The Smallholder Society

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I. Introduction

In recent years, the idea of promoting widespread property ownership in the United States by means of public policy has enjoyed a renaissance across the political spectrum. George W. Bush and other American conservatives have borrowed the term "ownership society" from Margaret Thatcher's Britain and employed it to justify a range of proposals from the partial privatization of Social Security to individual health savings accounts. On the Left, thinkers like Michael Sherraden and Bruce Ackerman, reviving a tradition that goes back to Thomas Paine, have proposed granting every citizen a substantial capital endowment.[1] More modest versions of this proposal have been enacted in Britain, in the form of "child trust funds," and introduced as legislation in the U.S. Congress. Promoters present policies to increase savings, such as tax-favored individual retirement accounts (IRAs) and individual development accounts (IDAs), as methods of raising the U.S. savings rate, or decreasing the gap in asset ownership between white and non-white Americans. Whether these proposals emanate from the Right, Left, or Center, they are often justified by invoking historic U.S. policies to promote property ownership, from the Homestead Act[2] in the nineteenth century to the federal home mortgage interest deduction in the twentieth.

Progressives should welcome the new interest in using public policy to promote widespread asset ownership. But there is a danger that this focus on incremental improvement will sap the potential for a major rethinking of U.S. policy. In particular, there is a growing danger that the litany of public policies to promote private asset ownership will be invoked opportunistically to provide a new and trendy argument for familiar conservative and liberal policy proposals. Conservatives and libertarians already employ the rhetoric of the "ownership society" to justify tax cuts and other measures that they formerly justified on the basis of other arguments. In response, a growing number of progressives are jumping on the ownership society bandwagon, redefining "ownership" to include

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[1] *See* Bruce Ackerman & Anne Alstott, The Stakeholder Society (1999); Inclusion in the American Dream (Michael Sherraden ed., 2005); Michael Sherraden, Assets and the Poor (1991).

[2] In 1862, Congress passed the Homestead Act, granting 160 acres to any American who would settle the land and improve upon it, usually through farming.

concepts remote from ordinary notions of individual property, such as social insurance entitlements and public education.

The idea of an ownership society is too important for progressives to allow it to degenerate into a fashionable label slapped onto familiar public policies. I will begin by discussing the deep roots of the belief that American democracy depends on widespread ownership of property among citizens who share a rough equality of condition. I will then argue that taking seriously the idea of the twenty-first-century United States as a real ownership society—a smallholder society—requires a radical restructuring of taxation. A genuine ownership society cannot be achieved by a single gimmick, be it the privatization of Social Security or an inadequate and symbolic child trust fund. In the absence of a consensus favoring serious reforms to promote a property-owning democracy, the newly fashionable "ownership society" will be nothing more than a Potemkin Village.

II. The Relationship Between Property and Democratic Republicanism

The idea that a society with a reasonably equal distribution of property is most likely to establish and maintain a democratic form of government has an ancient pedigree. Aristotle argued that democratic regimes were most likely to succeed in societies dominated by a large middle class.[3] During the Renaissance, both Machiavelli and the English republican author James Harrington made the same argument.[4] The idea that democratic government and civil liberty required a population dominated by self-reliant "yeomen" farmers, self-employed craftsmen, and small business owners passed into American political thought and discourse from English radicalism. John Adams argued in 1776 that "power always follows property." For this reason, Adams proposed "to make the acquisition of land easy to every member of society" or else "to make a division of land into small quantities, so that the multitude may be possessed of landed estates."[5] Ezra Stiles agreed: "We may as well think to repeal the great laws of attraction and gravitation, as to think of continuing a popular government without a good degree of equality among the people as to their property."[6] Noah Webster wrote in 1790:

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[3] *See* Aristotle, Politics bk.4, ch.11, at 119–21 (C.D.C. Reeve trans., Hackett Publ'g Co. 1998).

[4] *See* James Harrington, The Commonwealth of Oceana and A System of Politics 33 (Cambridge Univ. Press 1992) (1656); Niccolo Machiavelli, Discourses (Penguin Classics 1984) (1531).

[5] Letter from John Adams to James Sullivan (May 26, 1776), *in* 9 The Works of John Adams 375, 376–77 (Charles Francis Adams ed., AMS Press 1971) (1854).

[6] Edmund S. Morgan, The Gentle Puritan: A Life of Ezra Stiles 344 (1962).

> The basis of a democratic and a republican form of government is, a fundamental law, favoring an equal or rather a general distribution of property. It is not necessary nor possible that every citizen should have exactly an equal portion of land and goods, but the [inheritance] laws of such a state should require an equal distribution of intestate estates, and bar all perpetuities.[7]

Senator Thomas Hart Benton of Missouri claimed in 1826: "The freeholder . . . is the natural supporter of a free government, and it should be the policy of republics to multiply their freeholders, as it is the policy of monarchies to multiply tenants. We are a republic, and we wish to continue so: then multiply the class of freeholders . . . ."[8] Franklin Roosevelt agreed in 1936:

> In our national life, public and private, the very nature of free government demands that there must be a line of defense held by the yeomanry of business and industry and agriculture . . . . Any elemental policy, economic or political, which tends to eliminate these dependable defenders of democratic institutions, and to concentrate control in the hands of a few small, powerful groups, is directly opposed to the stability of government and to democratic government itself.[9]

A. *How Does Equality of Property Bolster Democratic Republicanism?*

What exactly is the connection between property and democratic republicanism? One tradition holds that economic independence is a necessity if citizens are to perform their duties in a democratic republic as voters and jurors. The idea is that "paupers" and wage earners, out of economic necessity, are more easily bribed and more likely to sell their votes in elections and juries. This thesis served as a justification for property requirements for voting and office-holding in many countries until the nineteenth or twentieth centuries.[10]

Another argument holds that, in a country in which property is concentrated in a few families, class war between the many and the few will destroy or make impossible a democratic republic. The wealthy, fearing

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[7] Noah Webster, Miscellaneous Remarks on Divizions of Property . . . in the United States (1790), *reprinted in* The Founder's Constitution (Philip B. Kurland & Ralph Lerner eds., University of Chicago Press 2000), *available at* http://press-pubs.uchicago.edu/founders/documents/v1ch15s44.html.

[8] 2 Reg. Deb. 727 (1826).

[9] President Franklin Delano Roosevelt, Address at the Texas Centennial Exposition (June 12, 1936), *available at* http://www.presidency.ucsb.edu/ws/print.php?pid=15302.

[10] *See* Alexander Keyssar, The Right to Vote 3 (2000).

redistribution, will prefer authoritarian government to electoral democracy, while the poor majority, out of frustration, will support demagogues or revolutionaries promising greater equality of wealth and opportunity, or, alternately, turn to crime. In the seventeenth century, Harrington made this argument: "For to make a commonwealth unequal is to divide it into parties, which sets them at perpetual variance, the one party endeavoring to preserve their eminence and equality, and the other to attain equality . . . ."[11]

In the United States, another argument, resting on natural rights, has perhaps been the most influential among ordinary Americans, if not intellectuals. John Locke famously claimed that everyone has inalienable rights to life, liberty and property. In the Declaration of Independence, Thomas Jefferson changed "property" to the "pursuit of happiness."[12] But many Americans, both in Jefferson's time and later, have endorsed the older Lockean claim, associated with the labor theory of value, that an individual has a natural right to the results of his own labor.

The natural rights theory of property differs from the independent-citizen and class-war theories by reversing the relationship between property and democratic republicanism. For natural rights theorists, government serves property, property does not serve government. Property is good not because it helps the democratic republic by reducing the likelihood of political corruption or class war, but because it is inherently good; any government, be it a democratic republic or not, is legitimate only to the extent that it upholds the right to labor to acquire property. Property, in turn, is elevated to the status of a natural right like life and liberty. Most political philosophers dismiss natural rights theories of all kinds, and academic economists long ago rejected the labor theory of value. But the claim that a right to property is a necessary concomitant to the fundamental rights of life and liberty retains its force in the United States and elsewhere.

The argument that widespread property ownership strengthens democracy by averting class war has recently received powerful support from the research of Carles Boix, a political scientist at the University of Chicago. In *Democracy and Redistribution*, Boix argues that comparative international history supports a connection between the kind and distribution of property and political regimes. Liberal democracy first evolved in agrarian societies with a highly egalitarian distribution of farmland, like Switzerland, Norway, and the nineteenth-century northern United States. Today, liberal democracy is strongest in countries with widespread

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[11] Harrington, *supra* note 4, at 33.

[12] Jefferson believed that land ownership was a social convention, not a natural right, and wrote that it is "a moot question whether the origin of any kind of property is derived from nature at all." Letter from Thomas Jefferson to Isaac McPherson (Aug. 13, 1813), *in* 13 The Writings of Thomas Jefferson 333, 333 (Thomas Jefferson Mem'l Ass'n eds., 1903).

ownership of assets, particularly assets that are difficult for governments to confiscate. Authoritarian governance is most likely in regimes with concentrated asset ownership, particularly if the assets are natural resources like oil. Boix argues that, in societies with widespread asset ownership, the poor are less likely to threaten the rich, who in turn are less likely to look to authoritarian government to protect their property from redistribution.[13]

B. From the Citizen-Producer to the Citizen-Consumer

Outside of the slave South, the early American republic was the model of a smallholder society. In mid-eighteenth-century Britain, two-thirds of adult white males were landless and only one-third owned land; in the American colonies, the proportions were exactly the reverse.[14] In his *Letters from an American Farmer*, J. Hector St. John de Crèvecoeur wrote: "Europe contains hardly any other distinctions but lords and tenants; this fair country alone is settled by freeholders, the possessors of the soil they cultivate, members of the government they obey, and the framers of their own laws . . . ."[15]

Abraham Lincoln, speaking in New Haven, Connecticut, in 1860, contrasted the free labor society of the North with the slave labor society of the South:

> What is the true condition of the laborer? I take it that it is best for all to leave each man free to acquire property as fast as he can. Some will get wealthy. I don't believe in a law to prevent a man from getting rich; it would do more harm than good. So while we do not propose any war upon capital, we do wish to allow the humblest man an equal chance to get rich with everybody else . . . . I want every man to have the chance—and I believe a black man is entitled to it—in which he *can* better his condition—when he may look forward and hope to be a hired laborer this year and the next, [to] work for himself afterward, and finally to hire men to work for him! That is the true system.[16]

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[13] *See* Carles Boix, Democracy and Redistribution (2003).

[14] Alan F. Zundel, Declarations of Dependency: The Civic Republican Tradition in U.S. Poverty Policy 25 (2000).

[15] J. Hector St. John de Crèvecoeur, Letters from an American Farmer 51 (E. P. Dutton 1957) (1782).

[16] President Abraham Lincoln, Address at New Haven, Connecticut (Mar. 6, 1860), *in* 14 The Collected Works of Abraham Lincoln 13, 24–25 (1953). For a further discussion of Lincoln's views, see Gabor S. Borritt, Lincoln and the Economics of the American Dream (1994) and Michael Lind, What Lincoln Believed (2005).

As Lincoln suggests, wage labor was supposed to be a way station on the road to economic independence, either as a small farmer or a small business owner. The youth labored as a hired hand until he could afford his own farm, or labored as a blacksmith's apprentice until he saved enough to set up his own smithy.

The crisis of the yeoman republic came with industrialization. Long production runs produced economies of scale for mass production in giant factories, at the expense of small shops. It was impossible for self-sufficient households or village artisans to compete with large-scale enterprises in making cars, refrigerators, or television sets.

The challenge was to find ways to finance large-scale industrial enterprises. In the United States, some proposed democratic socialism and others proposed populist schemes of cooperative ownership of large enterprises. Instead, corporate capitalism, based on the limited-liability joint stock corporation, prevailed as the major way of structuring the large-scale industrial economy. Limited-liability laws, by limiting the claims of creditors to the assets of a corporation and shielding the personal wealth of investors, provided an incentive for the pooling of private wealth on the large scale needed in an industrial economy. The limited-liability joint stock company is far from perfect; since its invention, it has been plagued by conflicts of interest between managers, on the one hand, and owner-investors and pooled capital, on the other. This capital, furthermore, is frequently used to bribe democratic politicians on behalf of particular enterprises or industries. But for all its faults, corporate capitalism—in conjunction with state capitalism that provides public goods like basic science research and development funds, public infrastructure, and public education—has proven to be a highly dynamic and successful engine of economic progress.

The existence of large-scale enterprises in certain industries did not, by itself, doom the yeoman society of home production and small craft production. Other developments in the twentieth century hastened the downfall of the yeoman society in the United States. Zoning and regulatory changes wiped out many small businesses run from the home, such as backyard poultry businesses. Professional licensing created legal monopolies for certain kinds of work and raised barriers to entry for those fields for those who could not afford expensive and specialized professional education.

These regulatory changes transformed both the social and literal landscape of America. Professional credentialing created a new class divide between the working-class majority with high school and trade school diplomas, and college-educated professionals. Single-use zoning created a landscape segregated by function, with homes in one area and businesses in another. The yeoman jack-of-all-trades was obliterated along with his natural habitat: the home that doubled as a shop or production site.

Rising living standards—chiefly the result of ever-cheaper goods from industrialized manufacturing and agriculture—disguised the long-term trend, which was the proletarianization of American society. A nation of independent farmers became one of dependent wage-earners, in which only around one in ten is self-employed.[17] Strictly speaking, the minority of professionals, like the working-class majority, consists of proletarians who derive their income from selling their labor in the labor market rather than from the ownership of service-performing or revenue-generating assets. When the tiny minority of genuine capitalists capable of living entirely off of their investments is excluded, the U.S. population consists of two types of what nineteenth-century Americans would have called wage slaves: Class A wage slaves (credentialed professionals) and Class B wage slaves (the high school–educated, working-class majority). Neither group can maintain its lifestyle for more than a brief period without a continuous stream of wage or fee income, or government subsidies, supplemented in some cases by private charity.[18]

The very concept of "ownership" was redefined in the twentieth century to fit the realities of this proletarian society. Beginning in the 1920s, the consumer credit revolution changed attitudes about thrift. Today, individuals are said to "own" their homes or cars when in fact many of them are renting the use of these from vendors or lenders. While business encourages consumption by promoting debt, the U.S. government since World War II has regarded maintaining high levels of consumption as one of the goals of economic management. "Middle class" is now defined in terms of levels of income and consumption of goods, rather than in terms of property ownership and self-employment. The American ideal of the largely self-sufficient citizen-producer has been replaced by the citizen-consumer.

C. Modern America as a Smallholder Society: Far from the Ideal

None of this is intended to disparage the achievements of twentieth-century social reform or modern American consumer capitalism. My purpose is to provoke. The United States today is not a capitalist country; it is a country of proletarian wage-earners with a tiny number of true capitalists.

According to a 2003 U.S. Census Bureau report, a majority of Americans in 2000 owned vehicles (85.8%), homes (67.2%), and interest-bearing

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[17] *See* Robert W. Fairlie, U.S. Small Business Admin., Self Employed Business Ownership Rates in the United States: 1979–2003, at 1–2 (2004), *available at* http://www.sba.gov/advo/research/rs243.pdf.

[18] On the basis of 1994 data, Andrew Hacker estimated that the number of Americans capable of receiving a million dollars a year in investment income without working amounted to "about thirty thousand households, one-thirtieth of one percent of the national total." Andrew Hacker, Money: Who Has How Much and Why 227 (1997).

assets at financial institutions, such as savings accounts (65.0%). Beyond cars, homes, and savings accounts, however, asset ownership in the U.S. population drops off sharply. Only 37.5% of Americans own regular checking accounts, and only about a quarter own stocks or mutual fund shares (27.1%) and IRA or Keogh accounts (23.1%). Only 10.8% of Americans own their own businesses, and the numbers are even smaller for those who own rental property (4.9%) or other forms of commercial real estate (6.6%). What is more, the value of the assets owned by the majority of Americans is relatively small. The median value of home equity in 2000 was $59,000, the median value of savings was $4,000, and the median value of checking accounts was $600.[19] Only about one in ten working-age Americans is self-employed.

If the ideal smallholder society is one in which a majority of citizens own modest amounts of a full range of assets, including stocks and bonds, IRAs and Keoghs, and other tax-favored savings accounts, and in which a substantial minority own their own businesses or rental properties, the contemporary United States is far from that ideal.

III. The Ownership Society: Current Approaches

A. *Redefining Ownership*

Some might object that the proletarianization of society is inevitable and even desirable. Inevitable because economies of scale in industrial societies make small units of production inefficient. Desirable because as long as their incomes are higher, people will likely prefer to be well-paid wage-earners with rights to government social insurance rather than poorly paid farmers or small business owners. In this view, self-reliance can and should be sacrificed for affluence and the security guaranteed by government social programs.

This is the argument made by some on what might be called the social democratic Left in the United States. Like European social democrats and democratic socialists, these thinkers are willing to jettison the older republican ideal of self-reliant citizens in favor of the ideal of the middle-class worker-consumer who relies on generous government welfare programs. In itself, this is a legitimate argument. What is not legitimate is the attempt to redefine "ownership" in order to justify all public goods and welfare programs, as distinct from those designed to promote the private ownership of real estate and financial assets.

An example of this attempted redefinition of ownership can be found in a recent publication of the Century Foundation: *Building a Real "Owner-*

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[19] Shawna Orzechewowski & Peter Sepielli, Net Worth and Asset Ownership of Households: 1998 and 2000, at 5 tbl.A (U.S. Census Bureau Current Population Report No. P70-88, 2003), *available at* http://www.census.gov/prod/2003pubs/p70-88.pdf.

ship Society." In an attempt to co-opt the language of the ownership society for the purposes of the social democratic Left, the authors blur the difference between programs to promote private property ownership and practically every other kind of government program apart from defense and infrastructure programs. In a chart entitled "The Assets We Need to Be 'Owners,'" the authors include three categories, which themselves mix genuine personal assets with public goods or welfare programs. For example, "financial" assets include not only homes and savings accounts, but also Social Security and "regulatory protections." Under "income-related" assets, the authors put the "right to collective bargaining" as well as "access to employment." The rubric of "human capital" includes both free public education and "security against costs of illness (insurance)."[20]

The political appeal of repackaging traditional social democratic policies under the newly fashionable "ownership society" label is obvious. But this effort at rebranding does damage to language and logic. If everything from public education to insurance to regulation is relabeled as an "asset" that people "own," then the concepts of assets and ownership are drained of their meaning. The authors themselves seem uneasy about their effort to appropriate the rhetoric of the ownership society, putting both "ownership society" and "owners" in quotation marks.[21]

B. Privatizing Social Insurance

How can the goal of a genuine ownership society be approached? In recent years, two major methods have been proposed: (1) converting social insurance into private property; and (2) giving all Americans "stakes" in the form of personal financial assets. Neither approach can realistically turn America into a genuine smallholder society.

In the name of promoting the ownership society, President George W. Bush has pushed the old libertarian conservative idea of replacing Social Security with private accounts. Partial privatization of Social Security would indeed provide individuals with substantially greater assets. But these assets could be used only as the basis of income in retirement. The actual property available to individuals during their working lives would not increase. There may be good reasons to encourage more private saving for retirement on top of the existing Social Security program. But privatizing Social Security would do nothing to increase the amount and diversity of assets that people between the ages of eighteen and retirement can actually use. If Americans were forced to divert some or all of their present payroll tax to private accounts, the effect of privatization would merely be to replace one type of retirement program financed by a

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[20] J. Larry Brown et al., Building a Real "Ownership Society" 29 tbl.2 (2005), *available at* http://www.tcf.org/publications/retirementsecurity/ownershipsociety.pdf.
[21] *Id.*

mandatory contribution with another, less efficient, retirement program. This is not "ownership."

C. The Stakeholder Society

Another approach to widening property ownership in the United States involves outright government grants of financial assets to every citizen. This idea, which goes back to the British radical Tom Paine in the eighteenth century, has recently been revived by Bruce Ackerman who, in *The Stakeholder Society*, proposes giving every American $80,000 at the age of eighteen, to be spent as the individual chooses.[22]

The Ackerman proposal has no chance of being adopted. Versions of the "stake" idea that are politically palatable tend to involve small sums and often come with strings attached. Britain has enacted a small-scale "baby bond" program that gives each citizen a small amount at birth. In the United States, similar child trust funds, including "Kidsave" and the ASPIRE Act, have been proposed but not enacted.[23]

In light of the deep distrust of welfare in the United States—a distrust rooted in America's citizen-producer republicanism—it is only natural that politicians would want to control how U.S. citizens spend grants of money. But proposals that limit the purposes for which the grant of money can be used are vulnerable to an obvious objection: they are merely government vouchers in disguise. The United States already has programs to help people attend college and obtain mortgages. It makes no sense at all to duplicate the efforts of these programs by adding vouchers, disguised as stakes, that can be used only for college tuition or home ownership. Even worse, in the absence of government-imposed price controls, the influx of public money into private markets would probably inflate the costs of both college and homeownership.

The problem with universal capitalist proposals is simple: those that would make a difference are politically unrealistic, and those that are politically realistic would not make a difference. Ackerman's proposal that every American be given $80,000 at the age of eighteen is an example of the former. The child trust fund legislation that has been introduced in the U.S. Congress, like the Blair government's "baby bonds" in Britain, involves amounts too small to make a serious difference in the overall distribution of property.

If we are serious about creating a smallholder society in the United States, neither privatizing social insurance nor child trust funds can play more than a tiny, token role. We need to try a bolder approach: the revi-

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[22] *See* Ackerman & Alstott, *supra* note 1.

[23] *See* The ASPIRE Act of 2005 (KIDS Accounts), S. 868, H.R. 1767, 109th Cong. (2005); *Saving from Birth: Baby Bonds Are a Great Radical Idea*, Guardian Unlimited, Apr. 11, 2003, http://society.guardian.co.uk/publicfinances/comment/0,,934537,00.html.

sion of the tax code to maximize the chances of ordinary citizens to obtain and maintain small properties of various kinds, from homes to appliances to savings accounts and investments.

IV. Toward a Smallholder Society

A. *Technology and the Citizen-Producer*

Ironically, conventional welfare-state social democracy is too conservative, not too radical. It takes for granted the possibly ephemeral twentieth-century pattern in which most citizens are inadequately compensated wage-earners whose costs of subsistence must be subsidized by the state. Influenced by Marxist and post-Marxist thought, with its focus on the factory proletariat, the thought of the conventional social democratic Left ignores the realms of household production for use and small craft production.

In the early industrial era, people in the United States and other countries often did improve their incomes by voluntarily changing themselves from proprietors (farmers) into proletarians (factory workers). But as a result of productivity growth, industrialized manufacturing, agriculture, and, more recently, clerical services, workers are producing more goods or services with less labor. Most jobs in the United States and other advanced industrial nations are being created in the non-traded domestic service sector, and in personal service fields like health care, child care, education, entertainment, and restaurant food preparation and service.[24]

Most of these new service sector jobs share two characteristics: (1) there are no economies of scale; and (2) many, if not most, can be performed by individuals, with adequate training and assistance, working for themselves. A hospital with 10,000 nurses is not better for each patient than a hospital with 100 nurses; indeed, the quality of patient care is likely to be highest in the case of a single highly attentive nurse visiting a patient at home. And productivity increases in medical technology, like home diagnostic technology, may make it ever easier for individuals to nurse themselves, rather than to rely on paid professionals.

Indeed, advances in technology may result in the partial return of many household functions that were outsourced to factories and businesses in the early industrial era, a process that has been occurring since laundries and laundromats gave way to home washers and dryers after World War II. Home-based diagnostic computers may make visits to clinics unnecessary; home entertainment centers may supersede commercial cinemas; advanced kitchens may permit individuals to prepare restaurant-quality food at home; and advanced media technology may permit home movies

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[24] *See* Bureau of Labor Statistics, *Tomorrow's Jobs* 6, fig.8, http://www.bls.gov/oco/pdf/oco2003.pdf (last visited Nov. 30, 2006).

to be of Hollywood quality. New "fab labs" may even make industrial-quality production of machines and appliances possible in home workshops.[25]

Far from promoting the division of labor, technology may be leveling the playing field between the commercial production of goods and services for sale and the household production of goods and services for use. The rapid growth of the entertainment and restaurant sector in the United States reflects not technological inevitability, but the growing concentration of wealth in the hands of a professional-managerial elite whose lifestyle revolves around dining and entertainment outside of the home—activities that are still luxuries for the majority of Americans who are working class.[26]

The ultimate goal of a smallholder society is not simply providing more people with cash in the form of wages and government subsidies in order to pay for goods and services. Rather, it is to allow more people to be able to buy and maintain assets that generate goods and services for personal use in the non-market family economy. This evolution would not result in a decline in the market economy so much as a shift from finished products to inputs for home assembly—a Home Depot, do-it-yourself producerist economy rather than a shopping mall consumerist economy. In a genuine ownership society, the emphasis would shift from finished consumer goods to capital goods used in home production. Technological trends do not oppose, and may even reinforce, the public policy decision to favor the diversion of wage earnings from purchasing goods and services produced outside the home to purchasing productive assets capable of generating more goods and services within the home.

B. The Power To Tax

The power to tax is the power to destroy. The implications for the project of enabling more citizens to acquire property follows from this fundamental axiom. If we wish to encourage broader ownership of property, then we should impose light taxation, or no taxation at all, both on property and on the labor income necessary to purchase it. If, on the other hand, we want to discourage a smallholder society, then we should tax both property and the labor income needed to buy it.

Measured by this standard, the U.S. tax system at all levels—federal, state, and local—is arguably more hostile than favorable to small prop-

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[25] MIT professor Neil Gerschenfeld's "Fab Lab," including a laser cutter, a vinyl cutter, and a high-resolution milling machine run by open-source software, costs $25,000 with another $10,000 for materials. The costs are likely to fall in the future. *See* Apoorva Mandavilli, *Make Anything, Anywhere* 442 NATURE 862, 862 (2006).

[26] Ajay Kapur has argued that the U.S. economy in recent years has turned into a "plutonomy," in which most growth has been in high-end luxury industries catering to the rich. *See* Philip Coggar, *The Short View Market Comment*, FIN. TIMES, Oct. 19, 2005, at 21.

erty ownership. Indeed, by accident or design, it discriminates in favor of the tiny number of people with substantial financial assets, and against workers seeking to purchase real property out of their earnings.

The disparity between the tax treatment of wage income and investment income is illustrated by a study of 2004 income data by the Institute on Taxation and Economic Policy (ITEP). Total federal personal taxes on wages and other earnings, including Social Security and Medicare payroll taxes as well as income taxes, averaged 23.4%, while the average federal personal tax on investment income was only 9.6%. This meant that taxes on earnings accounted for 88% of total federal personal taxes, although wages and other earnings were only 71% of total personal income. Meanwhile, taxes on investments were only 11% of total personal taxes, even though investment income accounted for 22% of total personal income. The Bush Administration's tax cuts have skewed the situation further still, reducing taxes on earnings by only 9% while slashing personal taxes on investment income by 22%.[27]

C. Reforming Payroll Taxes in the Smallholder Society

Even as the tax code has been rewritten to favor passive investment income and penalize wage income, the burden of payroll taxation has steadily grown. Between 1949 and 1962, the Social Security payroll tax rate rose from 2% to 6%. Following the establishment of Medicare in 1964, which is partly funded by a payroll tax, the combined Social Security and Medicare payroll tax rose to 12.3% by 1980 and was raised further to 15.3% in 1990.[28] For the average American, Social Security and Medicare payroll taxes absorb more earnings (12.7%) than income taxes (10.7%).[29]

The way that Social Security and Medicare are financed is the exact opposite of how they would be financed in a genuine ownership society. Because of the payroll taxes for Social Security and Medicare, wage income is, in effect, taxed more than once. The same wage income is taxed first by the personal income tax, then by the 2.9% Medicare tax, and finally by the 12.4% Social Security tax. Not only is income over $94,200 exempt from the Social Security tax, but investment income does not contribute to these entitlements at all.

Most Americans have to purchase property and accumulate savings and investments out of their after-tax wage income. The reduction of that

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[27] Citizens for Tax Justice, Do Fat Cats Pay Lower Tax Rates than Workers? 1–2 (2004), *available at* http://www.ctj.org/pdf/earnpr.pdf (last visited on Nov. 4, 2006). The full ITEP report, *Federal Taxation of Earnings versus Investment Income in 2004*, can be found at http://www.itepnet.org/earnan.pdf (last visited on Nov. 4, 2006).

[28] U.S. Dep't of the Treasury, *Fact Sheet: Taxes—History of the U.S. Tax System*, http://www.ustreas.gov/education/fact-sheets/taxes/ustax.shtml (last visited on Nov. 30, 2006).

[29] Citizens for Tax Justice, *supra* note 27, at 2.

after-tax income by rising payroll taxes thus reduces the ability of Americans to purchase property, accumulate savings, and make investments. The growing discrimination against wage-earners in favor of investors by the tax code adds insult to injury.

Before the election of Ronald Reagan, the top rate on earned income (50%) was lower than the top rate on investment income (70%). Payroll taxes were lower than today by one-fourth, while the top capital gains tax was more than twice as high (35% compared to 15%).[30] Today, while wage income is taxed at a top rate of 35%, realized long-term capital gains and eligible dividends are taxed at a much lower maximum rate of 15%, and interest on local and state bonds is tax-free. Conservatives may tout the ownership society, but since the election of Ronald Reagan in 1980, the U.S. tax code has become more hostile to smallholders.

The quickest and simplest way to increase take-home earnings that can convert labor into property, in the classic American model, would be to abolish the Social Security payroll tax. This would mean that Social Security would be paid for out of general revenues, which are more progressive and have a far vaster tax base.[31] The argument against financing Social Security out of general revenues—that absent a link between personal contribution and personal benefits, political support for public pensions would collapse—is belied by the experience of other nations that fund public pensions in whole or in part out of general revenues. Indeed, Medicare B is paid for out of general revenues, with no cost to public support for the program. The relatively small Medicare payroll tax, instead of being abolished, might be converted into a mandatory contribution to the purchase of health insurance.

D. Abolishing Property Taxes and Automobile Taxes

If we are serious about a smallholder society, then in addition to abolishing Social Security payroll taxes we should abolish property taxes, at least on modest homes. The property tax, like the payroll tax, penalizes ordinary citizens. The United States does not impose general wealth taxes, which would fall chiefly on the rich minority who own most investments. Instead, states, counties, and cities single out the major form of wealth owned by ordinary Americans: the home. Many jurisdictions also tax the (depreciating) asset that is owned by even more Americans: the automobile.

If property taxes and automobile taxes are retained, then there should be substantial exemptions for modest homes and modest vehicles. Some

[30] *Id.* at 3.

[31] Social Security could be paid for with an earmarked tax other than a payroll tax, rather than out of general revenues. But there is no more reason to fund entitlements with an earmarked tax than there is to fund Pentagon expenditures with an earmarked "Pentagon tax."

states already have homestead exemptions from property taxes for the elderly and other favored groups. Such homestead exemptions should be made universal.

If property taxes are abolished or greatly reduced by means of universal homestead exemptions, then what is to replace the lost revenue? The local public services and schools that traditionally have been funded by property taxes should be funded instead by general revenue-sharing schemes at the state or federal level. Statewide and federal taxes have larger bases and tend to be more progressive in effect.

E. Making Household Investments Deductible

While current payroll taxes and property taxes discriminate against ordinary workers in favor of the few who own large amounts of capital, current tax policy discriminates against household production of goods and services for use, in favor of household production for sale. Today, one can write off the use of a home office, car travel, or investment in household appliances for business purposes, but not for personal purposes. The tax code rewards you for buying a washer and dryer to do your neighbor's laundry for pay, but punishes you if you do only your own laundry. Is the goal a society in which everyone does everyone else's laundry for pay? Not only for-profit but also nonprofit corporations are rewarded while families are punished by the tax system. A nonprofit daycare center gets tax advantages that are denied to stay-at-home parents raising their own children.

If our goal is to maximize modest property ownership by the greatest number of citizens, this policy of penalizing investment for personal use in favor of investment by for-profit organizations or nonprofit organizations should be abandoned. The idea is simple but radical: *households should be treated exactly the same as for-profit and nonprofit entities.*

Individuals and families should be allowed to write off expenses for investments in domestic service-providing assets in their federal (and perhaps also state and local) income taxes: the car (a transportation-providing asset), the home (a shelter-providing asset), and domestic appliances like refrigerators, stoves and ovens, telephones, computers, and Internet access. In a smallholder society, the purchase of these assets for personal use would be treated exactly the same by the tax code as their purchase for use in a for-profit business or a nonprofit organization. The costs that could be written off would be the costs incurred by a modest working-class or lower-middle-class household. The same basic household assets that are given favorable tax treatment could also be protected by bankruptcy law.

F. Exempting Small Savings and Investments from Taxation

Yet another way to use the tax code to promote a true ownership society in the United States is to exempt small savings and other investments from taxation. The tax treatment of savings in the United States is perverse. To begin with, it is regressive: small savers and small investors pay exactly the same capital gains taxes as do the very rich. Even worse, interest and dividend income from savings is added to labor income for the purpose of income taxation.

The first step in reform should be to tax all savings and investment income separately from earnings income. This would require separate reporting for earnings income and capital income each year. Because banks, brokerage houses, and other institutions could automatically report the data for capital income to the IRS, this need not cause a significant increase in paperwork.

The second step should be to exempt small savings and investment income from taxation altogether. Many other countries already exempt small savings from taxation. Belgium and Chile, for example, exempt modest amounts of interest income from taxation. Other countries exempt modest amounts of dividend income from taxation as well.[32] Recently there have been proposals in the U.S. Congress to exempt the first $200 ($400 for joint filers) of interest or dividend income from taxation in 2005 and $400 in years thereafter, to the benefit primarily of low- and middle-income Americans.[33] This reform is essential if the United States is to become a genuine ownership society.[34]

G. The Tax System in a Smallholder Society

These proposals for encouraging more widespread ownership of cars, homes, essential domestic appliances, small savings, and small investments have radical implications for the U.S. tax system. Taxes on earnings and small property of all kinds, including small savings and small investments, would be dramatically reduced. Where would the money for government programs come from?

The progressive taxation of earnings, property, and capital income would still be a source of revenue in a smallholder society. Indeed, today's flat taxes on property, interest, and capital gains would be replaced

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[32] *See generally* AM. COUNCIL FOR CAPITAL FORMATION, SMALL SAVER INCENTIVES: AN INTERNATIONAL COMPARISON OF THE TAXATION OF INTEREST, DIVIDENDS, AND CAPITAL GAINS (1998), *available at* http://www.accf.org/publications/reports/sr-smallsaver-oct1998.html (last visited Nov. 30, 2006).

[33] *See* Simple Savings Tax Relief Act, H.R. 221, 109th Cong. (2005).

[34] *See* Daniel R. Wadhwani, *Protecting Small Savers: The Political Economy of Economic Security*, 18 J. POL'Y HIST. 126 (2006).

by progressive taxation on all three. A modest wealth tax, of the kind levied by some other advanced industrial democracies, should also be considered.

One new source of government revenue should be a federal consumption tax. A value-added tax (VAT) is preferable to a national sales tax because it can raise large amounts of revenue with less visibility and political opposition. Essential goods can be exempted from the VAT.[35]

A federal VAT would encourage the smallholder society indirectly in two ways. First, the revenue it could raise would enable major cuts in federal payroll taxes and, if federal VAT revenues were to be shared with state and local governments, in local property taxes as well. Second, the VAT could be designed to discourage the luxury industries patronized by the affluent minority while sparing the sectors that support a modest, working-class lifestyle. For example, the inputs for home cooking and home entertainment could be taxed sparingly, while heavy taxation could fall on restaurants, hotels, and other luxuries. Family life indirectly might be strengthened as a result.[36]

A move away from payroll and property taxes and toward progressive income and consumption taxes would mark a return to an older American system. Until the mid-twentieth century, progressive income taxes fell only on the rich, and the major taxes that Americans paid were consumption taxes, like tariffs and excise taxes. Such a system is far more compatible with a smallholder society than one that confiscates earnings needed to purchase property, and also taxes property itself.

V. Conclusion

None of the proposals critiqued earlier are capable of moving the United States further in the direction of an ownership society. The partial or complete privatization of Social Security would merely replace an efficient retirement system with an inefficient one, without significantly augmenting earnings or property ownership for working-age Americans. The only child trust fund proposals that the U.S. Congress conceivably might enact would be negligible in amount and, to make matters worse, would probably require that the money be spent for a limited number of purposes, thereby grafting an unwieldy and illogical voucher system onto

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[35] VAT is an indirect tax, in that the tax is collected from someone other than the person who actually bears the cost of the tax. As VAT is intended as a tax on consumption, exports (which are, by definition, *consumed* abroad) are usually not subject to VAT, or the VAT is refunded. *See generally* Paul L.E. Grieco & Gary Clyde, *America Badly Needs a Value Added Tax*, Fin. Times, Apr. 21, 2005, at 15; Europa, Taxation and Customs Union, How VAT Works: General Overview, http://ec.europa.eu/taxation_customs/taxation/vat/how_vat_works/index_en.htm (last visited on Nov. 30, 2006).

[36] Another possibility would be increased reliance on resource or pollution taxes, like a carbon tax. But if the purpose of a tax is to reduce a "bad," then, if successful, the tax would be self-liquidating, and could not serve as a long-term basis for government revenue.

existing programs for helping Americans pay college tuition or buy their own homes.

If we are serious about creating a smallholder society, then our focus should not be on minor and mostly symbolic subsidies or tax-favored savings programs. The major focus should be on bold tax reform.[37] We should rewrite the tax code to promote the wider ownership of multiple kinds of property. We should eliminate taxation of modestly priced cars and abolish property taxes on modestly valued homes. We should reduce or eliminate payroll taxes. We should allow individuals to deduct payments for modest cars, homes, and essential appliances from their income. We should exempt both small savings and small investments from taxation. And we should make up the revenue shortfall with new taxes on luxury consumption along with higher progressive taxation of earnings, savings, capital gains, and overall wealth.

If we are not willing to enact most or all of these reforms, then talk of an "ownership society" will prove to be mere rhetoric, employed to use the imagery of a propertied middle-class society in order to hide the reality of a proletarian nation.

[37] Many policies in addition to tax policies could promote the goal of an ownership society, including policies that raise he real wages needed to purchase property; infrastructure-based decentralization programs, which would make cheaper real estate accessible to more Americans; and research and development undertaken by commercial enterprises, government, and universities, that lowers the costs of essential goods and services.