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Op-Ed Columnist

Things to Tax

By Paul Krugman

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The supercommittee was a superdud — and we should be glad. Nonetheless, at some point we'll have to rein in budget deficits. And when we do, here's a thought: How about making increased revenue an important part of the deal?

And I don't just mean a return to Clinton-era tax rates. Why should 1990s taxes be considered the outer limit of revenue collection? Think about it: The long-run budget outlook has darkened, which means that some hard choices must be made. Why should those choices only involve spending cuts? Why not also push some taxes above their levels in the 1990s?

Let me suggest two areas in which it would make a lot of sense to raise taxes in earnest, not just return them to pre-Bush levels: taxes on very high incomes and taxes on financial transactions.

About those high incomes: In my last column I suggested that the very rich, who have had huge income gains over the last 30 years, should pay more in taxes. I got many responses from readers, with a common theme being that this was silly, that even confiscatory taxes on the wealthy couldn't possibly raise enough money to matter.

Folks, you're living in the past. Once upon a time America was a middle-class nation, in which the super-elite's income was no big deal. But that was another country.

The I.R.S. reports that in 2007, that is, before the economic crisis, the top 0.1 percent of taxpayers — roughly speaking, people with annual incomes over $2 million — had a combined income of more than a trillion dollars. That's a lot of money, and it wouldn't be hard to devise taxes that would raise a significant amount of revenue from those super-high-income individuals

For example, a recent report by the nonpartisan Tax Policy Center points out that before 1980 very-high-income individuals fell into tax brackets well above the 35 percent top rate that applies today. According to the center's analysis, restoring those high-income brackets would have raised $78 billion in 2007, or more than half a percent of G.D.P. I've extrapolated that number using Congressional Budget Office projections, and what I get for the next decade is that high-income taxation could shave more than $1 trillion off the deficit.

It’s instructive to compare that estimate with the savings from the kinds of proposals that are actually circulating in Washington these days. Consider, for example, proposals to raise the age of Medicare eligibility to 67, dealing a major blow to millions of Americans. How much money would that save?

Well, none from the point of view of the nation as a whole, since we would be pushing seniors out of Medicare and into private insurance, which has substantially higher costs. True, it would reduce federal spending — but not by much. The budget office estimates that outlays would fall by only $125 billion over the next decade, as the age increase phased in. And even when fully phased in, this partial dismantling of Medicare would reduce the deficit only about a third as much as could be achieved with higher taxes on the very rich.

So raising taxes on the very rich could make a serious contribution to deficit reduction. Don’t believe anyone who claims otherwise.

And then there’s the idea of taxing financial transactions, which have exploded in recent decades. The economic value of all this trading is dubious at best. In fact, there’s considerable evidence suggesting that too much trading is going on. Still, nobody is proposing a punitive tax. On the table, instead, are proposals like the one recently made by Senator Tom Harkin and Representative Peter DeFazio for a tiny fee on financial transactions.

And here’s the thing: Because there are so many transactions, such a fee could yield several hundred billion dollars in revenue over the next decade. Again, this compares favorably with the savings from many of the harsh spending cuts being proposed in the name of fiscal responsibility.

But wouldn’t such a tax hurt economic growth? As I said, the evidence suggests not — if anything, it suggests that to the extent that taxing financial transactions reduces the volume of wheeling and dealing, that would be a good thing.

And it’s instructive, too, to note that some economies already have financial transactions taxes — and that among those who do are Hong Kong and Singapore. If some conservative starts claiming that such taxes are an unwarranted government intrusion, you might want to ask him why such taxes are imposed by the two countries that score highest on the Heritage Foundation’s Index of Economic Freedom.

Now, the tax ideas I’ve just mentioned wouldn’t be enough, by themselves, to fix our deficit. But the same is true of proposals for spending cuts. The point I’m making here isn’t that taxes are all we need; it is that they could and should be a significant part of the solution.

This article has been revised to reflect the following correction:

Correction: November 28, 2011

An earlier version of this column referred incorrectly to Hong Kong’s political status. It is one of China’s special administrative regions, not an independent country.