight loss, distortion, big government, and it is seen as a central problem. If on the other hand there is a wedge between the amount my employer pays and the amount that I get that is accounted for by a health insurance premium 20 percent is going for all the people to chase all the other people around trying try to collect the bills, that's called the free market driving capitalism forward. As best as I can tell in terms of labor demand and in terms of labor supply they're the same thing.

So God knows there are a million mistakes Western Europe has made and I certainly wouldn't trade their economic performance for our economic performance in a million years, but to suggest that it would be creeping socialism to allow the level of our government spending to respond to the point where we could buy body armor, where we could have painted classrooms, that we could begin to do something about 47 million people without health insurance I just think is the height of absurdity.

MR. MURRAY: But the difference between 20 percent and 30 percent is not creeping.

MR. SUMMERS: Nobody that I know is anywhere near suggesting anything that approaches a 50 percent increase in the scale of the government and certainly the kind of agenda of which I just spoke is going nowhere in that direction. And you do need to distinguish very sharply between new government functions and expenditures that are being made anyway being run through a system that in some way involves government.

MR. MURRAY: Somebody please quickly jump in here, but we are --

MR. SUMMERS: I didn't mean to be speaking for Secretary Rubin who may have a very different view.

MR. RUBIN: No, I think he has rather colorfully represented what I think.

MR. MURRAY: In terms of the current health programs, we are headed toward 30 percent. It's a demographic decision. I understand you're saying we shouldn't care about that if it's simply routing expenditures that would be made other ways through the government.

MR. RUBIN: Look, Alan, I think Larry's comments and yours together make a point -- which is I think we're at a rather important time in our country's economic history and I think we need a kind of seriousness of purpose in our political system that we too often don't have to address a set of issues that are coming at us and we're basically not addressing them. Larry made the point about public education in much of America. Clearly demographics are driving a very different situation than we've had historically so that if revenues as a percentage of GDP at 18-1/2 percent or something like that has been adequate for the last X number of years, 20 or 30 years, whatever it has been Jason, that isn't going to work anymore to fit the demographics. But it seems to me you've got to have a political process that gets serious about this and makes cost-benefit judgments in terms of what your objectives are for your society about our whole system and makes decisions on what is the government going to do, how are we going to pay for it. It's wonderful to have a dividend exclusion because every economist believes in it, but in place a dividend exclusion with not one nickel to pay for it. We just sort of add it to the deficit. We had a prescription drug benefit, I think that was probably a very good policy not necessarily in every detail, but the idea of it was, we have not one nickel to pay for it and we just said we'll pay for it down the road. And I think we've got to get serious about economic policy in this country and decide what we want to do and how we're going to pay for it and make judgments about what are the effects of the various things that we do in federal government on our economy and on our society and I think it should heavily emphasize the kind of progressivity that we've discussed in a narrower context which was the tax code.

MR. SUMMERS: Can I add something? I agree with that, obviously. Can I just add something because in a way it previews what the next Hamilton event is going to be about? Alan you highlighted the question of health care. I don't think there's any question that with an aging society with health care costs rising 2 to 3 percent a year faster than GNP starting at 16 percent of the economy, go into a third of the economy on current trends, you're in a profoundly difficult situation that requires enormous thought as to how the country is going to move forward. That's the crucial issue. If we get that under proper control and we're also providing decent health care for everybody, we will do well in this space whether the national income accountants put the program under the government or whether the national income accountants put the program not under the government.

If we don't get that under control, we're going to do badly whether it shows up as staggering burdens on individuals and their employers or whether it shows up as something that's in the government account. So I think the crucial question is that we need to view these issues through what they are, what's the future of health and long-term care in an aging society, what's the future of education in a society that needs it more than ever and so forth, not what's the size of the government as the prism through which we view this.

MR. DESAI: Just briefly on this, and maybe this goes back to the conversation that Jason started about how you label all this, but I'm concerned that this conversation is not sufficiently attuned to the language of growth, to use the language that we were talking about before, just growing the pie larger through the tax system. That to me is a message that resonates and I'm concerned that the conversation is more about -- and maybe Jason is just about labeling it, how you frame this when you take it politically, but this conversation is very much about redistribution and unfairness and that could be a winning strategy. But there is a lot to be said for framing this and thinking about this in terms of fairness and making the pie larger. I have been a little bit surprised.

MR. SUMMERS: Let me respond to that. First I guess I've tended to learn over the years that we Harvard professors are better off concentrating on what's best for the economy and leaving the message stuff to others because we're maybe not entirely representative of the population and best at framing messages that will relate to them. So I'm going to stay away from the message stuff.

I mentioned some of the things that were different that were framing the debate right now. One major difference that I'm not going to belabor again is the sort of sea change in inequality and trend toward inequality that we have. The other that's completely different than when I started working on these subjects in some of the work that Alan referred to earlier in the 1980s is with respect to capital costs. In the 1980s when Bob played a central role in advising President Clinton to bring down the deficit as the center of an economic strategy in 1993, the country had high capital costs. Those high capital costs were holding back investment and the tax system was a major tool for reducing capital investment. Today you can say a lot of things about the American economy. The one thing you cannot say out there is that there is a shortage of capital, that there are low capital costs, or that a driving imperative needs to be to reduce the cost of capital. You don't really need to have an idea to raise money nowadays.

(Laughter)

MR. SUMMERS: So part of the reason why in -- tax policy it's not that you're not absolutely right that growth is of central importance, but the principal level through which tax policy is traditionally thought to have impacted on growth is through the whole set of issues around cost of capital and you sort of have to tailor your policy not to some timeless variety but to kind of the world as it is in this period, and the world as it is in this period is a world where inequality is a huge problem and excessive capital costs is a nonproblem and I think that's what's shaping the dimensions of this discussion.

MR. RUBIN: I had just one more thing. Alan Greenspan gave a speech about a year and a half ago, and Alan is not a bleeding heart liberal kind of a -- I think he's a terrific guy, wonderful, and Bernanke said something similar recently, which is that if you're going to have a market-based system and trade liberalization, a predominance of the people have to believe that it's going to work for them. And I think what's happened to the two separate but related issues of median real wages and inequality in the last 5, 6, to 7 years I think we're threatening that belief and I think you'll see it manifest itself first in the trade area, but I think that they were right. These do come together in many ways.

MR. MURRAY: Does anyone else on the panel have an issue they want to bring up before we open it up to the audience?

MR. PRATER : We've talked all about federal stuff here and I think to look at the state numbers, you need to see what's going on with the states, but I think the more transparency about what these numbers mean and the choices as we've talked about here are the better. There are fundamental political calls here. What the proper level of taxation is, what the proper level of growth and spending is. But I think here in D.C. we often ignore with the exception of programs that are tied to federal programs like Medicaid what's going on in the states and I think that that has to be part of the conversation as well.

MR. MURRAY: Anyone else quickly before we open it up?

MR. TALISMAN: Just one thought. Going to Larry's primary goal of progressivity, it strikes me, and I think this whole discussion has been centered on it, that again preserving the income tax and protecting it is in fact making it simpler so that there are fewer objections to it and is actually preserving that progressivity. I think the income tax is I think a goal that needs to be protected in this whole tax reform debate.

MR. MURRAY: Questions? There's one way back there. And please identify yourself first before you ask.

MS. KEMISH: I'm Ruth Kemish, I represent a new coalition called the American Producers Coalition. We are a group of business and labor interests who care about making things in America. Our biggest concern right now is obviously the trade deficit. I see it as being completely unsustainable, and how can we use the tax code to kind of help people who want to make things in America compete on an international level?

I noticed that none of you really spoke about the idea of a consumption tax and the last comment leads right into this with wanting to preserve the tax code. The tax code, we all kind of hate it because we deal with it personally once a year, but how can we change, maybe reduce the corporate income taxes to drastically change that to change our trade deficit?

MR. MURRAY: It's a very good question, and in fairness to Jason that was one of the questions he told me to ask that I didn't ask, about globalization and how the tax system fits into this trend. Which of you wants to take that on?

MR. FURMAN: One part of it is just mechanically that the trade deficit that we have is in effect the amount that we are borrowing from abroad and we are borrowing from abroad in part because the government is running such a large deficit, so anything you can do to bring that deficit under control will bring that trade deficit down.

I'm not sure where you're going with the part of your question, but I think pretty much all economists would agree that shifting from say an income tax base to a consumption tax base or a VAT wouldn't affect our trade balance because exchange rates would just adjust in a way that would lave it in the same place.

MR. MURRAY: But address the broader issue which is we've been talking about a tax system in a vacuum, in a closed economy, and we obviously aren't in a closed economy, we're in a much more open, dynamic economy. How does that affect the way you think about tax reform?

MR. FURMAN: And certainly the papers we released this morning, two of the three papers, were very much motivated by the challenges of taxing income in an increasingly global economy, and Ed didn't have time, but he has a whole international tax reform embedded in his paper as well and I think it's clear that we aren't doing a very good job of taxing international income right now. We have a system that itself is based on an incoherent compromise that was made during the Kennedy Administration that doesn't really have any basis in any underlying economic principle and replacing that with something, and I don't know if it's formulary apportionment or if it's a worldwide system that Ed has or if it's a territorial system that Pam supports, I think a lot of those have a plausible claim of being much better than where we are today which is fundamentally incoherent and broken and increasingly broken as a result of increased globalization.

MR. SUMMERS: I think there are four important ideas around this some of which I think are good and some of which I think are bad. One, if we save more as a country we'll need to borrow less from abroad and that will bring down the trade deficit, and that's why the macroeconomic stuff is imperative. It's probably the most important thing. Second, the dark side of capital mobility and easy capital mobility is avoidance of taxation and avoidance of regulation, and the right response to that is some form of international cooperation that prevents that from happening, and there are lots of different ways that it can happen, but you can't do it the way we are and I think that's a good idea too.

Third, there's a legitimate set of questions, I think it's much more complicated that is often supposed, but there's a legitimate set of questions around neutrality and what neutrality means and whether the tax system is encouraging people to invest in this country or whether the tax system is encouraging to invest outside this country and how those rules are structured, and that's an issue that properly gets attention though I think is very complicated.

Then I think the fourth idea is somehow the tax system should subsidize Americans who are trying to export so that they'll export more and import less, and I think that's mostly a confusion that we will be undone by a variety of kinds of changes and is not a useful prism for viewing the issue.

MR. MURRAY: Pam?

MS. OLSON: I think this raises a very important question, and it's curious that we don't lack of capital, the cost of capital is low, and yet investments are going abroad and I think that's the concern that was articulated. And I think it's something that we ought to be very concerned about because I think it is contributing to the rise in income inequality in this country and I think it's something we ought to be focusing on.

MR. MURRAY: How do you do that?

MS. OLSON: That's a question that I don't have an answer to, but I think to go back to Mihir's comment about growth, and maybe we shouldn't be talking about it, but it does seem to me that what we ought to be looking at is whether the proposals on the table will make us more competitive or whether they'll preserve our competitiveness in a global economy, and some of this may just be the economist's maxim of regression to the mean, that eventually the rest of the world is going to catch up with where we are, but it seems to me that is that perhaps occurring we've got a lot of people at the bottom or the middle who are concerned that they're not going to continue to advance or keep up and that we need to be looking at not putting some Band-Aids on a system that may make us feel better about what our system looks like or what we think it looks like, but that we really need to look at why the income inequality might be growing and whether that reflects contributions to society, that these people are perhaps not making or not being rewarded for, and what we can do to help lift them up so that they are making more greater contributions to society so that they're rewarded for it.

MR. SUMMERS: Let me respond to that, Pam. Yes, we should look at it and, yes, we should try to understand it. I can't resist recording that the single least plausible hypothesis I have ever heard for why inequality increased was the hypothesis you put forward citing New York and California earlier, that places with more progressive taxation got to have more inequality is the single most implausible hypothesis I have ever heard and I come back to it only because of the assertion you made a moment ago that somehow high tax rates and loss of investment from America was somehow a further contribution to inequality.

MS. OLSON: That's not what I suggested.

MR. SUMMERS: Good.

MS. OLSON: I was seconding your comment that the cost of capital is down and yet we're seeing capital investments going somewhere else, and that's --

MR. SUMMERS: This is the hard part of this and this is what I think heavily informed the paper that Jason and I wrote, there is a deep Catch-22 here because on the one hand because of globalization there are fantastic opportunities for the most entrepreneurially able to succeed in ways they never did before and that's an important part of why there's more inequality. And on the other hand, because of globalization, the threat that if you tax me a lot I'll pick up my marbles and I'll move to another country is more real than ever before. And so the same things that are producing the inequality are also making it more difficult to use the tax system do address the inequality and that's why these are serious and difficult problems and that's why the policy proposals that we advocate are really directed at getting it. The same computer technologies that are enabling globalization actually should enable you to do better in collecting taxes from the high income than we used to, not worse than we used to. The same forces approaches to international cooperation enable to cut across that dilemma and benefit not just people here, but people in other jurisdictions as well by forging more internationally cooperative approaches.

So, yes, you are right that you do need to be aware of the prospect of mobility, but I don't think that should be a council of despair with respect to progressivity. I think it should be an argument for being smart about how you pursue progressivity.

MR. MURRAY: Other questions?

MR. SEIDMAN: Larry Seidman from -- one way to get more progressivity without harming savings and investment capital accumulation is to use a progressive consumption tax. You don't have to do it in the dramatic way of replacing the personal income tax or the personal progressive consumption tax, but in a more modest way you could have a progressive consumption surtax as a component to the income tax on the 1040 where individuals say making more than $500,000 had to figure out their personal consumption. The more they saved the less they'd be taxed so that you would get none of the usual conflict, but those who are consuming at a very high level would pay at graduated rates a very high tax. It seems to me you can get both progressivity and more saving and investment if you add that component to our current personal income tax.

MR. MURRAY: Do either of you want to take that on? Bill would be great.

MR. GALE: The taxation of saving is what we have spent much of the morning talking about and especially at the high end it's quite complicated and it's made more complicated in sort of a tax planning purpose for all the reasons that Ed talked about. So it's not right to say that the return to saving at the very top is the marginal tax rate and that that's the marginal disincentive people are facing to begin with.

Having said that, there are lots of ways to think about consumption taxes and they all differ in terms of complexity, equity, efficiency -- scores well on the high progressivity front, if you will, which is often what people mean when they say equity, but it would not be simple I wouldn't think. So rather than starting a whole conversation about consumption taxes at 10 after 12:00, let me just say that it raises all the issues that consumption taxes raise.

MR. MURRAY: One last question? Last comment?

MR. FURMAN: I'll make the last comment which is to thank everyone for coming and tell you that on July 17th the Hamilton Project will be release four different approaches to get to universal health insurance or to near universal health insurance, so I hope you can all come join us for that. Thank you.

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