A Better Hope for Campaign Finance Reform

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I.   THE PROBLEM, AND A POSSIBLE CURE

Money, money, everywhere, and not a cure in sight.

The American political system, decades into the twenty-first century, seems badly broken. Money lies everywhere at the root of its worst evils. By almost any reasonable account, there is too much money in American politics.[1] The 2016 presidential and congressional election cycle saw an astonishing $6.5 billion in campaign contributions.[2] Looking at individual donors, Sheldon Adelson, the casino magnate from Nevada, gave $82.5 million along with his wife Miriam; the hedge fund manager and environmentalist Tom Steyer topped all donors with $90 million.[3] Things did not stop there; money-in-politics things never seem to stop anywhere. Adelson donated at least $100 million in the 2018 midterm elections,[4] while Steyer has pledged to spend $100 million on his own personal presidential

1.   For the record, David French appears to believe otherwise. *See* David French, *No, There's Not Too Much Money in Politics*, NAT'L REV. (Feb. 26, 2019, 4:33 PM), https://www.nationalreview.com/corner/no-theres-not-too-much-money-in-politics/ [https://perma.cc/FY3V-6FGZ].

2.   Niv M. Sultan, *Election 2016: Trump's Free Media Helped Keep Cost Down, but Fewer Donors Provided More of the Cash*, OPENSECRETS.ORG (Apr. 13, 2017), https://www.opensecrets.org/news/2017/04/election-2016-trump-fewer-donors-provided-more-of-the-cash [https://perma.cc/8TFC-NA5B].

3.   *Id.*

4.   Emily Kopp, *Sheldon Adelson Breaks Spending Record on Midterm Elections, Surpassing $100M*, ROLL CALL (Oct. 22, 2018, 8:59 AM), https://www.rollcall.com/news/politics/sheldon-adelson-breaks-all-time-spending-records-on-the-midterm-elections-surpassing-100-million [https://perma.cc/R8TY-QEPF].

campaign in 2020.[5] Topping them all, Michael Bloomberg, the billionaire former Mayor of New York City, was a late entrant to the Democratic primary, vowing to spend out of his estimated $58 billion personal fortune "whatever it takes to defeat Donald Trump."[6] Before his roughly one hundred days as a candidate were done, Bloomberg had spent a staggering $900 million on the quest.[7]

All of this is what is known and knowable: the rise of "dark money" in American politics has made the identity of many mega-donors and/or the extent of their giving opaque.[8] Given all that cash, it is easy to trace the root of many of our most pressing social and political problems to the outsized role of money in politics.[9] Money in, money out, with no end in sight.

The problem is not new, nor are attempts to solve it. Campaign finance regulation has been an issue in American politics for nearly half a century, following the reforms of the post-Watergate era.[10] It does not appear to be working. Failures and limitations have haunted meaningful efforts to get money out of politics in all branches and at all levels of government. Judicially, *Citizens United v. FEC*,[11] went further than precedents such as

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5.   *See* Alexander Burns, *Tom Steyer Will Run for President and Plans To Spend $100 Million on His Bid*, N.Y. TIMES (July 9, 2019), https://www.nytimes.com/2019/07/09/us/politics/tom-steyer-president.html [https://perma.cc/BM5N-Z6XJ].

6.   Seema Mehta, *What You Need To Know About Michael Bloomberg—The Latest Billionaire Who Wants To Be President*, L.A. TIMES (Nov. 26, 2019, 4:00 AM), https://www.latimes.com/politics/story/2019-11-26/bloomberg-self-funding-2020-presidential-campaign [https://perma.cc/TL9A-C4S3].

7.   Shane Goldmacher, *Michael Bloomberg Spent More Than $900 Million on His Failed Presidential Run*, N.Y. TIMES (Mar. 20, 2020), https://www.nytimes.com/2020/03/20/us/politics/bloomberg-campaign-900-million.html [https://perma.cc/NMP6-CBDJ].

8.   *See, e.g.*, JANE MAYER, DARK MONEY: THE HIDDEN HISTORY OF THE BILLIONAIRES BEHIND THE RISE OF THE RADICAL RIGHT (2016); *see also Dark Money*, OPENSECRETS.ORG https://www.opensecrets.org/dark-money [https://perma.cc/8MDR-9GFS].

9.   This Article does not set out to prove that the large campaign contributions of the wealthy are problematic for democracy but rather builds on a vast literature suggesting that they are. *See, e.g.*, LARRY M. BARTELS, UNEQUAL DEMOCRACY: THE POLITICAL ECONOMY OF THE NEW GILDED AGE (2d ed. 2016); MARTIN GILENS, AFFLUENCE AND INFLUENCE: ECONOMIC INEQUALITY AND POLITICAL POWER IN AMERICA (2012); Edward B. Foley, *Equal-Dollars-Per-Voter: A Constitutional Principle of Campaign Finance*, 94 COLUM. L. REV. 1204 (1994); Joshua L. Kalla & David E. Broockman, *Campaign Contributions Facilitate Access to Congressional Officials: A Randomized Field Experiment*, 60 AM. J. POL. SCI. 545 (2016); Spencer Overton, *But Some Are More Equal: Race, Exclusion and Campaign Finance*, 80 TEX. L. REV. 987 (2002).

10.   Beth Rowen, *Post-Watergate Campaign-Finance Reforms*, INFOPLEASE, https://www.infoplease.com/us/government/elections/post-watergate-campaign-finance-reforms [https://perma.cc/56ES-Y59Z].

11.   558 U.S. 310 (2010).

Buckley v. Valeo,[12] which had held that strict political expenditure limits are unconstitutional and reaffirmed that political speech has First Amendment protections that extend to corporations and other group entities such as labor unions.[13] Legislatively, Congress has so consistently failed to enact meaningful reforms to get money out of politics that leading scholars are beginning to accept the impossibility of ever doing so.[14] The executive branch has played its own role, as by no longer requiring non-profit "social welfare organizations" governed by Internal Revenue Code ("I.R.C.") Section 501(c)(4) to disclose their donors,[15] facilitating the rise of dark money pouring into the metaphorical swamp of federal government politics. Administratively, partisan gridlock has rendered the Federal Election Commission ("FEC"), established in 1975 as the arbiter and enforcer of the post-Watergate campaign finance reforms,[16] virtually impotent.[17]

Hope for getting money out of American politics seems hopeless.

Yet it is always darkest before dawn. It is time, past time, to get out of the conceptual boxes limiting effective campaign finance reform and do something about the outsized role of outsized wealth in American politics. This Article has a plan, as some would say. It begins with the simple idea that

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12. 424 U.S. 1 (1976).

13. For relevant critical commentary on *Citizens United* and the state of campaign finance regulation after it, see generally Richard L. Hasen, *Citizens United and the Illusion of Coherence*, 109 MICH. L. REV. 581 (2011); Michael S. Kang, *The End of Campaign Finance Law*, 98 VA. L. REV. 1 (2012). Note that the thought experiment and tax reform proposal discussed in this Article would not affect corporate political spending in the first instance, although tax-law changes could do so. *See also* Leo E. Strine Jr. & Nicholas Walter, C*onservative Collision Course?: The Tension Between Conservative Corporate Law Theory and* Citizens United, 100 CORNELL L. REV. 335 (2015).

14. *See, e.g.*, Kang, *supra* note 13, at 52–53 (asserting that due to a lack of preventative measures available, "[t]he way forward for campaign finance reform . . . must come from outside campaign finance regulation as we have known it," and concluding that "[c]ampaign finance reform must shift to ex post measures to limit the influence of campaign money once it is already in the system, as opposed to ex ante regulation of money to limit its entry in the first place"). Ironically, while this Article enthusiastically embraces Kang's idea that campaign finance regulation might best come from outside the traditional tools of the sub-discipline, the tax policy proposed is in effect an ex ante measure, aiming to limit the input of private money into politics.

15. Laura Davison & Bill Allison, *Many Political Tax-Exempts No Longer Required To Report Donors*, BLOOMBERG (July 16, 2018, 6:06 PM), https://www.bloomberg.com/news/articles/2018-07-17/many-political-tax-exempts-no-longer-required-to-report-donors [https://perma.cc/D75N-GNXC].

16. *Mission and History*, FED. ELECTION COMMISSION, https://www.fec.gov/about/mission-and-history [https://perma.cc/D2AR-SNYF].

17. For a background on the FEC's failure and interference with real campaign finance reform, see Note, *Eliminating the FEC: The Best Hope for Campaign Finance Regulation?*, 131 HARV. L. REV. 1421 (2018).

political donors are rational. We shall consider throughout the case of a hypothetical mega-donor, whom we call *Sheldon*. When Sheldon spends $100 million in political contributions, he rationally expects benefits back of at least $100 million, the simple premise of rationality being that actors should incur marginal costs less than (or equal to) the expected marginal benefits of any action:

$$[1] \; mc \; \leq \; mb.$$

For small political donors, the benefits of campaign contributions would rationally be expressive;[18] for mega-donors like Sheldon, political contributions increasingly seem transactional, meaning that the contributor expects economic or financial benefits from and commensurate with his expenditures.[19]

This Article is not about the right-hand side of the basic Equation [1]— the marginal benefits to be obtained from outsized contributions—although a wider theory of campaign finance reform should indeed consider why it is that governments can extend such largesse to private actors as to justify $100 million in political contributions. We leave that for another day. Here, we focus instead on the marginal cost or left-hand side of the basic equation. This Article proposes using the tax system to reduce campaign spending by raising the pre-tax costs of political expenditures. This is a standard public finance move: raising the costs of harmful activities by taxing them reduces their occurrence. A ready example is cigarettes, where taxes have proven more effective at reducing the undesired behavior than public education campaigns or warning labels.[20]

It is important to note from the outset, as we shall stress throughout, especially in Section 4, that the tax proposal being advanced is fully general.

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18.   *See, e.g.*, Sanford C. Gordon, Catherine Hafer & Dimitri Landa, *Consumption or Investment? On Motivations for Political Giving*, 69 J. POL. 1057, 1069–70 (2007).

19.   The general problem of "rent seeking" in politics is generally attributed to Gordon Tullock, who considered it paradoxical that the costs of rent seeking are generally low compared to the gains. *See* Gordon Tullock, *Efficient Rent-Seeking*, *in* TOWARD A THEORY OF THE RENT-SEEKING SOCIETY 97 (James M. Buchanan et al. eds., 1980). For applications in the legal literature, see Richard L Doernberg & Fred S. McChesney, *On the Accelerating Rate and Declining Durability of Tax Law Reform*, 71 MINN. L. REV. 913, 932 (1987); Richard L. Doernberg & Fred S. McChesney, *Doing Good or Doing Well? Congress and the Tax Reform Act of 1986*, 62 N.Y.U. L. REV. 891, 897–99 (1987); Edward J. McCaffery & Linda R. Cohen, *Shakedown at Gucci Gulch: The New Logic of Collective Action*, 84 N.C. L. REV. 1159, 1178 n.54 (2006).

20.   *See* Mark Goodchild, Anne-Marie Perucic & Nigar Nargis, *Modelling the Impact of Raising Tobacco Taxes on Public Health and Finance*, 94 BULL. WORLD HEALTH ORG. 250, 255 (2016).

It does not target political contributions specifically.[21] Rather, the proposal is to move the tax system generally and systematically from its current status as a nominal "income" tax to a consistent consumption tax, what we shall come to call a progressive spending tax. This is an idea with a long lineage in the academic literature,[22] supported by people as diverse as the billionaire Bill Gates[23] and the economist and columnist Robert Frank,[24] and actually the basis of a serious legislative proposal put forth on the floor of the United States Congress, the Nunn-Domenici USA Tax of 1995.[25] Because we hope that this Article is also of wide, general interest—not a narrow "tax" piece for the few who read such things—we shall explain tax principles to the extent needed for present purposes below. For now, the point to stress is that there would be no provision in the reformed tax system that is specific to political expenditures, other than provisions disallowing such expenditures as ordinary business deductions or as charitable contributions.

This is precisely the case as under the current income tax.[26] The tax reform is not directed at campaign finance per se; this Article is taking no position on disclosure rules or the role, if any, for the FEC, for example. The tax proposal is, as Professor Kang has called for, "campaign finance reform . . . from outside campaign finance regulation as we have known it."[27] This is a large advantage on the path to hope.

On account of its generality the proposal raises no significant First Amendment concerns such as those that have haunted and significantly

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21. In this regard, the Article differs from prior proposals to tax campaign contributions specifically, such as the idea of "corrective taxes" explored by David Gamage in his student note, *Taxing Political Donations: The Case for Corrective Taxes in Campaign Finance*, 113 YALE L.J. 1283 (2004). *See also* GUIDO CALABRESI, THE FUTURE OF LAW & ECONOMICS 85–87 (2016) (discussing concepts of merit goods and bads, taxation, and campaign expenditures).

22. *See* NICHOLAS KALDOR, AN EXPENDITURE TAX (1955); EDWARD J. MCCAFFERY, FAIR NOT FLAT: HOW TO MAKE THE TAX SYSTEM BETTER AND SIMPLER 97 (2002); ROBERTO MANGABIERA UNGER, DEMOCRACY REALIZED: THE PROGRESSIVE ALTERNATIVE 139–50 (1998); William D. Andrews, *A Consumption-Type or Cash Flow Personal Income Tax*, 87 HARV. L. REV. 1113, 1150–51 (1974).

23. *See* Chris Matthews, *Bill Gates' Solution to Income Inequality*, FORTUNE (Oct. 15, 2014, 8:42 AM), https://fortune.com/2014/10/15/bill-gates-income-inequality/ [https://perma.cc/3BUW-P8YX].

24. *See* ROBERT H. FRANK, LUXURY FEVER: WHY MONEY FAILS TO SATISFY IN AN ERA OF EXCESS 211–26 (1999).

25. *See* Murray L. Weidenbaum, *The Nunn-Domenici USA Tax: Analysis and Comparisons* 1, 7 (Weidenbaum Ctr. on the Econ., Gov't, and Pub. Policy, Occasional Paper No. 152, 1995); Laurence S. Seidman, *A Progressive Consumption Tax*, 40 CHALLENGE 63 (1997).

26. *See* I.R.C. § 162(e)(1) (2018).

27. Kang, *supra* note 13, at 52–53.

crippled efforts to get money out of politics:[28] the present income tax *already* makes political contributions nondeductible and hence fully taxable, just as it generally does the purchase of books, newspapers, and other speech-infused activities.[29] The principal problem with the status quo, as we shall see, is that the present system fails to tax the spending of the mega-rich consistently. The tax reform acts generally to tax the consumption of the rich, of which large political expenditures are but a particular example, at higher levels.

This is all because the tax law proposal aims at a larger problem of which outsized campaign contributions are but a part: the unchecked high-end spending of the mega-rich. The tax law changes aim to make the tax system more consistently apply to personal spending, and then to raise marginal rates, precisely because the tax will fall on and only on spending. Large levels of personal, consumptive spending become the relevant social harm being taxed at higher levels, like cigarette smoking under tobacco taxes. All that is then needed is for political contributions to be treated as non-deductible consumption or spending—as they are today, and always have been under the U.S. income tax—to be swept into the general effect.

That effect can be dramatic. Because political contributions are not deductible under current law, Sheldon's $100 million must come from money that Sheldon has available, after taxes. The rational question is, How much money does Sheldon need before taxes to be able to make $100 million in contributions after taxes? The best answer, under current law, to a first approximation, is $100 million. A plausible case can even be made that Sheldon is *saving* taxes, as much as $40 million, with his political expenditures: that $100 million in contributions really costs him and his family "just" $60 million in foregone personal consumption.[30] In short, the current tax system *encourages and even rewards* political mega-donors.[31] How much might Sheldon need to make the same $100 million political

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28. *See* Kathleen M. Sullivan, *Two Concepts of Freedom of Speech*, 124 HARV. L. REV. 143 (2010).

29. *See* I.R.C. § 162(e)(1); I.R.C. § 173 (2018).

30. This is an argument we press in Edward J. McCaffery, *Mike Bloomberg's Presidential Run Could Cost Taxpayers Billions*, CNN (Feb. 28, 2020, 11:59 AM), https://www.cnn.com/2020/02/28/opinions/bloomberg-presidential-run-could-cost-taxpayers-billions-mccaffery/index.html [https://perma.cc/9A7C-MRMU].

31. Note that this effect—an incentive to spend—is also present under the wealth tax proposals of Senators Bernie Sanders (I-Vt) and Elizabeth Warren (D-Mass): present consumption is a way to avoid wealth taxation. *See* Howard Gleckman, *A Wealth Tax Will Encourage More Spending by The Rich—And Maybe More Political Donations*, TAX POL'Y. CTR. (Oct. 31, 2019), https://www.taxpolicycenter.org/taxvox/wealth-tax-will-encourage-more-spending-rich-and-maybe-more-political-donations [https://perma.cc/8937-LVFM].

contribution under a consistent progressive spending tax? A plausible answer is $1 *billion.* In other words, moving to a progressive spending tax—a movement that is well justified on independent grounds—could have the effect of increasing the cost of political contributions for the mega-donor class by *ten times*. Sheldon would have to pay the government $900 million in taxes for the privilege of being able to make $100 million in campaign contributions.

That should do something to get money out of politics.

The balance of this Article explains these analytic facts and adds in normative justification for the general idea of a progressive spending tax as a response to the specific problem of too much money in American politics. In doing so, the Article sets forth a thought experiment. It does not proffer a detailed legislative policy proposal for tax reform. It aspires rather to get readers thinking differently about addressing perhaps the fundamental problem in American politics today, about specifying just what the social costs of economic inequality are, and about the tools available for a reasonable society to address those costs. The Article sees political spending as an example of the kind of outsized spending that is allowed unchecked and even encouraged under current laws. It sees the tax system as a major part of the problem of mega-spending, and it envisions a future in which tax becomes a major part of a solution instead. The thought experiment is bi-directional. High-end political spending helps us to see the problems of the current tax system in a new light, and considering tax helps us to think differently about the possibilities for curbing the role of money in politics by stepping outside the box of traditional campaign finance regulation. Tax brings hope to a cause that seems hopeless, and the cause in turn sheds light on the deepest failures of tax.

II.   POLITICAL CONTRIBUTIONS UNDER THE CURRENT TAX SYSTEM

A. A Touch of Tax Theory

Political contributions are not and never have been deductible under the U.S. income tax.[32] Sheldon can get tax deductions for various business expenses he might incur, or investments he might make, under I.R.C. Section 162,[33] but he cannot get a deduction for political expenditures under Section

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32. *See* I.R.C. § 162(e)(1).
33. *See* I.R.C. § 162.

162(e).[34] Sheldon can also get a deduction, under I.R.C. Section 170, for contributions he might make to qualified charities under I.R.C. Section 501(c)(3).[35] But Section 501(c)(3) organizations, by virtue of the so-called Johnson Amendment, cannot engage in direct political activities.[36] Various other forms of nonprofit entities, such as "social welfare organizations" under I.R.C. Section 501(c)(4)—including, for example, the National Rifle Association ("NRA") and the American Civil Liberties Union ("ACLU")[37]— *can* engage in political activities, and, under a Trump Administration rule, need not disclose their donors.[38] But contributions to such organizations are

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34.   I.R.C. § 162(e)(1) provides

> (e) Denial of deduction for certain lobbying and political expenditures
>   (1) In general: No deduction shall be allowed under subsection (a) for
>   any amount paid or incurred in connection with—
>   (A) influencing legislation,
>   (B) participation in, or intervention in, any political campaign on
>   behalf of (or in opposition to) any candidate for public office,
>   (C) any attempt to influence the general public, or segments thereof,
>   with respect to elections, legislative matters, or referendums,
>   or
>   (D) any direct communication with a covered executive branch
>   official in an attempt to influence the official actions or
>   positions of such official.

35.   I.R.C. § 501(c)(3) (2018).

36.   The relevant language of the Johnson Amendment is contained in the final clause of I.R.C. Section 501(c)(3), which provides that in order for a charity to qualify as a Section 501(c)(3) non-profit, to which contributions would be tax deductible under I.R.C. Section 170:

> no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation (except as otherwise provided in subsection (h)), and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office.

Note the similarities in the language to I.R.C. Section 162(e), *supra* note 34. *See generally Charities, Churches and Politics*, INTERNAL REVENUE SERV., https://www.irs.gov/newsroom/charities-churches-and-politics [https://perma.cc/WHG6-K9YM].

37.   Both the NRA and the ACLU have sister 501(c)(3) organizations, but the primary named entity is a 501(c)(4). *See* I.R.C. § 501(c)(4) (2018); Jeff Krehely, *501(c)(4) Organizations: Maximizing Nonprofit Voices & Mobilizing the Public*, NAT'L COMM. FOR RESPONSIVE PHILANTHROPY (Jan. 30, 2005), https://www.ncrp.org/publication/501c4-organizations-maximizing-nonprofit-voices-mobilizing-public [https://perma.cc/DLY3-9AK6].

38.   *See* Laura Davison & Bill Allison, *Many Political Tax-Exempts No Longer Required to Report Donors*, BLOOMBERG (July 16, 2018, 6:06 PM), https://www.bloomberg.com/news/articles/2018-07-17/many-political-tax-exempts-no-longer-required-to-report-donors [https://perma.cc/FG83-JWHG].

not tax-deductible.[39] This leaves political expenditures like Sheldon's $100 million in the residual category of non-deductible consumption under I.R.C. Section 262, which provides quite generally that no deduction shall be allowed for "personal, family or living expenses."[40] Political contributions are but an example of such nondeductible personal expenses. This all obtains without any need to particularly classify or describe political spending, other than to see that it is neither business-related nor charitable under the income tax.

That personal consumption is, and must be generally, nondeductible is in fact an essential part of what an income tax is, or is supposed to be. Consider the celebrated Haig-Simons definition of Income, which holds essentially that

$$[2]\ Income\ =\ Consumption\ +\ Savings.[41]$$

This is a very simple statement, a tautology, which helps to show that all inputs (Income) lead to outputs, and that all outputs are either spending (Consumption) or non-spending (Savings). But Equation [2] still shows that an income tax *must* include consumption in its base. Imagine for a moment if it did not: imagine, that is, that you could deduct from your income tax each year all the money you spent on "personal, family, and living expenses" such as food, clothing, shelter, and fun. Many readers, certainly most students, and all of our children, would end up paying no tax at all because they spend more than they earn.

As a practical matter, note that there is no need to define "consumption" under the tax laws, nor, for the same reason, is there any need to argue that political spending is consumption. Personal consumption is a residual category, that which is not deductible from income for some specific, stated reason. Once we classify political contributions as neither "business" nor "charitable" expenses, they are left as personal consumption, non-deductible under I.R.C. Section 262, and hence fully taxable. Sheldon's $100 million of political contributions will be taxed the same way that it would be if Sheldon had spent the amount on artwork, additional homes, a private jet, or a bunch

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39. *Donations to Section 501(c)(4) Organizations*, INTERNAL REVENUE SERV., https://www.irs.gov/charities-non-profits/other-non-profits/donations-to-section-501c4-organizations [https://perma.cc/FYT7-AACX].

40. I.R.S. § 262 (2018).

41. The full statement of the Haig-Simons definition of income is generally attributed to HENRY C. SIMONS, PERSONAL INCOME TAXATION: THE DEFINITION OF INCOME AS A PROBLEM OF FISCAL POLICY 50 (1938) ("Personal income may be defined as the algebraic sum of (1) the market value of rights exercised in consumption and (2) the change in the value of the store of property rights between the beginning and end of the period in question."). For a simpler statement, see EDWARD J. MCCAFFERY, INCOME TAX LAW 7 (Dennis Patterson ed., 2012).

of gold-plated toilets—no deduction, meaning that the payment must come from post-taxed dollars.

B. Calculating Before Tax Costs of Political Expenditures

Because Sheldon will not get a tax deduction for his $100 million contributions, he must actually have $100 million available to pay over to politicians, after he pays his taxes. Where did this come from? We need to calculate the amount of money, which we shall call B, which Sheldon must have before taxes to calculate what he will need to generate the $100 million in cash to give to candidates of his choice, after taxes have been taken into account.

On the initial amount, B, Sheldon will have to pay tax, at the tax rate t, meaning that -tB will have to be paid over to the government. This will leave Sheldon with (1 - t) of his initial B. Adding the term A to describe Sheldon's after-tax money, we arrive at,

$$[3] \; B \, (1 - t) = A$$

This is simple math. To put Equation [3] in a numeric example, imagine that the tax rate, **t**, is 40%, and you earned $100, which would be your B. You would have to pay 40% of B, or $40, in taxes. You would keep (1 - t), or 60% of $100, or $60, after taxes, which is your A.

In Sheldon's case, we know that the A, the actual contribution, is $100 million. What is Sheldon's B? For this, we simply rearrange Equation [3] to solve for B:

$$[4] \; B = A/(1 - t).$$

How much money does Sheldon need to start with to be able to spend $100 million? The answer turns on Sheldon's tax rate, t. Once we know that, we can solve for B simply enough using Equation [4].

C. The Before-Tax Cost of Political Expenditures Under the Current Income Tax

1.   Tax Rates on the Wealthy Under the Current Income Tax

In order to calculate the amount that Sheldon needs to have to make a $100 million political contribution, after taxes, we need to know what tax rate Sheldon faces on his wealth as it is being converted into funds for current consumption, under Equation [4].

We must therefore look at the proximate sources for Sheldon's spending. There are, broadly speaking, three possible candidates to consider under current law. We shall use simple, round numbers for the tax rates: actual tax rates vary, and the points this Article are making are general analytic ones. Precise details can wait.

One candidate for Sheldon's *t* is 40%, approximately the top "ordinary income" rate imposed by I.R.C. Section 1.[42] This is the rate faced on *labor* income, or wages, today.[43] Facing a 40% tax rate would mean that Sheldon worked for a living to generate his $100 million sum, which was in turn sourced to his labor.

But immediately we note that this is unlikely: it is almost certainly *not* the case that any real-world Sheldon would have $100 million *after paying ordinary income taxes* with which to make his political expenditures. Certainly, billionaires such as the late Steve Jobs, Warren Buffet, Bill Gates, and President Donald J. Trump do not ever show such large wages.[44] In 2018, chief executives at Fortune 500 companies averaged $14.5 million in earnings:[45] almost 300 times what an average American worker earned but still not enough to generate, after taxes, the ability to make $100 million campaign contributions every other year. (At a 40% tax rate, $14.5 million before taxes becomes $8.7 million after taxes. It would take 11.5 years to reach $100 million of cumulative after-tax income.) And much of CEO compensation is not taxed at ordinary income rates in any event.[46] Many high income earners, such as Wall Street hedge fund managers, rely on stock options, or report their "income" as capital gains, using a trick known as "carried interest."[47] The very richest of all, such as Buffet and Gates, do not even bother to show much income in the first place, relying instead on "unrealized appreciation," which is not taxable under the century-old Supreme Court decision of *Eisner v. Macomber*.[48] As Gates himself puts it:

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42.   I.R.C. § 1 (2019).

43.   *See* Edward J. McCaffery, *The Death of the Income Tax (or, The Rise of America's Universal Wage Tax)*, 95 IND. L. J. (forthcoming 2020) (manuscript at 43) (on file with author).

44.   *See id.* at 6–7.

45.   *See* Alexia Fernández Campbell, *CEOs Made 287 Times More Money Last Year than Their Workers Did*, VOX (June 26, 2019, 8:20 AM), https://www.vox.com/policy-and-politics/2019/6/26/18744304/ceo-pay-ratio-disclosure-2018 [https://perma.cc/NVX9-B4MG].

46.   *Id.*

47.   *See* Victor Fleischer, *Two and Twenty: Taxing Partnership Profits in Private Equity Funds*, 83 N.Y.U. L. REV. 1, 3 (2008); Victor Fleischer, *Two and Twenty Revisited: Taxing Carried Interest as Ordinary Income Through Executive Action Instead of Legislation* (Sept. 16, 2015) (manuscript at 3–4), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2661623 [https://perma.cc/Y65N-Z27E].

48.   252 U.S. 189, 219 (1920).

"In terms of revenue collection, you wouldn't want to just focus on the ordinary income rate, because people who are wealthy have a rounding error of ordinary income."[49] We listen to Gates and will not make the mistake of focusing on the 40% ordinary rate in our thought experiment.

A second candidate for Sheldon's *t* is 20%, approximately the rate faced on *capital* gains or income under I.R.C. Section 1(h),[50] which has historically been one-half or less of the ordinary income tax rate just discussed. This would obtain if Sheldon met his $100 million mark by selling assets that he owned, such that his full consumption were sourced to capital.

But again this is unlikely. *If* Sheldon had to sell assets to generate his $100 million expenditure, and *if* the assets he sold had no tax law "basis" under I.R.C. Sections 1011 and 1012, and *if* Sheldon had no capital losses to use to offset the capital gains under I.R.C. Section 1211, all such that the full amount realized under I.R.C. Section 1001 would be taxed, *then* Sheldon's *t* would indeed be the full 20%.[51] But studies have shown what common sense suggests: this is not what the rich do.[52] Because of the benefits of deferral, of the possibility of some basis offset, and of some available capital losses to net against any gain, Sheldon would be highly unlikely to face the full 20% rate even if he did have to sell some of his assets to finance his $100 million of spending.[53] "Income realized for tax or survey purposes usually understates economic income for the wealthy because capital income recognition is often voluntary," as one recent study concluded.[54]

This then leaves as the third, and most plausible, option for Sheldon's *t*: 0%. This would obtain if Sheldon simply borrowed to get the $100 million, making *debt* the source of his present consumption. Borrowing is tax-free under the current and, indeed, under any income tax, by definition: borrowing

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49. Tanza Loudenback, *Bill Gates Says the Politicians Proposing 70% Income Tax Rates for the Super Rich Are "Missing the Picture,"* BUS. INSIDER (Feb. 12, 2019, 9:48 AM), https://www.businessinsider.com/bill-gates-taxes-income-tax-wealthiest-americans-2019-2 [https://perma.cc/N8TB-UUAX].

50. I.R.C. § 1(h) (2018).

51. Under I.R.C. Section 1001, the amount of gain realized on any sale or other disposition of property measured by the fair market value of what is received minus the basis of the asset surrendered. "Basis" is a tax-law concept, initially referring to cost. I.R.C. § 1012 (2018).

52. *See* Jenny Bourne et al., *More than They Realize: The Income of the Wealthy*, 71 NAT'L TAX J. 335, 335 (2018).

53. If, for example, Sheldon sold corporate stock to generate his $100 million, and he had basis in the stock of $60 million, Sheldon would have to pay capital gains tax on the difference, or $100 - 60, or $40, which would generate $8 million of taxes (20% of $40 million), for a total effective tax rate of 8% on the sale ($8/100 million). *See* I.R.C. § 1001(a) (2018). Bourne et al., *supra* note 52, at 351 show conclusively that the actual effective tax for the wealthy is far below the statutory rate.

54. Bourne et al., *supra* note 52, at 335.

does not lead to a change in one's net wealth, the borrowed funds being offset by the obligation to repay the loan.[55] Combined with *Macomber*'s realization requirement, the nontaxation of debt gives a way for billionaires to monetize their unrealized appreciation, tax-free.[56] There is abundant evidence that the wealthy take advantage of this strategy: for example, President Donald J. Trump, who is known to avoid taxes in most years, is the self-proclaimed "King of Debt";[57] his fellow billionaire Larry Ellison has a personal line of credit of at least $10 billion.[58]

Later we shall discuss how this rough pattern of tax rates facing the wealthy as they finance present period consumption—forty, twenty and zero percent—is not an artifact of a particular time. Rather, such a rate structure is highly suggested, if not dictated, by the intrinsic structure of an income tax. In more formal economic terms, the rate structure on personal consumption is largely endogenous to the choice of tax system design—it grows organically from the initial policy decision to have an income tax.

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55.   Under the Haig-Simons definition, Equation [2] above, borrowing is both a source of income, on the left-hand side, and some use—either consumption or savings—on the right-hand side. So this becomes a "wash" on which no income tax is due. *See* SIMONS, *supra* note 41.

56.   *See* Lawrence Zelenak, *Debt-Financed Consumption and a Hybrid Income-Consumption Tax*, 64 TAX L. REV. 1, 7 (2010).

57.   *See* Edward J. McCaffery, *Donald Trump Is the King of Debt but Not of Taxes*, CNN (Sept. 2, 2016, 8:11 PM), https://www.cnn.com/2016/09/02/opinions/trump-king-of-debt-but-not-taxes-opinion-mccaffery/index.html [https://perma.cc/2FWU-NFTU].

58.   *See* Julie Bort, *Larry Ellison Has Secured $10 Billion Worth of Credit for His Personal Spending*, BUS. INSIDER (Sept. 26, 2014, 4:29 PM), https://www.businessinsider.com/larry-ellison-has-a-10b-credit-line-2014-9 [https://perma.cc/PN7R-Q2U9]. Many billionaires, including President Trump, seem to be cash poor. Consider the case of Elon Musk, for example, whose net worth is estimated to be over $20 billion: Mr. Musk, who draws no salary from his private company, Tesla, is said to be "cash poor," with debts of at least $500 million. Noah Kirsch & Alex Knapp, *Why Elon Musk Is Cash Poor (For a Billionaire)*, FORBES (Dec. 4, 2019, 4:59 PM), https://www.forbes.com/sites/noahkirsch/2019/12/04/why-elon-musk-is-cash-poor-for-a-billionaire/#59ef67f133f6 [https://perma.cc/S3FG-LU5X]. These billionaires are playing "Buy/Borrow/Die" to avoid taxation. *See generally* Edward J. McCaffery, *Taxing Wealth Seriously*, 70 TAX L. REV. 305 (2017). For those readers who consider that any interest on the loan is a cost of this strategy, consider again. First, interest rates available for billionaires have been historically low for decades. Second, the borrowing strategy of this third approach compares with the asset sale of the second approach. In the borrowing example, *Sheldon retains his asset*. Thus, the (minor) interest charge on a $100 million is offset by the rate of return on *$125 million* of an asset, which would have to be sold, and taxes paid, to generate the $100 million needed. In these circumstances, borrowing dominates selling as a means to get liquidity for billionaires. *See id.* at 322–23.

2.   Calculating the Before-Tax Cost

The prior section has given us a range of *t*'s to plug into Equation [4], above, in order to calculate how much Sheldon's $100 million would cost him, at the margin, taking into account any taxation imposed on the source of Sheldon's funds. We considered three possible sources: labor, capital, and debt. **Table 1** presents the results:

Political Contribution (A)	Tax Rate (%)	Funds Needed to Finance Contribution (B)
100	40	167
100	20	125
100	0	100

Table 1: Costs of Sheldon's Contributions under Current Law, in millions of dollars

The key column is the far-right one, showing *B*, the funds needed *ab initio* to finance Sheldon's $100 million contribution. **Table 1** illustrates that, in order for Sheldon to be able to write a check for $100 million in non-deductible political expenditures, he must have started with between $100 and $167 million under current law. The actual answer, in any real case, is almost certainly very close to $100 million; our Sheldon is no fool.

D. A Further Twist: Political Expenditures as Tax Expenditures Under the Estate Tax

Suppose, as would seem to be likely, Sheldon, like his fellow billionaires, has significant amounts of appreciated assets on hand,[59] and he simply writes a check for $100 million using some kind of margin account[60] to make his

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59. *See* Bourne et al., *supra* note 52, at 337.

60. A margin account, as can easily be set up at investment houses such as Charles Schwab or Fidelity, allows the owner of a stock and securities account to simply write checks effecting a loan secured by the securities in the account. As long as the margin loan balance does not exceed a certain percentage of the account's value, say 50%, interest simply accrues on the margin loan balance. As discussed in a prior note, the return generated by the securities in the account pledged as collateral should be offset against the interest charged on the margin loan, such that the loan

political expenditures. The prior section, using Equation [4], showed how this would cost Sheldon $100 million, before and after taxes. This is because Sheldon need pay no tax on the unrealized appreciation being used to finance his political payments, nor on using debt to monetize the non-taxed appreciation.[61]

In fact, Sheldon's after-tax situation may plausibly be seen as even better than this.

The reason is the existence of the estate tax. This is a tax on the net worth that someone leaves on her deathbed: on, that is, one's assets minus her liabilities postmortem. In Sheldon's case, the $100 million loan he used to make his political contributions would be a deduction from his taxable estate.[62] If Sheldon had $100 million cash on hand instead of needing to borrow, the result would be the same, with the actual cash being deducted from Sheldon's taxable estate.

After President Trump's Tax Cut and Jobs Act of 2017,[63] very, very few Americans must worry about an estate tax following their death. The exemption level has been raised to over $11 million for an individual and $22 million for a married couple with proper planning, both numbers indexed for inflation.[64] At these values, according to a study prepared by the Tax Policy Foundation, "an estate tax return will be filed for only about 0.15% of decedents, and only about 0.07% will pay any estate tax."[65] In other words, 99.93% of Americans need not countenance their families facing an estate tax after their passing.

Sheldon, however, let us presume, is indeed in the 0.07% category that will face an estate tax. The $100 million that Sheldon has available to give to politicians in our running example, alone, would put Sheldon well into the

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need not be paid off until after Sheldon's death, when his heirs would get a stepped-up basis in the securities pursuant to I.R.C. Section 1014. *See* I.R.C. § 1014 (2018). On margin loans in general, see *Investor Bulletin: Understanding Margin Accounts*, U.S. SEC. AND EXCHANGE COMMISSION (May 14, 2018), https://www.sec.gov/oiea/investor-alerts-and-bulletins/ib_marginaccount [https://perma.cc/ZL23-DHFD].

61.   The tax saving technique, all in, has been labeled Tax Planning 101, or the simple advice to buy/borrow/die. *See* McCaffery, *supra* note 58, at 306; Edward J. McCaffery, *A New Understanding of Tax*, 103 MICH. L. REV. 807, 888 (2005) [hereinafter McCaffery, *A New Understanding*].

62.   *See* I.R.C. § 2053 (2018).

63.   Budget Fiscal Year, 2018, Pub. L No. 115-97, 131 Stat. 2054 (2017).

64.   I.R.C. § 2010(c)(3)(C) (2018). The inflation adjustment made this exclusion amount $11.18 million for 2018 and $11.4 million for 2019.

65.   *How Many People Pay Estate Tax*, TAX POL'Y CTR., https://www.taxpolicycenter.org/briefing-book/how-many-people-pay-estate-tax [https://perma.cc/7T53-7TQU].

estate tax range. We can also consider him a widower, so that his estate will not have the "marital deduction" of I.R.C. Section 2056 to bail him out (having a spouse effectively doubles the exemption level and postpones the moment of taxation until after the second death). The estate tax has a rather flat rate of 40%.

The relevance of all this? Imagine, again not implausibly, that a mega-donor such as Sheldon is elderly and has plenty of funds available for his daily wants and needs, however luxurious. Our Sheldon is also not extremely philanthropic,[66] preferring to leave whatever wealth he has left over on his deathbed to his children and other heirs. This would mean that Sheldon's next best use of his $100 million is simply to save it such that it will go to his heirs after his death. If this were true, Sheldon's "opportunity cost" of the $100 million political expenditure would be a $60 million bequest—what of the $100 million he could get to his heirs, given his status as being fully subject to a 40% estate tax after his death.[67]

To illustrate: suppose Sheldon lay on his deathbed, with a net worth of $1 billion dollars. Were he to pass then and there, this would be the amount of his taxable estate, and his family would pay a tax of $400 million at the 40% rate. But if Sheldon were to write one last check, for $100 million, that he financed out of available cash, *or* by selling an asset worth $100 million, *or* by borrowing, his taxable estate would fall to $900 million ($1 billion minus $100 million, whether the $100 million came from cash, non-cash assets, or debt). The estate tax to be paid by his family would fall to $360 million, 40% of $900 million. The $100 million expenditure would lead to $40 million less in tax ($400 million minus $360 million), so would cost Sheldon and his heirs $60 million on net. This is what tax policy scholars refer to as "tax expenditure" analysis, as we explain below.[68]

We do not want to overstate this point, because it is true, as with the income-with-realization tax, that Sheldon would have relatively simple tax-planning options available to get his children their cake while allowing them

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66. If Sheldon were philanthropic, such as Bill Gates or Warren Buffet, he could avoid the estate tax for his family by giving his wealth away to charity, qualifying for the estate tax charitable contribution deduction of I.R.C. Sections 2055 and 642(c).

67. There is no need to discount the future tax, here $40 million, to Sheldon's present, because the $100 million he is spending on political contributions, if not spent, would be expected to grow at least the inflationary or discount rate.

68. For helpful background on the concept, stressing the role of Stanley Surrey in its formation and development, see William McBride, *A Brief History of Tax Expenditures*, TAX FOUND. (Aug. 22, 2013), https://taxfoundation.org/brief-history-tax-expenditures/ [https://perma.cc/8AUK-4HFN].

to eat it, tax-free, too.[69] But we make the point to underscore an analytic fact. Academics and policymakers have long referred to various deductions, credits, and exemptions under the income tax law as "tax expenditures."[70] The idea is simple to understand. An income tax is supposed to tax all consumption plus all savings, as the Haig-Simons definition, Equation [2], showed. If Congress allows a deduction for something that it *could*, legally, tax under the definition of "income"—all consumption plus all saving—then it is forswearing the tax it could have collected on that amount. If in our running example Sheldon were allowed to deduct his $100 million in political contributions, this deduction would lower his taxable income by the full $100 million and thus save Sheldon taxes—real money—at his marginal tax rate. If that rate were 40%, Sheldon would see his taxes reduced by $40 million on account of the $100 million deduction. So, Sheldon's $100 million given out in political contributions would be partially offset by the $40 million in saved taxes, such that Sheldon's net out-of-pocket cost for the contributions would be $60 million. The government would be chipping in the remaining $40 million via taxes forsworn. Sheldon would be playing with house money, in significant part.

Here is the point of current relevance: under a back-ended wealth tax like the estate tax, *all present consumption has the structure of a tax expenditure*. The tax base is one's net wealth on her deathbed. Any present expenditure that subtracts from this net wealth lowers the tax, hence saving the spender's family money at the estate tax's marginal rate, 40%, just as we went through above as Sheldon lay dying. This is why the simplest estate planning advice—Estate Planning 101 as it were—is to spend it all and die broke.[71] Sheldon's $100 million political contributions do save him, or his family, taxes—under the estate tax, not the income tax.

A principal reason to set this forth is to give a look at how perverse the current tax system can be, especially once high-end *spending* is identified as an important social harm. We have seen in the prior section that the current tax is not doing much at all to discourage Sheldon's political expenditures—

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69. For example, Sheldon Adelson was able to get nearly $8 *billion* to his children and heirs, tax-free, when the exemption level was far below its current level, at $1 million (during one's lifetime, the gift tax is supposed to apply to wealth transfers, such that policy makers refer to the combined gift and estate tax systems as a single, unitary wealth transfer tax, applying to both *inter vivos* gifts and testamentary bequests). *See* Zachary R. Mider, *Accidental Tax Break Saves Wealthiest Americans $100 Billion*, BLOOMBERG NEWS MAG. (Dec. 16, 2013, 10:01 PM), https://www.bloomberg.com/news/articles/2013-12-17/accidental-tax-break-saves-wealthiest-americans-100-billion [https://perma.cc/5B3R-JPZE].

70. *See generally* STANLEY S. SURREY & PAUL R. MCDANIEL, TAX EXPENDITURES (1985).

71. *See, e.g.*, STEPHEN M. POLLAN & MARK LEVINE, DIE BROKE: A RADICAL FOUR-PART FINANCIAL PLAN 3 (1997).

barely if at all raising their true net of tax costs. Adding in the estate tax as part of the status quo and the tax expenditure analysis just discussed shows how the current tax system is even worse on the score of discouraging large political contributions. America's tax system *encourages* the high-end consumption of the mega-rich, the very class of citizens whose spending habits ought to cause a reasonable democracy most concern. In both allowing vast sums of wealth to build up, tax free, under the simple planning steps suggested by *Macomber*'s realization requirement, and in allowing those sums to be spent or consumed, *also* tax-free, America's tax system is clearly a major part of the problem of wealth inequality in the country today, and no part of a solution. A tax system that is supposed to tax all consumption does not: it misses the spending of the rich, very much including their outsized spending on politics.

E. Summing Up

In order to pay out $100 million in political contributions, Sheldon needs to spend no more than $100 million under the current income-with-realization tax. There need be no tax paid on this value, although it represents personal consumption meant to be fully taxable under a true, Haig-Simons, income tax. At worst, there might be some "rounding error," as Bill Gates would put it,[72] in capital taxation, or Sheldon is not quite optimally advised, such that it takes closer to $125 million to generate the $100 million after tax in contributions. Thus, the current tax system barely if at all *discourages* Sheldon from making the expenditures. And when the estate tax, a back-ended wealth tax, is factored in, a plausible case can be made that the current tax system, the income-with-realization-plus-estate tax, *encourages* Sheldon's contribution, which costs Sheldon's family "just" $60 million after the $40 million of house money, via the tax expenditure analysis, is taken into account.

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72. Loudenback, *supra* note 49 (quoting Gates).

III.   POLITICAL CONTRIBUTIONS UNDER A PROGRESSIVE SPENDING TAX

A. A Tax Theory Twist

The tax reform proposal is for a consistent consumption tax. The academic literature has pointed out that there are different forms of a consumption tax,[73] all of which are single taxes on the flow of funds, as opposed to an income tax, which is supposed to tax savings twice (both as money is earned and when, having been saved, it generates a yield).[74] The two types of consumption taxes are "prepaid" models, where a tax is levied upfront, and never again, like the payroll tax; and "postpaid" models, where the tax is not necessarily imposed upfront—there is a deduction for savings—but instead when money is used for personal consumption or spending, like a sales tax.[75]

The tax reform proposal here is for a postpaid consumption tax, one that is levied as funds are put to use in financing personal spending, so we call it a spending tax. It shall feature progressive rates, so we shall call it a progressive spending tax.

A progressive spending tax of the sort being proposed is not a spending tax levied on particular purchases at point of sale, like the familiar state and local sales taxes most Americans pay daily. A progressive spending tax would look very much like the current income tax: it would have an annual form, like the dreaded IRS Form 1040, to be filed each year, at least by those wealthy enough to have to do so. In the case of a progressive spending tax, the form would "simply" add up all sources of Income, and then equally simply subtract all forms of Savings, to arrive at the residual category of Consumption, or personal spending. A progressive marginal rate structure would then be applied to each household's spending for the year. Political expenditures would be included in Consumption, just as they are under the current income tax, as discussed above, here because political expenditures would not qualify for any deduction as Savings. Hence progressive rates would apply to political spending, as they would to all personal spending.

It may be easier to understand how a progressive spending tax works by returning to the Haig-Simons definition, Equation [2] above:

$$[2]\ Income\ =\ Consumption\ +\ Savings.$$

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73.   *See generally* McCaffery, *A New Understanding*, *supra* note 61 (describing two forms of consumption tax).

74.   *Id.* at 824–27.

75.   *See* Andrews, *supra* note 22.

A simple algebraic manipulation—subtracting Savings from both sides of Equation [2]—shows us how simply a consumption tax, along a cash-flow or spending tax model, can come to be:

$$[5]\ Consumption\ =\ Income\ -\ Savings.$$

In words, a spending tax can be had easily enough by adding up all sources of Income—just as an income tax is supposed to do—and systematically subtracting all Savings, as many have proposed that the income tax should do, and as the Nunn-Domenici USA tax would automatically do.[76] The residuum—what resources you had available that you did not save—is, by definition, Consumption.

The most important practical policy change from the status quo is the need to include debt, or the proceeds of borrowing, as income.[77] This follows simply from the systematic subtraction of savings: debt is negative savings, and subtracting a negative leads to addition. Debt that is used to save will end up as a "wash": the inclusion for the debt will be offset by the deduction for savings. Borrowing to consume, on the other hand, will be taxable. This may sound odd, but note that it is just as it is in the case of the familiar state and local sales taxes that exist across America today: when you pay for a good using borrowed funds, as by putting the purchase on a credit card, you still pay sales tax at the time of purchase.

While a progressive spending tax faces the challenge of finding a way to report on and include taxpayer borrowing in its base, it would importantly and significantly simplify the tax system by removing any need to tax savings directly.[78] Thus, a progressive spending tax needs no realization requirement, no tax-law concept of "basis" (since no savings has been taxed, savings do not need basis). The rise in value of assets inside tax-favored savings accounts will not be taxed, just as today when gains inside pension plans or individual retirement accounts ("IRAs") are not currently taxed. The difference will be that savings accounts will be unlimited in potential amount. Taxpayers will pay tax only when they withdraw from the accounts to spend, or when they spend out of current income, or when they borrow to spend. Under a consistent consumption tax along the lines of Equation [5], the fact of spending is what triggers tax, not the facts of work or savings.

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76. *See* Seidman, *supra* note 25, at 63.
77. The Nunn-Domenici USA Tax Plan from 1995, mentioned above, failed to include borrowing in its base; this would have proven to be a fatal flaw in the plan, as taxpayers could pretend to save all of their income and then borrow to engage in present consumption. *See id.* at 81.
78. *See* McCaffery, *supra* note 22, at 97.

The ultimate source of that spending, whether it be from labor, capital, labor and capital combined, debt, gifts, bequests or anything else, is irrelevant. And this is how a reasonable society ought to think about political expenditures: *whatever* the ultimate source of the funds, the unchecked ability of individuals to give $100 million per campaign cycle is a significant and mounting social problem. (In Section 4, we generalize this argument to extend to all forms of mega-spending.) The current tax system, by failing to consistently tax personal spending—it lightly taxes spending funded by capital and ignores spending financed by debt altogether—misses the high-end spending of the rich. It is that very high-end spending that is precisely the target of a progressive spending tax.

B. Tax Rates Under a Progressive Spending Tax

Although the one practical legislative proposal that has come closest to a progressive spending tax, the Nunn-Domenici USA tax plan from the 1980s (with "USA" standing for "unlimited savings accounts") featured progressive rates up to 40%,[79] most commonly known consumption tax models feature flat rates. This does not have to be so.[80] Indeed, there are compelling reasons, sounding in arguments both of economic efficiency and of normative fairness, that a spending tax can and should have *higher* marginal tax rates than an income tax.[81] The potential for a different tax rate structure on high-end spending is a central part of this Article's thought experiment and of the case for a progressive spending tax.

The efficiency argument for such a pattern of progressive rates is straightforward. The current income tax, with its realization requirement and overall light hand on the capital side of taxation, is mainly a wage tax.[82] Faced with a tax on work, a taxpayer's principal marginal decision is to work or not. High tax rates under an income tax thus risk distorting *labor* effort, as taxpayers earning high incomes shift to leisure, or to various forms of non-wage compensation, such as stock options or carried interest. A consistent spending tax along the lines of Equation [5], in contrast, leaves taxpayers with *two* decisions: to work or not, *and* to consume or not (that is, to save). A consistent spending tax need have no deterrent effect on the socially productive activities (work and savings) of the mega-wealthy who are already

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79. *See* Seidman, *supra* note 25, at 82.
80. *See generally* McCaffery, *supra* note 22.
81. *See* Edward J. McCaffery & James R. Hines, Jr., *The Last Best Hope for Progressivity in Tax*, 83 S. Cal. L. Rev. 1031 (2010).
82. *See* McCaffery, *supra* note 41, at 12.

at maximum consumption and are happy to save their excess good fortune. A progressive spending tax can be, as Robert Frank has suggested, a "win-win" situation, since the rich subject to it can see their welfare improve simply by saving more.[83]

Normatively, arguments that a progressive spending tax can bear higher marginal tax rates than an income tax are also straightforward, if less mathematically demonstrable than the efficiency arguments for such rates. The idea turns on the commonsensical notion that we should tax "bads" rather than "goods." High-end spending can be seen as a "bad" in various ways, as it skews the allocation of goods towards luxury tastes, incites envy, and represents a failure to save—to maintain the social capital stock—by the economic actors most able to do so.[84] With the case of outsized political contributions in mind, it is easy to consider the harms of allowing billionaires unchecked spending power, while the case for the social harm of their productive activities, of generating income, is far less clear and is in fact highly contestable.

Back to math. Let us return to the case of Sheldon, contemplating his $100 million of political expenditures in one particular year. What marginal tax rate might he face under a progressive spending tax? It is reasonable to assume that Sheldon is already spending well; a conservative estimate of billionaires' personal spending habits would put them at at least $40 million a year, a mere 4% of $1 billion.[85] Under an income tax, there would be little reason to create a bracket above $40 million: few would be in it, and the high tax rate, as we have discussed, would only encourage those who were to work less, or to show less income—things that are easy to do under current tax laws. Today's income tax rates, for example, reach their peak of 37% at around $600,000 of taxable income for a married couple[86]—far short of the average billionaire's spending level.

A progressive spending tax is a different matter. It can justify higher marginal tax rates at its higher levels. Imagine, in our example, the same top rate of 40% we considered in the prior section on ordinary income, mainly

83.   *See* FRANK, *supra* note 24, at 211–16; *see also* Edward J. McCaffery, *The Tyranny of Money*, 98 MICH. L. REV. 2126 (2000) (reviewing ROBERT FRANK, LUXURY FEVER (1999)).

84.   I explore these arguments in greater depth in Edward J. McCaffery, *Must We Have the Right To Waste?*, *in* NEW ESSAYS IN THE LEGAL AND POLITICAL THEORY OF PROPERTY 76 (Stephen Munzer, ed., 2d ed. 2001).

85.   Tanza Loudenback, *The World's Billionaires Have So Much Money It's Hard To Fathom—Here's How Their Spending Compares to the Rest of Us*, BUS. INSIDER (Mar. 6, 2018, 8:13 AM), https://www.businessinsider.com/worlds-billionaires-spending-compared-to-average-people-2018-3 [https://perma.cc/3QEH-6LDG].

86.   I.R.C. § 1(j)(2) (2018).

labor. Congress is considering adding in new marginal tax rates on personal spending, which is what a progressive spending tax taxes. Perhaps they will add new marginal rate brackets for spending above $1 million, and $10 million, and finally—just to continue the thought experiment—a bracket for those who, again, *spend* more than $50 million a year, which would certainly include any mega-donor like Sheldon who is making political expenditures, alone, of $100 million every two years.[87] To have a visual for our running thought experiment, your task is to complete the following table:

Personal Spending	Marginal Tax Rate
Up to $1,000,000	No higher than 40%
$1,000,000 to $10,000,000	x
$10,000,000 to $50,000,0000	y
$50,000,000 and above	z

Table 2: Potential Marginal Tax Rates under a Progressive Spending Tax

Specifically, for Sheldon, given our thought experiment's focus on mega-political donors, the question is what rate you will choose for *z*, the rate that *only* applies to personal spending in excess of $50 million per year. We will, in the following section, consider three:

1. 50%, which seems like a reasonable minimum for a tax rate on personal *spending* in excess of $50 million a year;

2. 70%, which is the highest tax rate under Robert Frank's proposal, and a tax rate that was obtained under the income tax from the time of John F. Kennedy, in 1963, until Ronald Reagan, in 1981; and

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87. A brief primer on marginal tax rates: these work like a step function, like rungs on a ladder. That is, when one enters a new rate bracket, her rates do *not* increase across her whole range of taxable income or (in the case of a consumption tax) spending. If, say, the rate until $1,000,000 of spending had been 40%, such that the taxpayer pays $400,000 on her $1,000,000, she would still pay that $400,000, plus a tax on what she spends *above* $1,000,000 at the new rate. That is, the rates are those that apply *on the margin*, to the next dollar earned or spent, as the case may be.

3. 90%, which is less than the highest marginal tax rate under the income tax that obtained from 1944 until 1963.[88]

We calculate in the next section what such tax rates under a consistent spending tax would mean for Sheldon.

C. *The Before-Tax Cost of Political Expenditures Under the Current Income Tax*

As always, Sheldon wants to make $100 million in political expenditures. The question is how much money he needs to start with in order to contribute that much under a consistent spending tax. As under the current income tax, there will be no deduction for the political expenditures as business expenses, savings, or charitable contributions. Once again, we will use Equation [4]:

$$[4]\ B\ =\ A/(1\ -\ t).$$

Sheldon's *A* remains $100 million but now we consider the tax rates, *t*'s, just discussed, of 50, 70 and 90%. The results are set forth in **Table 3**.

Political Contribution (A)	Tax Rate (%)	Funds Needed to Finance Contribution (B)
100	90	1,000
100	70	333
100	50	200

Table 3: Before Tax Costs of Sheldon's Contributions under a Progressive Spending Tax

In words, this means that, at a 50% tax rate (for personal spending in excess of $50 million per year), Sheldon will need $200 million in order to pay politicians $100 million. There will be no escaping this. Whether Sheldon simply writes a check from available funds, works and earns wages, sells appreciated assets, borrows money, or uses gifts from others, he will have to

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88. For the history of the top marginal rate bracket under the income tax, see *Table 23: U.S. Individual Income Tax: Personal Exemptions and Lowest and Highest Bracket Tax Rates, and Tax Base for Regular Tax, Tax Years 1913–2015*, IRS, https://www.irs.gov/statistics/soi-tax-stats-historical-table-23 [https://perma.cc/F6SM-C4XB].

pay $100 million to the government for the privilege of making his $100 million political contribution. Sheldon will have to start with $200 million, which he can pull out of his unlimited tax-favored savings account. He will pay 50% of that amount, or $100 million, to the government, leaving $100 million for Sheldon's favorite politicians and political causes.

At a 70% rate, Sheldon would have to start with $333 million, paying $233 million, or 70%, for the privilege of the $100 million of personal spending. And at a 90% marginal tax rate—bearing in mind that this is simply, and only, on personal spending in excess of $50 million a year—Sheldon would need to pull out $1,000,000,000, one billion dollars. Sheldon would have to pay $900 million, or 90% of the one billion dollars to the government *before* he could give $100 million in political contributions. This would get done without specifically needing to list Sheldon's political gifts—Sheldon would have spent money under a consistent spending tax without his spending qualifying for any kind of deduction as savings. Sheldon's $100 million in political campaign spending will be taxed just the same way as spending on luxury houses, planes, cars, or gold-plated toilets.

D. Summing Up

In addition to taxing all consumption, however sourced, a progressive spending tax changes the discussion about possible marginal tax rates, allowing a return to a more progressive past without running into arguments against disincentivizing work or savings. A consistent progressive spending tax disincentives high-end spending, and only high-end spending: this is something that a reasonable society might well chose to do. A progressive spending tax can have peak marginal tax rates of 50, 70, or even 90%, as the actual income tax has had in its past. Under these rates and a consistent spending tax, things change for Sheldon. A lot.

We have seen above how under the current income tax, Sheldon would need $100 million to make his $100 million political expenditures. Under a consistent spending tax, with plausible rates in a rate bracket applying only to those American households *spending* more than $50 million a year, Sheldon would need between $200 million and $1 billion to afford the same $100 million contribution.

That is a very big change, affecting Sheldon's marginal calculus.

IV.   THE GENERALITY OF THE CASE

This Article began by noting the ever-growing problem of money in American politics, specifically the problem of outsized political contributions

from America's billionaire class. It is a fact that individual Americans are now contributing sums as large as $100 million or more per electoral campaign cycle. It is also a fact that practical, meaningful solutions to the attendant problems have not been forthcoming, despite decades of thought and effort. Where there is money, there is influence. Where there is outsized money, there is outsized influence.

Rather than taking aim directly at the problem in its most particular, readily observable instantiation, by attempting to develop rules specifically limiting mega-political donations, the Article switched perspectives. It looked at the outsized personal consumption of the rich as a *general* problem. It then became easy to see that political expenditures are just an example of the spending patterns of the rich, and also that the current tax system's primary failure is its failure to reach high-end spending. Tax provides a solution to the seemingly hopeless problem of campaign finance reform; campaign finance provides an important case study to reveal the deepest problem of our current tax system, its failure to reach the high-end spending of the rich.

This section adds a normative argument that supports this move. But first we pause to address a compelling skepticism.

A. *On Comparing Apples and Oranges*

We consider a plausible objection at this point, namely that we are comparing an apple, that is, the present, highly flawed income-with-realization tax system, with an orange, that is, a stylized, ideal progressive spending tax. This is true enough. But the arguments presented here regarding tax are quite general. *Any* income tax must include personal consumption in its base, as we have seen above. And how *any* income tax and *any* spending tax in fact tax consumption is not happenstance. The tax structure constrains their ability to reach high-end spending in particular.

There are two structural issues that separate any income tax from the progressive spending tax being proposed: (1) the taxation of the various *sources* for financing present period spending and (2) the nature of the marginal tax rate schedule. On each front, it is clear that the income tax is a highly restricted tool.

Regarding sources, we considered three different sources of paying for spending: labor, capital, and debt. The current income tax struggles mightily with *capital*; there has been a century of failure to tax economic gains from

capital beginning with *Macomber*.[89] There are indeed many proposals for a cure, but none have made the wealthy pay much of anything.[90] Taxing assets as they rise in value without market transactions is simply a difficult technical task. Worse, any income tax will *not* include debt, because borrowing is simply not income under the Haig-Simons or any other definition of "income." This leaves *labor* as the main source of taxable funds used to finance personal spending,[91] but the disincentive effects of high marginal rates on labor effort constrain the income tax.[92]

A spending tax has no such difficulties with taxing the source of present consumption. There is not even much reason to belabor this analytic point: one can see it in the operation of a simple sales tax, another form of the orange. When you buy a good such as a cup of coffee subject to a sales tax, the cashier never asks you where you got the money to pay for it. It does not matter if you pay with cash or credit card, does not matter if the cash came from your paycheck or the credit came from your parents. All money used to consume is taxed. Sources are irrelevant. This has always been one of the most attractive features of a "cash-flow consumed income tax," as the late Professor William D. Andrews called our version of a spending tax,[93] building on the work of Nicholas Kaldor:[94] its source neutrality. Ironically, such neutrality has always been a rallying cry of income tax supporters who seek to tax, in the words of the Sixteenth Amendment, "all incomes, from whatever source derived,"[95] including, in the famous language of *Macomber*, the gains "derived from capital, from labor, or from both combined."[96] But once we shift our gaze to focus on the particular social harm of high-end consumption, even an ideal income tax fails to pick up a major source, debt. A spending tax is fully, generally, source neutral.

This leads to the second structural issue, the nature of the marginal rate schedule. Once again, *any* income tax, because it falls fully and primarily on the gains to labor—wages—in the first instance, will face pressure to maintain moderate tax rates. This is a primary lesson of the optimal income tax literature of the late Nobel Laureate James Mirrlees[97] and others,

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89. *See* McCaffery, *supra* note 58.

90. *Id.*

91. *See* McCaffery, *supra* note 43, at 6–10.

92. *See* McCaffery & Hines, *supra* note 81, at 1038.

93. *See* Andrews, *supra* note 22, at 1120.

94. *See* KALDOR, *supra* note 22.

95. U.S. CONST. amend. XVI.

96. Eisner v. Macomber, 252 U.S. 189, 207 (1920).

97. *See* Jame Mirrlees, *An Exploration in the Theory of Optimum Income Taxation,* 38 REV. ECON. STUD. 175, 207–08 (1971).

popularized by the likes of Arthur Laffer.[98] But once again, these arguments do not apply with the same force to marginal tax rates under a consistent *spending* tax. Because rates as high as 90% could be avoided by the wealthy "simply" continuing to save, a social good, the purely economic efficiency losses under a progressive spending tax are muted.[99] Put another way, when a rich person decides not to *spend* because of the tax system, there is not the same harm to society—indeed, we are suggesting that there is a social *benefit* to curtailing high-end spending—as there would be if the rich person decided to cease engaging in the socially productive acts of work or savings.

So while we are indeed comparing an apple to an orange, we are not doing so by sleight of hand. No apple could reach all personal spending, as any orange would. And while high rates under the apple might lead us to cut off our noses to spite our face—might, that is, lead people to work and save less—oranges give us hope for a win-win outcome. This Article follows that hope.

B. *The General Problem of High-End Spending*

The progressive spending tax works in a fully general way. There is no need, within the tax system, to particularly itemize political contributions. The money to make them had to come from somewhere, and all such "wheres" lead to Income under the rearranged Haig-Simons definition:

$$[5]\ Consumption\ =\ Income\ -\ Savings.$$

Whatever Sheldon uses as the proximate source of his $100 million, it has to come from some place: current period earnings, savings withdrawn from the universal tax-favored accounts, debt, gift. All sources are Income. And because political expenditures are not Savings allowed to take place within the tax-favored accounts (just as, today, one cannot make political contributions from within a tax-favored IRA or qualified pension plan), there is no deduction for them, and they end up in the residual, taxed, category of Consumption. This will also be true, for just the same reasons and in just the same way, for Sheldon's purchases of more homes, yachts, or gold-plated toilets. All that matters is the price tag, not the item's description.

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98.   Elizabeth Popp Berman, *Trump Is Giving Arthur Laffer the Presidential Medal of Freedom. Economists Aren't Smiling.*, WASH. POST (June 1, 2019, 3:42 PM), https://www.washingtonpost.com/politics/2019/06/01/trump-is-giving-arthur-laffer-presidential-medal-freedom-economists-arent-laughing/ [https://perma.cc/KC6J-SY9W].

99.   *See* McCaffery & Hines, *supra* note 81, at 1056–57, 1063–64.

The generality of the case helps to obviate the need even to consider First Amendment objections to the tax reform proposal for its—potentially massive—increase in the net cost of political expenditures. We would be taxing consumption, and much consumption—not just or even paradigmatically political expenditures—has a speech component.[100] But this can hardly be made into a plausible Constitutional objection, especially given the simple fact that we are taxing consumption today, under the income tax.[101] We are just not taxing consumption very well, and loopholes allow mega-donors like Sheldon to avoid paying any tax on much particular spending, including political contributions.[102] A consistent spending tax aims at all spending or, equivalently, consumption. Its rate structure can reflect this choice of focus. High-end spending will be taxed at high-end rates.[103] This will include but in no way be focused on or limited to political spending. The distinctions that the progressive spending tax makes are ones of degree—the general level of one's spending or lifestyle—not kind.

In terms of mounting any kind of challenge on the grounds that moving to a progressive spending tax somehow impermissibly infringes on protected First Amendment rights, it also bears noting that there is only one change needed to convert the present, flawed income tax into a consistent spending tax: an unlimited deduction for savings. That is not a structural reform targeted at speech.

Still, the generality of the case, analytically helpful in sparing the need for extensive First Amendment analysis, requires a separate normative defense. That is, if we are going to tax all of the high-end spending of the rich, and not just their political expenditures, at high-end rates, we should be willing to justify taxing all of the high-end spending of the rich, and not just their political expenditures, at high-end rates. Can we?

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100. *See* Grosjean v. Am. Press Co., 297 U.S. 233, 250 (1936) (customary taxes on newspapers allowed; *higher* burdens on them not). The progressive spending tax has no *special* rate on political contributions or any other particular form of personal spending. Its distinctions are made on the basis of the level of overall personal spending: it is a matter of degree, not kind.

101. U.S. CONST. amend. XVI; *see also* McCaffery, *supra* note 43, at 11, 20–21. By taxing income and allowing deductions for savings, the income tax has become a consumption tax for all except those who save more than $19,000 of payroll income each year, which is a very small portion of Americans.

102. McCaffery, *supra* note 43.

103. Historical marginal income tax rates have been as high as 94% in the past, so the suggestion of rates this high again on extreme consumption is hardly extreme of itself. *Historical Highest Marginal Income Tax Rates*, TAX POL'Y CTR. (Feb. 4, 2020), https://www.taxpolicycenter.org/statistics/historical-highest-marginal-income-tax-rates [https://perma.cc/3G7Q-T5NS].

Yes, we can. These are arguments we have pursued elsewhere, in making the general case for a progressive spending tax, so we will not repeat them at length here.[104] But the arguments rest on rather commonsensical propositions, such that it is better to tax "bads" than "goods." Indeed, "sin taxes" have often been used to control harmful activities, such as smoking or drinking alcohol.[105] High-end spending of the rich can also be seen as a "bad," if not a "sin," in that it can be harmful to others, as the case of mega-political donations well illustrates: here, the personal spending of the rich distorts our very democracy and its processes. But *any* outsized spending of the rich generates harms. It distorts the allocation of resources towards luxury goods, and away from middle class wants and needs. It incites envy, driving up what Adam Smith referred to as the price of "appearing in public without shame."[106] Perhaps most importantly, the outsized spending of the rich represents a failure of the most privileged class to save, depriving society of capital that other classes, and the government itself, struggle to maintain.

There is also this: the government must tax *something*. As it is, we are taxing the wealthy very little if at all.[107] In this age of inequality, it is a social imperative to tax the rich more. But *what* of the rich should be taxable? The idea of a progressive spending tax is that it is the wealthy's spending, or consumption, that should be taxed. This is, simply, a better time and activity to tax than the work, savings, investment, or beneficence of the rich. The latter are socially productive activities we ought to encourage; the former—the spending of the wealthy—is the activity causing social harm.

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104. *See* McCaffery, *A New Understanding*, *supra* note 61.

105. *Are Sin Taxes Healthy for State Budgets?*, Pew Charitable Tr. (July 19, 2018), https://www.pewtrusts.org/en/research-and-analysis/reports/2018/07/19/are-sin-taxes-healthy-for-state-budgets [https://perma.cc/Y9AM-SG5B].

106. *See* Adam Smith, An Inquiry into the Nature and Causes of the Wealth of Nations 393 (R.H. Campbell et al. eds., Oxford Univ. Press 1976) (1776):

> By necessaries I understand not only the commodities which are indispensably necessary for the support of life, but whatever the custom of the country renders it indecent for creditable people, even of the lowest order, to be without. A linen shirt, for example, is, strictly speaking, not a necessary of life. The Greeks and Romans lived, I suppose, very comfortably, though they had no linen; but in the present times, through the greater part of Europe, a creditable day-labourer would be ashamed to appear in public without a linen shirt, the want of which would be supposed to denote that disgraceful degree of poverty, which, it is presumed, nobody can well fall into without extreme bad conduct. Custom, in the same manner, has rendered leather shoes a necessary of life in England.

107. *See* McCaffery, *supra* note 58, at 306.

For, finally, another way to see the general advantages of a progressive spending tax is to look at the matter through the lens of what incentives a tax system generates and what behaviors it shapes. All taxes have incentive effects, good or bad. An income tax discourages work and savings; the wider tax system discourages marriage and inter-generational altruism.[108] At the same time, the current tax system, as we have seen, *encourages* and even *subsidizes* (as we considered with Sheldon and the estate tax) outsized-spending, including outsized spending on political campaigns. A progressive spending tax, in contrast, only discourages the high-end personal spending of the rich. It allows the rich to continue to save, and even to pass on wealth to their children—which fortunate heirs will be taxed when, but only when, they spend. The progressive spending tax gets back to an idea set forth by the British philosopher Thomas Hobbes, that we should tax people not when they contribute to a "common pool" of social capital, but when they *withdraw* from that pool, to use the wealth on themselves.[109]

These are, again, general arguments for a tax system that will deter high-end spending in part at the "cost," such as it is, of encouraging or allowing high-end savings. A progressive spending tax allows private wealth to be built up but looks askance at the wanton personal use of such wealth. There are compelling and compellingly general reasons to do so, perhaps especially when we consider the case of large scale personal political spending.

V.   FINAL THOUGHTS AND HOPES

"[I]t is said that hunger and poverty make men industrious, and that laws make them good. There is no need of legislation so long as things work well without it, but, when such good customs break down, legislation forthwith becomes necessary."

Niccolo Machiavelli, *Discourses on Livy*[110]

Human nature being human nature, many Americans have become spectacularly wealthy. And, human nature being human nature, many of these wealthy people are spending huge sums to influence our nominally

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108. The gift and estate tax is a tax on inter-generational altruism. For a discussion of "marriage penalties" in the law see EDWARD J. MCCAFFERY, TAXING WOMEN (1999).

109. As Hobbes also argued in Leviathan, chapter 30: "For what reason is there that he which laboureth much, and sparing the fruits of his labour, consumeth little, should be more charged than he that living idly, getteth little, and spendeth all he gets; seeing the one hath no more protection from the Commonwealth than the other?" THOMAS HOBBES, LEVIATHAN 229 (J. C. A. Gaskin ed., Oxford Univ. Press 2009) (1651).

110. NICCOLO MACHIAVELLI, THE DISCOURSES 112 (Bernard Crick et al. eds., Penguin Group 2003) (1531).

democratic politics—to buy politicians or political offices or laws. There is little hope of changing the facts of human nature. People will continue to be rational, and rational people will continue to incur marginal costs to generate larger marginal benefits. That is what being rational means. As long as the marginal benefits from campaign contributions exceed their marginal cost, the mega-rich like our Sheldon will continue to make them.

We cannot change the facts of human nature. But we can change the marginal costs that humans face in doing business, even as we wait for that business—the business of governing our great democracy—to become less prone to capture by the rich. When it comes to the nexus between money and politics, good customs have broken down. Things are not working well without legislation. Legislation forthwith has become necessary. Rich people spending immense sums of money on politics unchecked is a "bad." Why not use the same legislative strategy against this "bad" that America has used, repeatedly, over centuries, against lower class "bads" like alcohol and tobacco? Why not, that is, tax high-end spending?

Once we have come to see the extremely high-end political spending of billionaires as a problem, and as a subset of a problem of extremely high-end spending of any non-public-regarding sort, a legislative solution emerges. We can indeed change the costs of doing business, by raising taxes on—and only on—high-end spending. A progressive spending tax could increase the actual, bottom-line cost of political expenditures by the wealthy as much as ten-fold. That's a law that could make even the most industrious among us good.