

Historical evolution of income tax in France and the US

Arthur Jatteau

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Some definitions

- Usually, the rates presented are the marginal tax rate, which is the tax rate that applies to the last dollar (or to the last brackets) of the tax base. Normally, it increases as income increases. We have to distinguish it from the average tax rate.
- Some of the modern income tax systems are proportional (everybody pays the same percent of her income), but most of them are progressive (which means that the average tax rate increases with the income). If the tax rate is progressive, the average tax rate will be lower than the marginal tax rate.



Until 1914

- The french fiscal system was exceptionnaly stable from 1792 to 1914.
- There were only 4 direct taxes ("les quatres vieilles") which were based not on incomes but on several index.
- The weight of these taxes was remarkably low for the top incomes ("accumulation en paix").
- Nevertheless, several taxes were implemented, like the "impôt sur le revenu des valeurs mobilières" (1872) or the "impôt progressif sur les successions" (1901).



Creation

- The (progressive) income tax was created in 1914. But at its beginning, only 2 % of the households had to pay it, and the top marginal tax rate was only... 2 %.
- The tax rates increase several times during the war. At its end, the rates were defined by "average tax rate" (this is not the case in France since 1942), which is more simple to understand what people pay.



Until 1944

- There is a new born of the income tax after the war in 1920. Because of the war damages, the government decided to maintain this income tax which higher tax rate.
- During these years, the income tax varies a lot. The top income tax rate increased from 2 % in 1915 to 90 % in 1924. It was even decided by the right !
- The "Front Populaire" decided to increase notably the tax rates, which were established in "average tax rate" and not in "marginal tax rate".



Since WW2

- A law in 1945 lays the foundations of the modern income tax :
 - 1 The "familal quotient" allows families to get some reductions if they have children.
 - 2 The system was based on marginal tax rates. The top income tax rate was remarkbly stable until 1998 (55-65 %). But it decreased last years (today it's only 40 %).



Today

- There are 5 different marginal tax rates (from 0 % to 40 %). 36 millions "foyers fiscaux" exist, but only 20 millions are subject to the income tax.
- They pay 51 billions (17 % of the state budget), which is less than the VAT.



Origins

- In order to pay for its war effort in the American Civil War, the United States government imposed its first personal income tax in 1861. But the tax rates were low.
- But in 1895, the federal income tax was declared unconstitutional by the United States Supreme Court.



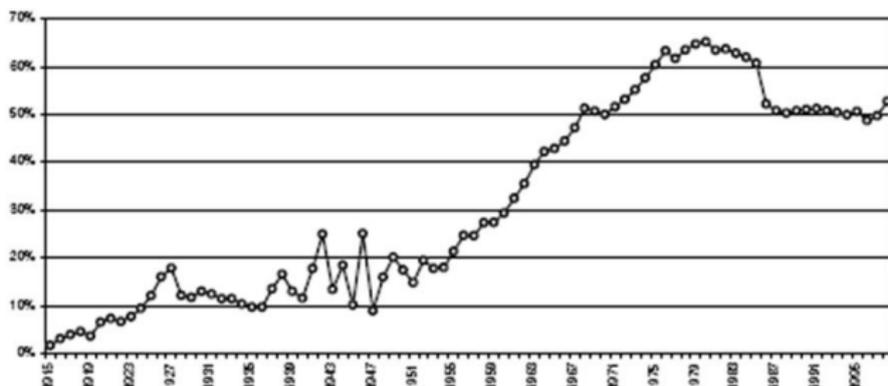
Sixteenth Amendment

- In response to the Supreme Court decision in the Pollock case, Congress proposed the Sixteenth Amendment, which was ratified in 1913 and which states : "the Congress shall have power to lay and collect taxes on incomes, from whatever source derived, without apportionment among the several States, and without regard to any census or enumeration".
- Congress enacted an income tax in 1913, levying a 1% tax on net personal incomes above \$3,000, with a 6% surtax on incomes above \$500,000.
- Today, there are 6 different marginal tax rates (from 10 % to 35 %). So in the US, everybody pays income tax (it's not the case in France).



Fraction of population subject to income tax

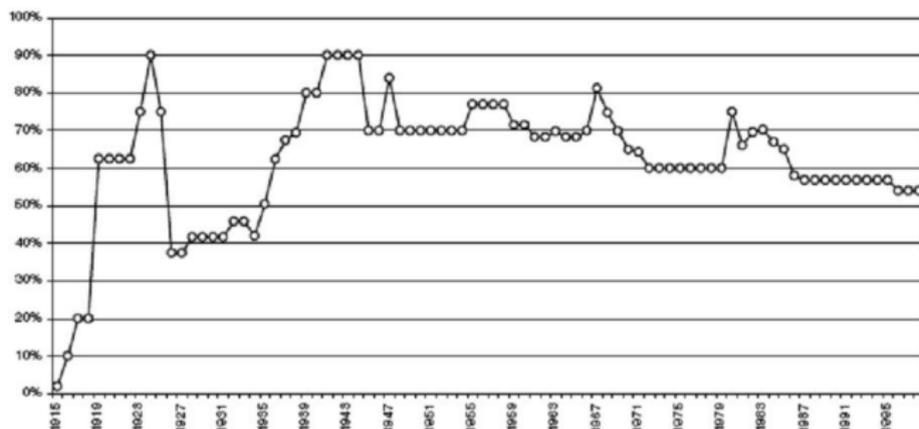
Graphique 5-1 : La proportion de foyers imposables à l'impôt sur le revenu de 1915 à 1998





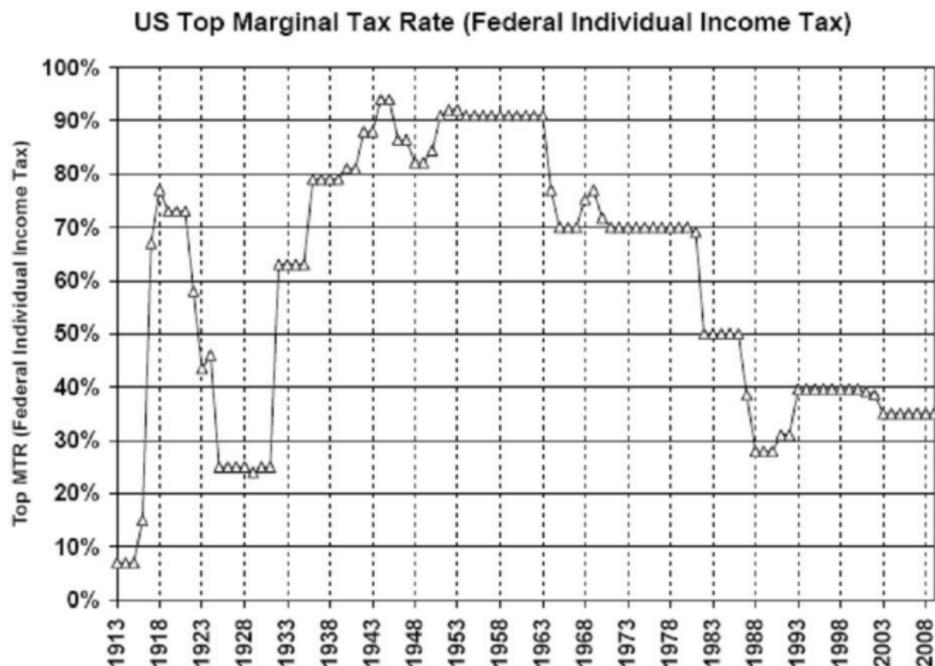
Top marginal rate in France

Graphique 4-1 : Le taux marginal supérieur de l'impôt sur le revenu de 1915 à 1998





Top marginal rate in USA





The scarcity of the increases

- The increases of the income tax were extremely scarces. The way to massify the income tax was not to say it clearly, but was to not adjust the different thresholds to inflation.
- There were only 3 "real" (= assumed) increases of the income tax in France (1920, 1936 and 1981).
- Except these points, according to Piketty, to sum up, we can say that the right government slightly decrease the income tax, since the left ones... don't do anything !



A mass tax I

- In France, between 1914 and 2010, the income tax became a "mass tax". At its becoming, the income tax affects only the top incomes. In 1915, only 2 % of the households had to declare what they earned. It's only after the WW2 that they were more than 20 %.
- At the beginning, they were only few to pay, and for people included in the "classe moyenne" (P90-P95), they payed almost nothing. For example, between 1915 and 1940, the average income tax rate was always below 0,5 % of their income. During this period, the income tax was built for the richest (the "200 families"). People included after P99 typically payed 90 % of the total income tax at this time.

A mass tax II

- After WW2 and until 1970's crisis, the income tax progressively became a mass tax. This process ended with the crisis and the fraction of population subject to income tax, which increased until 70 % during the 1970's, fell down at 50 % during the 1990's. In 2008, it's more about 55 %.



The (statistical) disparition of the top incomes

- The threshold above which the top income tax rate was applicated has been divided by 9 since 1936. It means not only that more and more people payed the income tax, but it also means that the philosophy of the tax has changed.
- Between the world wars, the top income tax rate was applicated on incomes which were 200 times higher than the average income. Today, it's only about 6 times higher. The top income tax rate had been popularized.



A tax which remains concentrated

- If the income tax is payed by more people than at its beginning, it is still progressive. The 10 % of the richest households always pay more than half of the total income. A the end of the 1990's, they pay around 70 % of the total income tax.
- The average income tax rate for the 90 % of the poorest household is only 3 %, and it is 8 % for the people included in P90-P95.



Conclusion

- The presentation of the income tax by marginal rates complicate the understanding of what we pay. Maybe, it could be an interesting option to compute the tax in avaral rate.
- In France, the income tax clearly became a "mass tax" since WW2. In US, it's the case "by definition".
- What we learnt, it's also the decrease of the top income tax rate these last 40 years. It could be a good way to think that one day, the top marginal tax rate, both in US and France, was 90 %...