GROVE CITY COLLEGE

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ARTICLES

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The editors strongly prefer articles under 15,000 words in length, the equivalent of 50 *Journal* pages, including text and footnotes. The *Journal* will not publish articles exceeding 20,000 words, the equivalent of 60 *Journal* pages, except in extraordinary circumstances.

To facilitate our anonymous review process, please confine your name, affiliation, biographical information, and acknowledgements to a separate cover page. Please include the manuscript's title on the first text page.

Please use footnotes rather than endnotes. All citations and formatting should conform to the 20th edition of *The Bluebook*.

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GROVE CITY COLLEGE

JOURNAL OF LAW & PUBLIC POLICY

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GROVE CITY COLLEGE

Grove City College was founded in 1876 in Grove City, Pennsylvania. The College is dedicated to providing high quality liberal arts and professional education in a Christian environment at an affordable cost. Nationally accredited and globally acclaimed, Grove City College educates students through the advancement of free enterprise, civil and religious liberty, representative government, arts and letters, and science and technology. True to its founding, the College strives to develop young leaders in areas of intellect, morality, spirituality, and society through intellectual inquiry, extensive study of the humanities, and the ethical absolutes of the Ten Commandments, and Christ's moral teachings. The College advocates independence in higher education and actively demonstrates that conviction by exemplifying the American ideals of individual liberty and responsibility.

Since its inception, Grove City College has consistently been ranked among the best colleges and universities in the nation. Recent accolades include: The Princeton Review's "America's Best Value Colleges," Young America's Foundation "Top Conservative College," and U.S. News & World Report's "America's Best Colleges."

GROVE CITY COLLEGE JOURNAL OF LAW & PUBLIC POLICY

The *Grove City College Journal of Law & Public Policy* was organized in the fall of 2009 and is devoted to the academic discussion of law and public policy and the pursuit of scholarly research. Organized by co-founders James Van Eerden ’12, Kevin Hoffman ’11, and Steven Irwin ’12, the *Journal* was originally sponsored by the Grove City College Law Society. The unique, close-knit nature of the College’s community allows the *Journal* to feature the work of undergraduates, faculty, and alumni, together in one publication.

Nearly entirely student-managed, the *Journal* serves as an educational tool for undergraduate students to gain invaluable experience that will be helpful in graduate school and their future careers. The participation of alumni and faculty editors and the inclusion of alumni and faculty submissions add credence to the publication and allow for natural mentoring to take place. The *Journal* continues to impact educational communities around the country and can now be found in the law libraries of Akron University, Regent University, Duquesne University, the University of Pittsburgh, and Pennsylvania State University. The *Journal* has been featured by the Heritage Foundation and continues to be supported by a myriad of law schools, law firms, and think tanks around the nation.

EDITOR'S PREFACE

Dear Esteemed Reader,

This volume of the *Grove City College Journal of Law & Public Policy* is the tenth we have published since our inception nearly ten years ago in the spring of 2010. The *Journal* has always been and always will be an entirely student-led publication. This is both a distinctive of our organization and a great challenge. As one of the only student-led undergraduate law journals in the nation, we must contend with a rapid rate of turnover amongst our staff. Most executive editors are on the board for two to three years at most before they graduate. This year, all the executive editors working for the *Journal* undertook new roles.

This publication you are holding in your hands is the result of countless hours of hard work throughout the last fifteen weeks of this semester from our team of twenty-five student editors and our array of authors. Since the start of the spring semester this January, we have been working feverishly to solicit and edit high-caliber articles for Volume 10.

This volume marks the second edition we have published and disseminated during my first year as the Editor-in-Chief. After numerous production delays last semester, due in part to the staffing changes of our organization, we finished the production of Volume 9. That volume was an opportunity for us to learn and grow as a team as we considered our plans for finishing and releasing Volume 10 on time. I hope to codify much of what we have learned this year so the future leaders of the *Journal* can begin each publication cycle with confidence and direction.

Learning from the past is an integral part of progressing as a civilized society. Prominent British author and Christian apologist, C.S. Lewis, cautioned against chronological snobbery: "the uncritical acceptance of the intellectual climate common to our own age and the assumption that whatever has gone out of date is on that account discredited." It is important

for thoughtful reflection on the past, to accept the good and learn from the bad as generations come and go. To that end, we have decided to theme this edition "In Retrospect." As such, the articles we selected to publish reflect on past policies, look at precedent established by the Court, consider the shift in the way our culture views the executive branch, and theoretically examine the economics of autocracy.

Beginning with this volume, we chose to establish an overarching theme for the content in each edition that we hope will interest our readers. Our move in this direction is a result of conversations among the current executive board members, as well as with Mr. Jeff Prokovich '89, Mr. Adam Nowland '07, and Grove City College's ninth president, the Honorable Paul J. McNulty '80. As we reflect on our organization and evaluate our dgoal, we feel this move will allow the *Journal* to more effectively serve as a resource and reference to you, our readers, donors, and supporters.

In addition to publishing two volumes this year and implementing the concept of themed publications, we also decided to reestablish our release presentation at the annual Institute for Faith & Freedom Conference (formerly Center for Vision & Values) this past April. Following introductions by myself and our faculty advisor, Dr. Caleb Verbois, Luke Leone '18 presented his article, "Compact Theory & Modern Nullification," from the previous volume. President McNulty '80 concluded the presentation with an introduction to his article, which you will read in the proceeding pages of this publication.

As I reflect on our work this year, I am encouraged by the positive progress we have made and look forward to spending my fourth and final year with the organization solidifying the publication process and working toward our next edition. On behalf of our entire editorial team, I would like to thank everyone who has played a role in the success of this publication—our associate editors, our faculty advisor, our authors, the administrators

in the Office of Institutional Advancement, the staff from the Institute for Faith & Freedom, the staff in Print Production & Mail Services, and most importantly you, our donors and valued supporters. Without your continued support of undergraduate research and scholarship in the form of financial contributions, our organization would not exist. We would ask that you consider making a gift to Grove City College, designated for the *Journal,* using the enclosed envelope or online at http://giving.gcc.edu/. Your generosity makes our efforts possible.

To make a financial gift, subscribe to the *Journal*, request print copies of past editions, or submit an article, please email us at LawJournal@gcc.edu or visit our website at www2.gcc.edu/orgs/GCLawJournal/. Electronic copies of all previous editions are archived in the HeinOnline database, which maintains over 2,600 law-related periodicals. Again, thank you for your readership and continued support of the *Grove City College Journal of Law & Public Policy*.

Falco Anthony Muscante II ’20

Editor-in-Chief

FOREWORD

Dear Reader,

It is a pleasure to have been asked to write this modest foreword to the latest edition of the *Grove City College Journal of Law & Public Policy*. I arrived at Grove City College in the fall of 1997. It is hard to believe that I have been here over for 20 years. I have seen great things happen here, and met many wonderful faces, students and faculty alike, who have come and gone. One of the most edifying developments on campus during that time was the creation of this special journal, so unique among undergraduate institutions. It is gratifying to see students and faculty alike come together to contribute to the pages of this publication—a testimony to the caliber of people at Grove City College, the camaraderie, and the harmony between students and faculty.

This current issue of the journal features essays by three student contributors—Hannah Schuller, Tegan Truitt, and Tyler Gustafson—plus one faculty member, Professor Richard Snyder, and our president, Paul J. McNulty. Hannah Schuller provides a timely review of U.S. Supreme Court rulings concerning affirmative action in higher education, from the historic Bakke decision to the recent case involving Harvard University. Tyler Gustafson looks at the American presidency today and over time, pondering whether the executive branch and bureaucracy is something altogether completely different from what the American founders envisioned. Has the executive branch really changed all that much? In a departure, Tegan Truitt examines the relationship between democracies and free markets, and challenges the consensus that insists that the two always go hand in hand. He writes on the political economy of "autocratic legislation."

Richard Snyder has contributed a fine essay on tax law, a subject he knows inside and out, as both a practitioner and a professor. We are grateful that he has taken time to illuminate us on the latest machinations involving

the current tax code, particularly the changes under President Trump in the Tax Cuts and Jobs Act of 2017. And finally, Paul McNulty has written on the remarkable moment in history known as the impeachment of President William Jefferson Clinton, a subject he knows inside and out. He was an eyewitness to that extraordinary event, from the impeachment by the House of Representatives in December 1998 to the vote in the U.S. Senate in January 1999, which occurred 20 years ago. I remember lecturing on the Clinton impeachment in my Intro to Politics course here at Grove City College. I was a mere outside observer, with not even a ringside seat. McNulty was inside the ring. This journal today, in the spring of 2019, benefits from his witness testimony.

Given that one of my unintended themes here seems to be 20th-anniversary markers, I will conclude with this thought: Some 20 years before McNulty lived that special history on Capitol Hill, he was an undergrad at Grove City College—like Hannah, Tegan, and Tyler, like Falco Muscante, editor-in-chief of this journal, like Emma Nitzsche, executive articles editor, and like the many fine students on this journal's current editorial board or who have contributed to its pages since its inception a decade ago. One wonders which (or how many) of them will go on to play their own remarkable roles in the history of this country 20 years from now. Which of them may be writing for this journal in the year 2039? What will they see? Truly only Heaven knows.

Until then, we hope you enjoy these essays and this latest edition of the *Grove City College Journal of Law & Public Policy*.

Paul Kengor, Ph.D.
Professor of Political Science
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PASSIONS, POLITICS AND THE REMOVAL OF A PRESIDENT: LESSONS LEARNED FROM THE IMPEACHMENT OF PRESIDENT CLINTON

The Honorable Paul J. McNulty '80, J.D.

Abstract: *The Constitution of the United States provides an extraordinary means for addressing unlawful misconduct by the president: impeachment. This tool has only been advanced through the House of Representatives twice in the history of the United States, first with the impeachment of Andrew Johnson in 1867, and then with William Jefferson Clinton in 1998. Neither president was ultimately removed from office as a result of the impeachment proceedings. Using the Clinton impeachment as a case study, this paper will explore the question of whether the tool of impeachment is ever workable by examining the challenges facing Congress in conducting an impeachment inquiry and two of the key elements necessary for fulfilling this responsibility.*

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* The Honorable Paul J. McNulty '80 spent more than 30 years in Washington, DC as a lawyer in public service and private practice before becoming Grove City College's ninth president in 2014. His time in public service included leading the Department of Justice as the Deputy Attorney General, serving as the United States Attorney for the Eastern District of Virginia in the immediate aftermath of the 9-11 terrorist attacks, and working on Capitol Hill for 11 years. During his service in the House of Representatives, he held the position of Chief Counsel and Director of Communications for the Clinton impeachment proceedings. This position on the House Judiciary Committee 20 years ago serves as the basis for this article.

Introduction

On December 19, 1998, in an unusual Saturday session on Capitol Hill, the U.S. House of Representatives impeached William Jefferson Clinton, the 42nd President of the United States. The House approved two articles of impeachment. By a vote of 228 to 206, the President was charged with committing perjury before a federal grand jury. By a closer vote of 221 to 212, the President was charged with obstruction of justice.

Mr. Clinton was only the second president in U.S. history to be impeached. In 1867, Andrew Johnson was impeached by the House on 11 articles, but subsequently acquitted in the Senate trial by one vote. It may be worth noting that Article X charged that President Johnson was in violation of the "courtesies which ought to exist and be maintained between the executive and legislative branches of the government," and that he attempted "to bring into disgrace, ridicule, hatred, contempt and reproach, the Congress of the United States…by making certain

intemperate, inflammatory and scandalous harangues."[1] Deep political divisions are not new to American politics.

In Federalist No. 65, Alexander Hamilton observed that the misconduct in question in an impeachment proceeding will by its nature be "POLITICAL" because it will be "related chiefly to injuries done immediately to the society itself."[2] He presciently added:

> The prosecution of them, for this reason, will seldom fail to agitate the passions of the whole community, and to divide it into parties, more or less friendly, or inimical, to the accused. In many cases, it will connect itself with the pre-existing factions, and will enlist all their animosities, partialities, influence, and interest on one side, or on the other; and in such cases there will always be the greatest danger, that the decision will be regulated more by the comparative strength of parties, than by the real demonstrations of innocence or guilt.[3]

This article addresses some of the enormous challenges confronting the legislative branch in an impeachment inquiry. Hamilton predicted that an attempt to impeach a president will "agitate the passions of the whole

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1 DEPT. OF THE INTERIOR, THE ARTICLES OF IMPEACHMENT: ARTICLE X (1868).

2 THE FEDERALIST NO. 65 (Alexander Hamilton).

3 *Id.*

community."[4] Can impeachment ever be enacted without causing undue distress to the public? Using the impeachment of President Clinton as a case study and the benefit of my personal involvement with that matter, I suggest that a rigorous commitment to the principles of fair process and the cultivation of a significant bipartisan consensus are critically necessary in the fulfillment of this solemn responsibility.

The Clinton impeachment proceedings, as discussed below, involved conduct harmful to the public, the severity of which has often been debated by reasonable minds. Few would dispute the wrongfulness of a president lying under oath or obstructing justice, but the salient question in this context was whether such offenses justified President Clinton's removal from office. If a president's crimes were especially heinous in nature and supported by a profound weight of evidence, bipartisan agreement for impeachment and conviction would be far more likely. In applying lessons from the past to any future process, this article assumes that the behavior in question will not be of this most egregious

4 *Id.*

type.[5]

Two key elements of an impeachment inquiry will be considered: 1) the role of the Chair of the Committee on the Judiciary in the House of Representatives as the singular leader of an impeachment effort; and 2) the appropriate proceedings of the House of Representatives leading up to consideration of articles of impeachment by the House. In order to use the Clinton impeachment as a case study, a brief summary of the facts in the matter may be helpful.

Background on the Clinton Impeachment

The events leading to the impeachment of President Clinton began with a law suit by Arkansas state employee Paula Jones in 1994 alleging that she had been sexually harassed by Clinton while he was governor of Arkansas. Potentially impeachable behavior began to unfold in the weeks leading up to civil depositions in the Jones lawsuit in late 1997. On December 5, 1997, Monica Lewinsky's name

5 In the Nixon impeachment proceedings, bipartisan support for impeachment gradually emerged in the House Judiciary Committee as the severity of the President's misconduct became known. The high likelihood of impeachment triggered Nixon's resignation.

first appeared on a witness list in the Jones case, revealing to the President that Jones' lawyers may have found out about his inappropriate relationship with Lewinsky, who was a White House intern when their sexual interludes first began. Concern about the relationship's discovery triggered a series of actions to cover up the scandalous affair by the President, including some actions the House considered to be criminal.

More than two decades removed from the tumultuous events of 1998 and early 1999, most Americans would be hard-pressed to identify the specific conduct for which President Clinton was impeached. That was most certainly not the case in the fall of 1998 due to around-the-clock media coverage and the publication of Independent Counsel Kenneth Starr's report to Congress. The behavior referenced in the Articles of Impeachment included:

- encouraging a witness in a federal civil rights action to execute a sworn affidavit that contained false and misleading testimony;
- encouraging a witness in a federal civil rights action to provide false and misleading testimony;
- engaging in a scheme to conceal evidence that had been subpoenaed in a federal civil rights action;

- attempting to secure employment for a witness in a federal civil rights action in order to encourage the provision of false and misleading testimony;
- allowing the President's attorney to provide false and misleading information to a federal judge in a federal civil rights action; and
- Providing false and misleading testimony before a federal grand jury.[6]

Congressional Democrats showed little interest in disputing the accuracy of the factual information supporting the impeachment proceedings. Instead, the President's supporters argued forcefully that the entire narrative subsequent to and connected with the President's unacceptable relationship with Lewinsky did not warrant impeachment and removal from office. According to the polling data at the time, a majority of the American public agreed with the Democratic position. Not surprisingly, the U.S. Senate eventually acquitted the President on both articles by votes of 45-55 on the perjury charge and 50-50 on the obstruction of justice article. Sixty-seven votes are needed for conviction and removal.

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6 H.R. REP. NO 105-830, at 7-10 (1998).

My Role

In conjunction with the Starr Report's arrival on Capitol Hill on September 9, 1998, House Judiciary Committee Chairman Henry J. Hyde (R-IL) assembled a staff to work on the anticipated inquiry. I was serving at the time as the Chief Counsel of the Subcommittee on Crime of the House Judiciary Committee. Chairman Hyde asked me to serve as the "Chief Counsel/Director of Communications" for the impeachment inquiry. With no small amount of trepidation, I accepted.

My responsibilities included formulating daily messaging and serving as the Committee Republicans' spokesperson. While lawyers generally focus on the details of a given case and avoid as much as possible being distracted or influenced by public opinion, I was expected to study public perceptions and understand how best to respond to media inquiries and prepare Republican members for their public comments. I had, therefore, a unique opportunity to appreciate the political challenges of a presidential impeachment.

The Work of the House Judiciary Committee Chairman

Chairman Henry J. Hyde was a man of remarkable intelligence, wit, and civility. He was universally regarded at the outset of the Clinton impeachment proceedings as exceptionally fair-minded and committed to bipartisanship. Even as the House process came to a conclusion in December, Democratic members still acknowledged that Hyde maintained his cordiality and concern for fairness.

Speaking on the House floor at the outset of the impeachment process, Chairman Hyde challenged his colleagues to rise above partisan politics. He implored with soaring rhetoric, "Let us conduct ourselves and this inquiry in such a way as to vindicate the sacrifices of blood and treasure that have been made across the centuries to create and defend this last best hope of humanity on earth, the United States of America."[7]

Though he worked tirelessly to address Democratic concerns and objections, Chairman Hyde eventually concluded that moving forward was necessary even if one party was almost unanimous in its opposition. He opened the

7 105 CONG. REC. 20,020 (daily ed. Sept. 11, 1998).

floor debate with the following assertions:

> Mr. Speaker, my colleagues of the people's House, I wish to talk to you about the rule of law. After months of argument, hours of debate, there is no need for further complexity. The question before this House is rather simple. It's not a question of sex. Sexual misconduct and adultery are private acts and are none of Congress' business.
>
> It's not even a question of lying about sex. The matter before the House is a question of lying under oath. This is a public act, not a private act. This is called perjury. The matter before the House is a question of the willful, premeditated, deliberate corruption of the nation's system of justice. Perjury and obstruction of justice cannot be reconciled with the office of the president of the United States.
>
> The personal fate of the president is not the issue. The political fate of his party is not the issue. The Dow Jones Industrial Average is not the issue. The issue is perjury – lying under oath. The issue is obstruction of justice, which the president has sworn the most solemn oath to uphold.[8]

As the person charged with the duty of leading an impeachment inquiry, Henry Hyde's magnanimous character proved insufficient for overcoming Alexander Hamilton's warnings about pre-existing party factions. To the degree

8 Chairman Hyde, *Opening Statement during House Debate on Articles of Impeachment against Pres. Clinton,* (Dec. 18, 1998).

that any future leader lacks Hyde's devotion to fairness and civility and is less determined to seek genuinely the opposing party's cooperation, the experience of the Clinton impeachment would suggest that the historic episode will be "doomed to be regulated more by the comparative strength of parties, than by the real demonstrations of innocence or guilt."[9]

Proceedings of the House

The Starr Report received by the House in early September of 1998 was extensive, requiring 18 boxes to contain all of its papers. Along with Starr's summary of his investigation, the boxes contained transcripts of interviews and testimony, investigative reports and various other documents. House leaders[10] met the next day to consider, among other things, whether the report should be released to the public. Given the report's salacious content, Chairman Hyde expressed concern about the appropriateness of this

9 THE FEDERALIST NO. 65 (Alexander Hamilton).

10 This group included Speaker Newt Gingrich, Majority Leader Richard Armey, Minority Leader Richard Gephardt, Judiciary Committee Chairman Henry Hyde and Ranking Minority Member John Conyers.

action. Speaker of the House Newt Gingrich and senior Democrats disagreed with Hyde, and the report was released to the public. Publication of the unsavory details of the Clinton-Lewinsky relationship left the President permanently damaged, but it also began to impact public opinion against the GOP for what appeared to be political gamesmanship.

It is a curious fact that Democratic leaders favored immediate release of the report. Perhaps this was because a slower gradual disclosure of information would drag out the severely negative news concerning the President. Another reason could have been that immediate release would help ignite political backfire against congressional Republicans. Regardless of the motive, it is clearer in hindsight that the political fallout was already starting to build five months before the final Senate votes.

Public dissatisfaction became clearer when on September 21, the video tape of Clinton's four-and-a-half hour grand jury testimony was nationally broadcast on C-Span. No doubt the President's supporters cringed when he uttered his infamous response, "Well, it depends what the definition

of 'is' is."[11] However, televising the embarrassing questions from the Starr prosecutorial team further aggravated public concern about the GOP's motives.

In early October, the House easily passed a resolution authorizing the impeachment inquiry by the Judiciary Committee. The resolution was nearly identical to the one written by Democrats two decades earlier, at the outset of the Nixon impeachment process. With the resolution in hand, Chairman Hyde could begin the committee process. Immediately, Committee Democrats began to voice their objections. They wanted first to define the constitutional standard for impeachment, since there was a strong view on their side of the aisle that the President's behavior warranted sanction but not removal from office. They also wanted, though not with the same fervor, to employ an extensive fact-finding process, rather than relying on the evidence assembled by the Independent Counsel's office. Furthermore, there were simultaneous and contradictory calls for a speedy end to the process. This latter concern once again resonated

11 *Presidential Grand Jury Testimony,* (C-SPAN television broadcast Aug. 17, 1998).

with the public as it wearied from 24/7 news coverage of the inquiry.

Any question about where the American voters stood on the issue of impeachment became clearer with the results of the November midterm elections. The 1998 congressional elections should have been a political setback for Clinton, consistent with the historic pattern for a second term incumbent. Instead, Republicans lost five seats in the House. Later in the month – Speaker Gingrich, who had left no doubt about his strong support for impeachment leading up to the elections – announced his resignation.

Convinced that the President's conduct was a serious violation of his constitutional duty to uphold the rule of law, Hyde and the vast majority of the House Republican conference believed that the process should move forward. However, Chairman Hyde faced a quandary. Attempting to manage a restless public, he promised to complete the House's work by the end of the year. This made it easier for Democrats to object to a rushed process. In an effort to strengthen the factual record, Starr testified before the Committee in a marathon session on November 19.

In addition, the President was given 81 "do you admit or deny" questions that addressed all of the issues in the matter. Clinton cleverly provided responses to the questions on the Friday after Thanksgiving. Once again, however, the responses included considerable legal hairsplitting, and they set the stage for Committee and floor action on impeachment articles in December, 1998.

Following the nearly party-line passage of two articles of impeachment by the House, the process moved to the Senate at the start of the new year. By now, public opinion was generally set in opposition of Clinton's removal from office. Believing that a two-thirds vote for conviction was not within reach, Senate Republican leaders wanted to find the best pathway for fulfilling their responsibilities with the least amount of political repercussion.

Chairman Hyde and twelve other GOP Judiciary Committee members were appointed by the Speaker to be "managers" in the Senate proceedings. Once again, these representatives felt duty-bound to press the case as effectively as possible. Some thought that if Monica Lewinsky and other witnesses could be heard in live testimony, public opinion

might shift. Senate leaders were dead set against what they judged would be an undignified spectacle. On February 12, the President was acquitted.

Conclusion

I worked in the House of Representatives for more than a decade, including as Chief Counsel and Director of Legislative Operations for the Majority Leader. Few if any members of Congress in that era had a stronger reputation for fair-mindedness than Henry Hyde. It is also entirely reasonable to conclude that President Clinton did lie under oath and obstruct justice. It is difficult to find a defense of Clinton's actions put forth by any party other than his own attorneys.

Nevertheless, the party alignments foreseen by Alexander Hamilton in Federalist #65 could not be overcome. What does this say about future impeachment efforts? First, congressional leaders should follow the example set by Henry Hyde and steadfastly avoid appearing to use impeachment to settle political scores or damage the president's standing with the American public. Attempting to overturn presidential

election results through legislative action severely threatens the peace of the nation. Public confidence in the judgments of elected representatives must be strong. Partisan clashes frequently played out before a watching public will destroy this essential confidence. Second, the president's supporters should be given a clear opportunity to state publicly where they stand with reference to the appropriate proceedings. Assuming the conduct in question raises legitimate concerns about a president's continued service in office, the onus should be on the president's supporters to identify what they consider to be an appropriate way forward. Absent some resulting bipartisan agreement, there is little reason to believe, especially in our highly divisive political and media climate, that moving forward would not be an enormous waste of time and particularly damaging to the public interest.

One Democrat on the House Judiciary Committee in 1998 captured some of these concerns quite well: "The impeachment of a President was reserved by the Framers of the Constitution for only the most severe threats against the nation and our system of government. It exists as a remedy to prevent the President from becoming a tyrant. It should

not be used for mere partisan purposes to overturn the will of the people as expressed in two national elections."[12]

12 H.R. Rep. No. 105-830, at 302 (1998).

LIBERALISM, STABILITY, AND PROFIT: THE POLITICAL ECONOMY OF AUTOCRATIC LEGISLATION

Tegan Truitt '21

ABSTRACT: *There is a general consensus that markets and democracies go hand in hand. This consensus is unsurprising, given the prevalence of capitalist democracies and the absence of economic freedom in dictatorships. Nonetheless, I argue that this consensus is without theoretical grounding. Instead, the institutional incentives facing autocrats should, in paradigmatic cases, generate highly liberal laws. I argue further that, we should not only expect autocracies to manifest more liberal rulesets than democracies, but also rules that are more liberal than those produced by anarchies, or "competing systems of private clubs." I then provide a theory as to why, empirically, my thesis appears false. When regimes are unstable, or autocrats have ideological views that supersede their profit motives, autocrats pass illiberal laws. Since most autocracies fulfill one or both of these criteria, most, then, are illiberal. The illiberal autocracy should, however, be understood as a deviation from the benchmark, and not the standard case. I conclude with a brief analysis of the fruitfulness of the theory going forward.*

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Introduction

There is a substantive body of literature addressing the political economy of democracies, in which it has generally been concluded that democracies produce highly illiberal laws, due to rational ignorance[1] and rent-seeking special interest groups vis-à-vis the public choice school. Regardless, it has remained the consensus that, to quote Churchill, "Democracy is the worst form of government, except for all the others." Autocracies are decidedly bad. Economics has, as a discipline, embraced Acton's warning against absolute power.

This paper sets out to address the economics of autocracy and provide a theoretical model for understanding autocratic rule creation. I begin by analyzing the work of Leeson and Coyne, which predicts the "wisdom" of various rulesets arising from different institutional frameworks.[2] They argue that private rules overcome a wisdom/

1 Bryan Caplan, MYTH OF THE RATIONAL VOTER: WHY DEMOCRACIES CHOOSE BAD POLICIES, (Princeton Univ. Press 2008).

2 Peter T. Leeson and Christopher J. Coyne, *Wisdom, Alterability, and Social Rules*, 33 MANAGERIAL AND DECISION ECONOMICS 441, 441-451, (2012).

alterability tradeoff inherent to legislation and norms. While I fundamentally agree with their analysis, I offer criticism of their use of the term "wisdom," which they employ to mean, "preference satisfaction." I reevaluate legislation with respect to liberalism, as opposed to preference satisfaction, concluding that democratic legislation and private clubs should both produce relatively illiberal rules. The surprising conclusion: autocracies, when stable, should yield more liberal rules than either democracies or markets. I argue that instability produces authoritarian law, and thus, the instability of many autocracies around the world causes them to perform worse than democracies with respect to liberalism. Lastly, I formalize this in a simple model: stable autocracies are more liberal than either democracies or private clubs, which are more liberal than unstable autocracies.

Legislation, norms, and private rules

Leeson and Coyne measure social rules on two axes: wisdom and alterability. "Wisdom refers to the extent to which social rules reflect society members' rule demands… Alterability refers to the ease with which society members

can change social rules when their rule demands change in response to changed conditions."[3] From there, they taxonomize three different kinds of rules, and evaluate their relative performance on these criteria.

> Three questions provide the basis for analysis:
>
> (1) What incentives do social-rule producers under a particular social-rule source have to produce rules whose substance reflects society members' rule demands? (2) What information do social-rule producers under a particular social-rule source have about the substance of rules society members demand? (3) What incentives and information do social-rule producers under a particular social-rule source have to modify the substance of existing rules to reflect changes in society members' changing rule demands?[4]

It quickly becomes apparent that two of the rule types – legislation and norms – confront a wisdom/alterability tradeoff. Legislation is highly alterable. It can be effectively changed in minutes at any meeting of the parliamentary body in any Western democracy. However, policy makers have neither the necessary incentives nor the necessary information to formulate rules that correspond broadly

3 Leeson and Coyne, *supra* note 2.

4 *Id.*

with the demands of their constituents. First, and perhaps most insurmountably, legislation confronts the "knowledge problem."[5] The specific knowledge requisite for the efficient coordination of society is not concentrated in any individual database, but is instead fragmented: each person possesses a small fragment of information, relevant to his circumstances, but of unknown importance to the aggregate, and "frequently contradictory" to the information held by others in different circumstances.

Leeson and Coyne also argue that legislation suffers from a principal-agent problem. Legislators (the agent) face a strong incentive to exploit their constituents (the principal) when monitoring is insufficient. Revolution checks an autocrat, but, due to collective action problems, it will only occur under anomalous circumstances.[6] The problems are possibly worse for democratic regimes. Since individual votes count for so little in national elections, voters have little incentive to monitor office holders. This

5 F.A. Hayek, *The Use of Knowledge in Society*, 35 AMERICAN ECONOMIC REVIEW 519, 519-530, (1945); F.A. Hayek, 1 LAW, LEGISLATION, AND LIBERTY (Univ. of Chicago Press 1973).

6 Gordon Tullock, *The Paradox of Revolution,* 11 PUBLIC CHOICE 89, 89-99 (1971).

causes many democracies to be "characterized by vote-seeking politicians, rationally ignorant voters, and special interest groups".[7] Furthermore, ballots are not an effective means of tabulating voter preferences and thus overcoming the information problem. Since each ballot only expresses a preference, without regard to the intensity of that preference, ballots cannot be relied upon to accurately represent the voters' policy wishes. Thus, voting does not accurately manifest consumer preference in law.

Norms – rules that emerge spontaneously, and are observed and enforced, without having been handed down from a central government – are wise. They arise to address the particular needs of the people in a particular time and place. They are venerated by experience. As a result, they correspond strongly to their subjects' preferences. However, they are largely unalterable. Since the norm was not established by a legislative body, there is no legislative body that can convene to eliminate it. Another unfortunate consequence of norms' inalterability comes in the fact that

7 Leeson and Coyne, *supra* note 2.

they can take a great length of time to effectively develop. While norms may be relied upon for their wisdom once they exist, during their formative stages, the problems that the norms will eventually address must remain unsolved.

Leeson and Coyne present private rules as an alternative that overcomes this wisdom/alterability tradeoff:

> The possibility of different clubs offering different social rules, including the possibility of forming a new club or refraining from joining a club altogether, contributes to the existence of a diversity of opinions and independence in opinion formation. Under a system of private rules people are able to form diverse opinions and to self-select into clubs that reflect those opinions. Further, as their opinions change over time, they're able to reselect into a new club that better satisfies their preferences… The possibility of different clubs offering different social-rule alternatives means that the production of private rules is decentralized. There's no centralized, monopoly body that imposes rules on everyone per legislation. Finally, private rules provide the information aggregation and feedback mechanisms required for wise crowds. As Mises and Hayek pointed out, prices and profits and loss in markets provide precisely such mechanisms.[8] This is as true for producers of "ordinary" goods and services as it

8 Ludwig von Mises, *Economic Calculation in the Socialist Commonwealth,* (1920 [1935]), in COLLECTIVIST ECONOMIC PLANNING 87-130 (F.A. Hayek ed., George Routledge & Sons 1945); F.A. Hayek, *The Use of Knowledge in Society*, 35 AMERICAN ECONOMIC REVIEW 519, 519-530.

is for producers of private rules."[9]

One objection to this analysis might be to the word "wisdom." The word might imply that the "wise" rule is normatively desirable. It is entirely plausible, however, that the demanders of rules will, out of ignorance or bad temper, demand rules that are invasive and destructive. In other words, it is not necessarily good that a given ruleset be structured according to the wishes of its subjects if we ascribe to an ethic other than preference satisfaction. This objection has been comprehensively raised by Taylor and Crampton.[10] The following analysis is not normative in its nature; i.e., neither Taylor and Crampton nor I make claims about the desirability of non-invasive rules. Rather, it should be understood as a conditional: if we desire a society in which the lives of some are not violently intruded upon by others, then we should be cautious to label preference-satisfaction as "wise."

The Wisdom of Private Rules?

9 Leeson and Coyne, *supra* note 2.

10 Brad Taylor and Eric Crampton, *Anarchy, Preferences, and Robust Political Economy*, SSRN ELECTORNIC JOURNAL (2009).

Taylor and Crampton grant that a society governed by competing private rulesets

> "will be robust to the existence of self-interested knaves: a well-functioning private defense industry will be capable of preventing aggression against property… however, [it] will be less robust to certain distributions of meddlesome preferences. In an anarchic society, not only the protection of rights, but also the definition of the rights themselves is determined by market forces: if consumers demand illiberal law, that is what they will get."[11]

Taylor and Crampton compare private rules to legislation by appealing to a factor noted by Leeson and Coyne: preference intensity. They begin by dividing the constituents of a hypothetical society into three broad classes: busybodies, libertines, and indifferents. Busybodies have "meddlesome preferences," that is, they desire rules to prohibit behavior that doesn't inflict any physical cost on them. Busybodies might want their beliefs regarding substance use, sexuality, or firearm ownership, among other issues, reflected in law. Libertines are the target of the busybodies' tender ministrations. They use psychoactive substances, pursue alternative sexual lifestyles, hunt recreationally, etc.

11 *Id.*

Indifferents don't engage in activities that the busybodies want to control, but neither do they care if others engage in these activities.

In a democratic country, if there are a great many busybodies, the busybodies will have their way. However, if there are a small number of busybodies, no matter how intensely they harbor their meddlesome preferences, their preferences will not be reflected in law. In a civilization governed by private rules, preference intensity becomes vastly more significant. "Anarchy… produces no budgetary boundary between political and non-political resources: law and private consumption are purchased with a common currency. A person with strong preferences over law can have a disproportionate influence in all issues by forgoing private consumption."[12]

This generates the conclusion that, given sufficient intensity of busybody preference, market law will tend to be less liberal than the product of democratic legislation. The capacity for the busybody to influence policy outcomes by foregoing personal consumption is very slight, given the

12 Leeson and Coyne, *supra* note 2.

extremely low impact of individual votes he might purchase, and the extremely high transaction costs associated with bribing elected officials (as well as the fact that he must compete with public opinion for the politician's favor). The capacity for the busybody to purchase invasive rules is significantly increased by giving preference intensity a voice through the market.

Furthermore, a system of private rulesets is likely to manifest groups that have intense, meddlesome preferences. Taylor and Crampton draw upon the work of Mulholland[13] and Berman and Laitin, among others, to show that hate groups and extremist organizations are more likely to form where there is not a source of security from the state.[14] The simple reason is that these groups are capable of providing the public good of security, and so their existence is more demanded in areas where security is lacking. While these clubs are not necessarily meddlesome, "requiring members

13 Sean E. Mulholland, *Hate Fuel: On the Relationship Between Local Government Policy and Hate Group Activity*, SSRN ELECTRONIC JOURNAL (2008).

14 Eli Berman and David D. Laitin, *Religion, Terrorism and Public Goods: Testing the Club Model*, 92 JOURNAL OF PUBLIC ECONOMICS 1942, 1942-1967 (2008).

to conform to costly behavioral norms weeds out the uncommitted and reduces free-riding."[15]

It thus seems tendentious to label consumer satisfaction "wise," if we want a kind of liberalism to be reflected in our legal order. Taylor and Crampton demonstrate that democracy yields more liberal rules only under certain preference dispersions; if busybodies have low-intensity preferences, then private clubs will yield more liberal rules. For the purposes of this paper, it is not necessary to estimate the array of conditions under which democracy performs more liberally than clubs, and vice versa. The point is simply that, while democracies tend to produce illiberal law for a variety of reasons, private clubs can do so just as easily.

Residual Claimancy and the Creation of Rules

Residual claimancy extends the time horizon of the property owner, and it is the contention of some that an autocrat will have a longer time horizon because he owns the capital value of a country. This extension of time horizon has been

15 Taylor and Crampton, *supra* note 10.

shown to minimize state plunder. Olsen begins his analysis of autocracy by sharing with the reader a statement from an Italian villager: "Monarchy is the best kind of government because the king is then the owner of the country. Like the owner of a house, when the wiring is wrong, he fixes it".[16] To one raised in a democratic society, this statement might seem shocking. We should not find it so surprising, however, given our intuitions regarding institutional incentives. The common is subject to tragedy – communal ownership of a good results in a race for consumption that destroys its capital value. Conversely, if the good is durable and its value has a residual claimant, we should expect that, *ceteris paribus*, its value will be maintained for a longer length of time.

Olsen raises this point to discuss a hypothetical anarchy before states exist. His theory of state formation is essentially that, if there were a time at which society was primarily composed of victimized villages and roving bandits, eventually, some of the bandits would become "stationary." Realizing the benefits of leaving a village

16 Mancur Olson, *Dictatorship, Democracy, and Development*, 87 AMERICAN POLITICAL SCIENCE REVIEW 567, 567 (1993).

around to plunder again – say, annually – a bandit gang would set up its jurisdiction over the village and levy taxes. To prevent a tragedy of the commons in village-plunder from foiling its rapacious endeavors, the bandit gang would likely provide some measure of defense against other bandits. Thus, states arise. The radical welfare implication that Olsen derives is that subjection to a stationary bandit constitutes an improvement for the village – the plunderer's barbaric interests align with the villagers' desire for protection. Plunder is minimized dynamically.

Hoppe expounds upon the matter by applying the logic of collective ownership to rule creation.[17] A profit-maximizing owner of a resource wants to balance the loss of capital value due to consumption with the profits accrued as a result of the resource's use. If the resource is owned collectively, then any of the individual claimants can have no guarantee of the resource maintaining its capital value. If one claimant abstains from use in order to preserve the resource, others might not. This possibility creates an

17 Hans-Hermann Hoppe, DEMOCRACY – THE GOD THAT FAILED: THE ECONOMICS AND POLITICS OF MONARCHY, DEMOCRACY, AND NATURAL ORDER, (Transaction Publishers, 2002).

incentive to consume. The value yielded by using the resource accrues instantly to the user; the value of abstaining from consumption is uncertain at best. When all members of the collective realize this, they will attempt to consume as much of it in the present as possible, so that they can be assured of realizing some of its value for themselves, as opposed to seeing it all disbursed into their neighbors' hands. Thus, the capital value of the resource is destroyed. Following such logic, elected representatives can be seen as owners of the current use value, but not capital value, of a country. As a result, they face an incentive to "consume" the country – extract as many resources as possible for personal gain before they can no longer hold office. Hereditary monarchs can conversely be conceived of as owners of the capital value of the country. For the king, capital consumption in the present reduces future profit.

Hoppe and Olsen are in agreement that the critical component is the time horizon of the autocrat. Political elites who face longer time horizons have a lower incentive for consumption. The bandit who is most stationary has the longest time horizon. Given the welfare superiority of

governance by the stationary bandit over the marauding one, the question arises: if a society is governed by a low time-preference autocrat, can we expect its rules to be "wise"?

Not according to Leeson and Coyne:

> The sovereign's residual claimancy on citizens' productivity might provide an alternative channel through which his interests could be aligned with citizens'. But this fails too. The sovereign isn't a residual claimant on the revenues he generates from producing social rules citizens desire. He's a residual claimant on the revenues generated through his citizen's productivity. This gives the sovereign an incentive to maximize his citizens' productivity. But the social rules that maximize citizens' productivity needn't be the ones that maximize citizens' welfare. And these are the social rules citizens desire. The social rules the sovereign will produce legislatively only dovetail with the ones citizens demand in the event that citizens care only about maximizing their incomes. That would, for example, require citizens to value leisure only instrumentally—as a means of making them more productive laborers. This is unlikely.[18]

If by wisdom we mean preference satisfaction, then clearly a low time-preference autocrat will create unwise rules. However, we have already seen that preference

18 Leeson and Coyne, *supra* note 2.

satisfaction does not necessarily coincide with liberal laws. If we consider the wise rule to be the liberal rule, then the autocrat's wisdom is still up for debate.

Autocratic Liberalism

There is a necessary link between productivity maximization and welfare, contra Leeson and Coyne. If the autocrat generates his revenue by taxing income, production, or exchange, he has a vested interest in facilitating the highest number of voluntary exchanges possible. In addition to allowing large amounts of taxable wealth creation, maximizing his subjects' voluntary exchanges expands the division of labor, which, of course, allows for further wealth creation. The division of labor can exist only when it is coordinated by an infrastructure which provides both *knowledge* of what to create and *incentive* to create. The price system, as demonstrated by Mises and Hayek, whose arguments were referenced by Leeson and Coyne, supplies this coordination.[19]

19 Ludwig von Mises, *Economic Calculation in the Socialist Commonwealth,* (1920 [1935]), in COLLECTIVIST ECONOMIC PLANNING 87-130 (F.A. Hayek ed., George Routledge & Sons 1945) and F.A. Hayek, *The*

Mises and Hayek furthermore demonstrate that the price system can only exist in a market, i.e., to the extent that production is controlled by the state, prices will be artificial. They will provide neither the necessary information nor incentives. Thus, in any sufficiently large economy, productivity depends upon economic freedom. This allows us to make several predictions about an autocrat's behavior. (1) If the ruler has a vested interest in taxing productivity for personal gain, then he should make the laws such that his society is subject to few economic regulations and controls. (2) He also faces a strong incentive to protect his subjects' property rights, not only against external invasion, but also from domestic crime, as this, too, will threaten the number of voluntary exchanges. (3) Black markets will generate untaxable income, so the revenue maximizing autocrat should also do as much as possible to stamp them out, by legalizing all exchanges. In addition to rendering most exchanges taxable, legalization is less costly than enforcement. No third party to any exchange incurs any cost,

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Use of Knowledge in Society, 35 AMERICAN ECONOMIC REVIEW 519, 519-530.

excluding negative externalities. Preventing an exchange involves, at a minimum, the opportunity cost of time and material resources in finding the unlawful exchange and applying enough violence to prevent it. When you outlaw entire classes of exchanges, the process becomes significantly more costly. It also then involves establishing a bureaucracy to govern the law-enforcement process, which amplifies costs dramatically. This demonstrates the significant incentive, to a profit-maximizing autocrat, for legalization. By facilitating productivity, in other words, the autocrat passes highly liberal laws: light economic regulation, strong property protection, and few, if any, illicit goods.

Leeson and Coyne are correct in their argument that residual claimancy—that is, ownership of rules—is essential to wise and alterable rule creation. But freedom can be significantly curtailed in the society structured according to private rule clubs. As we have seen, democratic policies are often illiberal as well. A stationary bandit who expects to pillage his land routinely, however, faces incentives that maximize individual liberty. If liberalism is our guiding legal light, then a stationary bandit creates wiser rules than

a private club.

It should be noted that this refutes Leeson and Coyne's contention that "citizens must value leisure only instrumentally" for their interests to coincide with the autocrat's. On the contrary, by cultivating a market, and thus creating such a liberal ruleset, the autocrat must necessarily leave his citizens the opportunity to pursue leisure. The only case in which the autocrat will "crack down" on leisure arises when the costs of monitoring unproductive citizens is exceeded by the cost of their un-productivity. This will only occur when monitoring is almost costless or when the citizenry is *extremely* unproductive. Since there will not, however, be any sort of social safety net in the pure case, citizens will face a fairly steep opportunity cost of excessive leisure, unemployment, and thus we should not expect this latter occurrence.

Lastly, a brief note on tax rates: we should expect autocrats to tax less than their democratic counterparts, but perhaps more than a private club would charge. Democratically elected representatives face strong incentives to earn future votes through wealth transfers. These transfers

are necessarily the product of taxation or inflation (which functions as a tax via Cantillon effects). Private clubs must compete with each other to lower rates, so we can expect membership prices far lower than the tax burden in a democracy. An autocrat has no competition, so he need not lower his tax rate significantly on that account. However, low tax rates allow for more future wealth creation and hence more future tax revenue.[20] The longer he abstains from plundering, the more wealth will be created. Thus, the longer the autocrat's time horizon, the lower he will set the tax rate.

Stability and Time Horizon

It has been clearly shown that the time horizon is a critical component in the reduction of plunder. Democracies fail to produce liberal rules on account of the numerous incentive problems they confront. Private clubs fail to produce liberal rules because they will manifest illiberal

20 It is a universally acknowledged fact among economists that taxes create deadweight loss (a reduction in voluntary exchanges). Obviously, some level of deadweight loss is desirable to the autocrat – that is, after all, how he gains any revenue at all. Wealth taken by the autocrat, however, is not reinvested in his country's capital structure. Thus, the more he takes, the less his capital structure expands, meaning that he will have more wealth in the present but his country will produce less dynamically.

preferences. Ironically, autocratic governments should theoretically produce the *most* liberal rules. Why, then, do autocratic regimes have such abysmal track records when it comes to freedom? If the preceding analysis is correct, then the problem lies not in the nature of autocracy, but in the autocrats' rates of time-preference. Autocrats with insufficient time horizons face the incentives of democracies and roving bandits – they must extract as much value as possible from their resource before time runs out.

Most autocracies are unstable. This is not endemic to autocracy, but instead to government. Almost 70% of countries globally are classified at the "warning" stage by the Fragile States Index.[21] The capacity for an autocrat's continued resource consumption is uncertain. Dictators never know when there might be a coup, a peasant insurrection, or an international intervention. This shortens their time horizons and makes them more eager to consume. Further, given their instability, they form coalitions with local factions and members of the international community.

21 Messner, et al., *Fragile States Index*, FUND FOR PEACE, (2018), https://fundforpeace.org/2018/04/24/fragile-states-index-2018-annual-report/.

In exchange for these parties' support, autocrats must often provide legislation friendly to these foreign aims. The result is that many meddlesome preferences are manifested in law. Moreover, the regional instability accelerates the time horizons for these local factions as well as the dictator, so they make more consumptive demands in exchange for their loyalty. This theory predicts a couple of outcomes that should be empirically tested by future research: (1) law should be more oppressive and tax rates should be higher in less stable autocratic regions; (2) in a given autocratic region, tax rates should increase and laws should become more oppressive in times of greater instability.

Formalizing the Model

Taken together, the arguments above provide a theoretical model for a benchmark liberal government. Where L represents the extent to which law is liberal, D signifies democracy, P signifies private clubs, As signifies stable autocracy, and Au signifies unstable autocracy, we can expect:

Assuming profit-maximization: $L_{As} > L_{D} = L_{P} > L_{Au}$

This satisfies our intuitions regarding the authoritarianism of autocracy, as it predicts a range of cases in which autocratic regimes produce highly illiberal law. The model also provides a theoretical case for a kind of government that satisfies our economic intuitions but is empirically unlikely to occur: liberal autocracy. Lastly, it recognizes that democracies and private clubs function as a check on authoritarian government, but contain their own illiberal strains of rules.

By providing a benchmark institutional grounding for rule predictions, the model can help explain deviations. For instance, if a stable autocracy bans psychoactive substances, we can reasonably conclude that its autocrat is not a perfect profit maximizer. The ideal case allows us to understand to what extent, and on what issues, autocrats are "true believers" – that is, the extent to which they are willing to forsake monetary profit for psychic gain (likely a result of ideology). Alternatively, the model functions as the basis of a predictor of a region's stability. If we hold constant the assumption that the autocrat is reasonably motivated by profit, then the extent to which his ruleset is liberal informs

us of the stability of his domain. We should expect that in a draconian autocracy, there are a number of concessions to factions/international powers that the governor must make, from which result the invasive policies.

Conclusion

In summary, the model relates three different variables: the degree to which laws are liberal, the stability in a region, and the extent to which an autocrat is motivated by pecuniary reward. By holding two constant, we can form a reasonable expectation about the third. It also raises a counterintuitive conclusion: autocracies, under the right conditions, will generate more liberal rules than any other system of social organization.

The model can benefit from empirical testing. The questions outlined above regarding the nature of stability are viable avenues of future research. Additionally, since examining the wisdom/alterability tradeoff outlined by Leeson and Coyne, I have left the subject of norms. A model for the propensity of liberal or illiberal norms to arise would help to expound upon this model. Most importantly, the

question must be resolved: is there a stable, liberal autocracy to which we can point?

Regardless, the model presents an important theoretical baseline from which we ought to begin our inquiries into the political economy of autocracy. Rather than expecting brutal dictatorship, though that may often arise, we should hold autocracies up to a benchmark of liberalism. Their failing to be liberal should not be interpreted as something endemic to autocracy or inherent in the nature of power, but rather as the result of exogenous circumstances. Liberalism and autocracy are not incompatible. They coalesce when the autocrat is profit-motivated and holds a secure position of power.

THE MODERN AMERICAN PRESIDENCY: HOW THE EXECUTIVE BRANCH HAS CHANGED

Tyler Gustafson '20

Abstract: *Has the American presidency shifted to a completely different version than what the founders intended, or would the founders approve of the presidency that is seen today? Ultimately, the founders would, indeed, approve of the presidency that is seen today. Certain presidents have changed the office of the president but not in ways that make the office unconstitutionally powerful. Indeed, there are differences in how the president functions today versus how that office functioned at the founding. Presidents Woodrow Wilson and Franklin Delano Roosevelt are the main cause of this change. President Wilson wanted to democratize American government while placing so-called experts in positions to determine policy making. FDR took Wilson's ideas and implemented them with the Reorganization Act of 1939. This allowed FDR to change the office of the president permanently by expanding the Executive Bureaucracy. But this change is not unconstitutional, for the founders created a path by which the president could become what it is today.*

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Did the American Presidency change from traditional to "modern", or did a different change take place? Some scholars suggest that there is a difference between the traditional presidency of the founders versus the "modern" presidency of today. Typically, this shift from the original presidency to the "modern" presidency is attributed to President Franklin D. Roosevelt.

One scholar, Fred Greenstein, posits four areas where the "modern" presidency has taken on roles that the original presidency would not. First, he states that the president became actively involved in initiating and seeking congressional support for legislation and frequently using the power of veto as a way to pursue his legislative agenda. Second, Greenstein notes that the president, who normally exercised few unilateral powers, transitioned into the frequent use of executive orders to bypass Congress. Third, the president created an extended bureaucracy in the executive branch to support his own legislative agenda through independent policy making. Finally, the presidency became personalized.[1]

1 Fred Greenstein, *Change and Continuity in the Modern Presidency* (1978)

Greenstein attributes these changes to FDR[2]. However, his assertions are flawed. One only needs to look to the Constitution and the framers' intention for the presidency to understand that all four of the above categories fall under the original jurisdiction of the president. Greenstein's rules for the "new" presidency which he believes began under FDR, miss the mark regarding the changes FDR actually initiated in the presidency. Yet, other scholars seek to blame the modern presidency on other presidents. Jeffery K. Tulis claims that the modern presidency was created under Woodrow Wilson.[3] His two main problems with this "modern" presidency are that it creates a "Super-man" role for the president by raising his expectations far too high, and it makes extraordinary power seem routine.[4] Both of these scholars recognize that there is change in how the executive branch is perceived. However, they both fail to recognize where the real problem lies. The "modern" presidency is not modern.

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in THE NEW AMERICAN POLITICAL SYSTEM, (Anthony King ed. AEI Press 1990).

2 *Id.*

3 Jeffrey Tulis, *The Two Constitutional Presidencies* in THE PRESIDENCY AND THE POLITICAL SYSTEM 2 (Michael Nelson, ed. CQ Press 2014).

4 *Id.* at 23.

Rather, the framers would support the office of the president as it is used today. The real problem can be found in how policy-making changed and how FDR and Woodrow Wilson shifted the executive branch.

James Wilson set up how the president was to operate. His language regarding the presidency allowed for an executive with oversight of the executive branch. According to Wilson, the executive must act with energy, dispatch, and responsibility[5]. James Wilson looked to the Governor of New York as a template for the American presidency.[6] Governor Morris of New York was also a prominent supporter of a strong executive[7]. Wilson saw what New York was doing as practicable and useful for America going forward. New York's general grant of executive power is similar to the Constitution's Vesting Clause. The Vesting Clause reads, "The executive power shall be vested in a President of the United States of America."[8] This clause was left intentionally vague to allow the executive to act when necessary.

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5 Charles Thach, THE CREATION OF THE PRESIDENCY, 1775-1789: A STUDY IN CONSTITUIONAL HISTORY 90 (Liberty Fund Inc. 2010).

6 Thach, *supra* note 5, at 104-105.

7 *Id.*

8 U.S. CONST. art II, §1.

Governor Morris is why the Vesting Clause reads in such a manner. However, that wording is not necessarily problematic in its original meaning. Morris was tasked with writing the Constitution and, in doing so, he included what he thought to be the correct view of presidential power. As David Nichols points out, "Under Morris' formulation, the legislative powers of the government are limited to those specifically granted by the Constitution, but the executive power is subject to no such limitation."[9] The framers, fearful of an overpowered legislature, created mechanisms by which the legislature could be checked. The executive, however, was different. It would be checked in other ways not like the enumerated powers of Congress. The president is bound by the people and the Constitution. The framers' foresight allowed for an expansive executive branch. The Vesting Clause and the language that the framers used surrounding the president made the office one that could accommodate change.

Greenstein's analysis of the presidency's chang-

9 David Nichols, THE MYTH OF THE MODERN PRESIDENCY 38 (Penn. St. Univ. Press 1994).

es seems to disregard the Vesting Clause. Through such a clause, the executive branch was inherently going to be expansive. Thomas Jefferson, the third president of the United States, initiated and sought after legislation to make the Louisiana Purchase. After Congress acted too slowly to make the purchase, Jefferson did so unilaterally. His unilateral action was even supported by one of his adamant opponents, Alexander Hamilton, who understood that the executive had such authority over foreign affairs. Jefferson later explained his actions to the public and although his explanation of executive power was flawed through his assertion of prerogative power, he demonstrated the personalization of the presidency. During Andrew Jackson's presidency, Jackson used the power of veto in a manner pursuant to his legislative agenda. Jackson thought that he had an obligation to the people. Jackson's presidency further demonstrates how Greenstein misses the mark. Of these presidents both would be considered "modern," but they both demonstrated traits of Greenstein's "modern" presidency.

Like Greenstein, Tulis has a flawed understanding of the presidency. James Wilson wanted a single executive with

energy, dispatch, and responsibility.[10] The executive branch was to be separate from the legislature to prevent any means of creating a privy council over the president. According to Tulis, that separation for the executive signaled the framers' intention to make the presidency independent from Congress and the people.[11] He is correct in asserting that the president was to remain independent from the legislature. However, Tulis misses the mark regarding the president's relation to the people. The framers bound the president to the Constitution through a national election, and, in doing so, tied the president to the people. Inherently, a nationally-elected executive must be in touch with the people. James Wilson believed that it was necessary for the executive to have good leadership in managing the office[12]. In doing so, the executive must be able to make public arguments.

Jeffery Tulis makes another distinction that separates the traditional and "modern" presidencies. He calls that distinction the divide between the first and second constitutions; the first is what the founders intended, the sec-

10 Thach, *supra* note 5, at 90.
11 Tulis, *supra* note 3, at 10.
12 Thach, *supra* note 5, at 104-105.

ond is more concerned with rhetoric.[13] Tulis, however, fails to account for James Wilson's argument that the president must be able to make public arguments and use executive power as a single executive[14]. Tulis tries to credit the rhetorical presidency to Woodrow Wilson. However, the rhetorical presidency did not start there: presidents prior to Woodrow Wilson were rhetorical and acted unilaterally. Examples of such presidents are not hard to find. George Washington, James Monroe, Andrew Jackson, and Abraham Lincoln all made public arguments and acted within the purview of the Constitution as it related to executive power. Tulis also claims that the second constitution makes a situation like the Iran-Contra affair more likely due to greater perceived executive power.[15]

Tulis seems to be correct if one only considers recent affairs. President Obama illegally entered Libya which led to the infamous Benghazi terrorist attacks. However, Tulis is wrong. Thomas Jefferson engaged in a quasi-war with the Barbary Pirates off the coast of Libya. He did so unconsti-

13 Tulis, *supra* note 3, at 1.
14 Thach, *supra* note 5, at 74.
15 Tulis, *supra* note 3, at 25.

tutionally without the approval of Congress, despite the fact that only Congress possess the power to declare war. The Iran-Contra affair was unconstitutional, but it was not made more likely by the second constitution. Such actions took place long before the arrival of Tulis' second constitution.

Wilson and FDR both enacted change on the executive branch but did not change the entire branch, as Greenstein and Tulis assert. If the "modern" presidency is so vastly powerful, beyond what the framers intended, how does one go about explaining the similarities between the "traditional" and "modern" presidents? Both Presidents Jefferson and Obama illegally engaged in military affairs near or in the country of Libya. President Jackson wielded the veto power like a sword. Presidents Abraham Lincoln, Thomas Jefferson, and George Washington engaged with the people through addresses. Although there are more examples, those presidents demonstrated traits of the "modern" presidency, yet they are not modern.

The "modern" presidency can be seen through many "traditional" presidents. Likewise, the "traditional" presidency can be seen in "modern" presidents. Consider George

W. Bush. His presidency did not demonstrate vast executive power beyond the framers' intent. Before going to war in Iraq, Bush first went to Congress. He conducted military operations constitutionally, during a time when many would not exercise such restraint. Additionally, Bush demonstrated how a "modern" president did not follow Tulis' second constitution claim that the new presidency is more rhetorical. President Bush often struggled to clearly articulate his plan for the nation. The "modern" presidency is not new. Wilson and FDR did, however, change the office and how it functions.

Although the presidency of Woodrow Wilson was not new in terms of its rhetorical status, it was different in that it attempted to change the American system of governance. At first, Wilson wanted parliamentary government. When he became president, he pivoted to stating that the president should have the most power. In reality, Wilson wanted to make the American government a pure democracy, rather than democratic republic the Constitution established.[16] The founders, who were fearful of pure democracy, set up a form

16 Nichols, *supra* note 9, at 19.

of representative government to curb purely democratic tendencies. The balance of power was made so that it would be difficult to pass legislation. Wilson harbored a distaste for the separation of powers that the Constitution had set up.[17] His aversion to grid-lock, and preference that the president and Congress be integrated, furthered what some scholars have termed a "Darwinian" approach to the Constitution, as opposed to what may be termed the founders' "Newtonian" approach.[18] This approach essentially treated the Constitution as a living document. His apathy toward the Constitution allowed him to think and operate in ways that changed American governmental practices. Wilson wanted big debates about big principles and sought to eliminate interest groups as he saw them as detrimental to democracy. Wilson sought to change the deliberative practices that the framers intended for the passage of legislation. However, such changes were dealt to the entire system rather than just the office of the President.

Woodrow Wilson sought to expedite the process by

17 Christopher Wolfe, *Woodrow Wilson: Interpreting the Constitution*, 41 REVIEW OF POLITICS 121, 128 (1979).

18 Nichols, *supra* note 9, at 14-15.

which legislation was passed and sought to eliminate the checks and balances that slowed down that legislative process. In his view, the agendas should be informed by "non-partisan" experts.[19] Thus, the executive bureaucracy took on a greater role in the policy planning of America. When Franklin Roosevelt took office, Woodrow Wilson's plan for America took off. FDR was strongly influenced by the thoughts and practices of Woodrow Wilson who is recognized as the first writer to advocate the doctrine of responsible party government.[20] FDR's New Deal solidified the notion that there had been a shift in the American governmental system. That shift signified that the New Deal gave impetus to an extension of presidential responsibility which tended to replace partisan politics with the executive administration.[21]

In an environment where poverty was high and people were struggling to find ways to live during the Great Depression, FDR's New Deal seemed like a plausible solution no matter what it did to the Constitution. FDR promised a

19 *Id.* at 17.

20 Sidney Milkus, *Franklin D. Roosevelt and The Transcendence of Partisan Politics*, 100 POLITICAL SCIENCE QUARTERLY 479, 480 (1985).

21 *Id.*

concrete plan for the New Deal as a campaign tactic. In reality, he did not have such a plan. He had an ideology which proved to be harmful to the framers' government. The Second Bill of Rights demonstrated how FDR thought of power and how he planned to go about changing America. He listed them as: the right to a useful job; the right to earn enough for adequate food, clothes, and recreation; the right of a farmer to sell products for decent living; the right for businesses to free trade; the right of every family to a decent home; the right to adequate medical care; protection from economic problems of old age; and the right to a good education.[22]

FDR announced these rights to the public without congressional approval, in a rhetorical way. That was not a major issue and was a part of the traditional presidency. Rather, the problem stemmed from the positive nature of these new rights. The original Bill of Rights consisted of negative rights stating what the government could not do. The Second Bill of Rights was stated in the opposite fashion, elaborating on what the government could and should

22 Franklin Roosevelt, State of the Union Message to Congress, (Jan. 11, 1944).

do. Such a pivot from the original understanding of rights changed how Americans interacted with the government. Most people began to expect the government to provide for them when they could not provide for themselves. Such dependence on the federal government, through the New Deal, fostered a culture of reliance.

In order to act on his Second Bill of Rights, FDR had to first take on his own party. One scholar, Sydney Milkus, asserts that Roosevelt tried to establish a personal party. His idea of a personal party was illuminated by the election of 1938 which is often dubbed the "Purge Campaign of 1938".[23] Roosevelt's purge was likened to Adolf Hitler's weeding-out of dissension within the German Nazi party and Joseph Stalin's elimination of disloyal party members in the Soviet Communist Party of Russia, but without the massive casualties.[24] FDR's endorsement of candidates was not unprecedented, but his use of government funds to do so was questionable and possibly illegal. Until the Hatch Act of 1939, FDR used the growing army of federal workers in local and

23 Milkus, *supra* note 20, at 485.

24 *Id.* at 486.

state political activity to get people of his liking elected. The Hatch Act barred federal employees from participating in campaigns. Prior to the Hatch Act, some thought that Roosevelt was assembling a modern Tammany.[25] His political actions, regarding the purge of the Democratic Party were vital in passing the New Deal. FDR knew that in order to pass such sweeping change he would need to change the mindsets of those in the legislature or replace the current minds with new ones who would follow his ideas. With a legislature that thought like him, Roosevelt had set up the path by which the next step could be taken to advance his agenda.

FDR enabled the government to act on his Second Bill of Rights with the passage of the Executive Reorganization Act which greatly expanded the executive bureaucracy[26]. This act permanently changed how legislators operate. In 1933 the executive bureaucracy employed around 500,000 people. By 1945 it had expanded to include 3.5 million people.[27] This allowed the president to become the main initiator

25 *Id.* at 494.

26 5 U.S.C. § 133 (1939).

27 *The Development of the Bureaucracy,* US HIST., http://www.ushistory.org/gov/8a.asp (last visited Apr. 28, 2019).

of legislative material. The huge staff that was allotted to the executive branch through this act enabled the president to research policy and create public policy plans.

Although controversial, the Executive Reorganization Act was not unconstitutional. Clearly, the framers intended to give legislative authority to Congress. Article one of the Constitution delineates that power to them[28]. However, FDR turned that practice on its head. By advocating and campaigning for politicians who followed his own New Deal doctrine, FDR enabled himself to pursue his own agenda. He effectively got Congress to turn over their power to create legislation to the president through the Executive Reorganization Act. Policy and legislation making has not been the same since then. Similarly, the growth of the executive branch has given much of the perceived power of the purse to the president. By the 1970s Congress relied heavily on the president to submit a budget and relied on the estimations and projections of executive branch officials.[29] Such change can be credited to FDR's New Deal practices which set up a

28 U.S. CONST. art I.

29 Nichols, *supra* note 9, at 66.

system by which he could achieve his goals efficiently.

Such an overgrown executive branch is not unconstitutional. Modern presidency theorists fail to recognize the expansive tendency of Article II of the Constitution. Additionally, the president is the only elected official that is elected by the nation as a whole, which should dispel the notion that the legislature is the branch that is closest to the people.[30] That said, FDR still changed how the American government functions.

One can view the effects of such change today. President Trump and his lack of direction for Congress shows how FDR changed that process. Since FDR, presidents have been the leading agenda-makers. Arguably, President Trump's position can be described as true to the Constitution. Whether he knows it or not, he is allowing Congress to do its intended job. The fact Congress has been ineffective in doing so demonstrates the dependency on the president as an agenda maker. Without a vision from the president, Congress has been inept. In this way, President Trump has been a "traditional" president. On the other hand, President

30 *Id.* at 28.

Trump would be considered "modern" by Tulis through his use of Twitter and many opportunities to speak directly to the American people. Although the framers could not have foreseen the arrival of social media, they would not consider it problematic to use it to speak to the American people. The content of what President Trump includes in his Twitter account is a different matter, but its use is aligned with how the framers saw the presidency. It is true that many framers, including James Wilson, understood that the president should be in touch with the people. However, the current executive branch is tainted by the effects of FDR and Woodrow Wilson. Although Congress finagled the budget plan, they ultimately relied on the executive branch to come forth with a plan to move forward.

Although FDR changed how legislation was created, it was not an unconstitutional change. Some people succumb to the notion that the president has no place in the legislature. That rudimentary understanding fails to account for the executive's veto power and state of the union address. Clearly, the framers intended for the president to have those powers that involve the act of legislating and articulating an agenda

for the nation. To claim that the president has no authority to interfere with legislation is equivalent to ignoring the text of the Constitution. Additionally, those who support the notion of an entirely different modern presidency often point to the mushrooming effect of the executive administration after FDR.[31]

Modern presidency theorists fail to recognize that the president has the constitutional authority to oversee those administrations. A notable part of the executive's job is to execute the laws. Doing so requires the discretion afforded the president by his office. Although the oversight and expansion of the executive bureaucracy is constitutional and a part of the traditional presidency, this does not mean that FDR did not have a significant impact on the way America functions.

The presidency, as seen today, is not an unconstitutional version of the office. Rather, it is an extension of what the founders put in place. FDR and Woodrow Wilson, radically progressive as they were, did not create an entirely new version of the presidency. Instead, constitutional prac-

31 *Id.* at 93.

tices changed in a manner congruent with the Constitution. The results, however, were negative. FDR created many new programs and vastly expanded the executive bureaucracy. It has not shrunk since then. Resulting from such expansion is a massive deficit, unsustainable social programs, and a population very dependent on the government. One only needs to view the current state of affairs to see such results.

Wilson and FDR's pragmatic approach to the Constitution, the "living constitution perspective," has damaged the executive branch. However, their presidencies have not destroyed the executive branch. Although the "modern" presidency is not so modern, the practices of the government changed due to Woodrow Wilson and FDR. They expanded the executive branch and changed how legislation was created. Because of them, America has become a society trapped by New Deal politics.

AFFIRMING THE COURT'S DECISION IN REGENTS OF THE UNIVERSITY OF CALIFORNIA V. BAKKE

Hannah Schuller '19

ABSTRACT: *In light of the recent affirmative action case surrounding Harvard University, there is no better time to review the precedent of Supreme Court rulings regarding affirmative action in higher education. Justice Lewis F. Powell Jr.'s plurality opinion in the landmark Supreme Court case Regents of the University of California v. Bakke provides a compelling argument that delegitimizes racial quotas, yet promotes the idea of applying a racial "plus" system in order to enhance diversity in a university setting. In several similar cases following this decision, Justices have largely relied on Powell's argumentation in their own attempts to avoid discrimination, while also allowing universities the freedom to foster a diverse student body. This paper will argue that Regents of the University of California v. Bakke was decided correctly and should be used as a framework as the Supreme Court rules on future affirmative action cases.*

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While speaking to an audience in Chicago, Illinois, in 1858, Abraham Lincoln stated his desire for all citizens of the United States to come to a point where not one person would doubt that "all men are created free and equal."[1] For many citizens living during Lincoln's presidency, Lincoln's sentiments regarding equality for all citizens were admirable. Others, however, took issue with Lincoln's beliefs. In addition to the backlash toward Lincoln's pursuit of equality in the United States during his presidency, there have been countless challenges to the idea of equality throughout history, resulting in cases such as *Plessy v. Ferguson* and *Brown v. Board of Education* which eventually led to the creation of the Civil Rights Act of 1964. Fortunately, a wide variety of higher education institutions and places of employment across the nation have responded to race-related challenges by seeking to admit or hire an increasing number of minority appellants, particularly African-American citizens. However, many of these organizations have experienced the tension between seeking to expand diversity and preventing special

1 President Abraham Lincoln, Speech at Chicago, Illinois (Jul. 10, 1858), https://teachingamericanhistory.org/library/document/speech-at-chicago-illinois/.

preference for certain people based solely on race.

One pertinent example of this tension is found in a lawsuit currently facing Harvard University. On October 15, 2018, a case filed against Harvard in 2014 was finally presented in court.[2] The plaintiff, Students for Fair Admissions (SFFA), has argued that Harvard holds Asian-American applicants to a far higher standard than applicants of other races. SFFA claimed that Harvard's admissions staff is guilty of consistently rating Asian-American applicants lower than their non-Asian counterparts when evaluating applicants' courage, likeability, and other positive personality traits – strongly enforcing the negative stereotype that Asian Americans are solely gifted in academic pursuits but lacking in personality. [2] As a result, SFFA accused Harvard of violating Title VI of the Civil Rights Act of 1964, which forbids the use of racial discrimination in all programs that receive federal funds.[3] Additionally, SFFA is petitioning for a race-blind admissions protocol at Harvard and beyond in order to ensure that race-based discrimination in higher

2 Students for Fair Admissions, Inc., v. President and Fellows of Harvard College et al., No. 1:14-cv-14176-ADB (D. Mass. Feb. 13, 2019).

3 IV of the Civil Rights Act of 1964, 42 U.S.C. § 2000d, et seq.

education will swiftly come to an end.

SFFA's case is largely focused on research presented by Dr. Peter Arcidiacono, an economics professor at Duke University.[4] Dr. Arcidiacono was hired by SFFA to analyze six years of Harvard's admissions data and search for signs of discriminatory practices while evaluating applicants. Arcidiacono testified that his research shows patterns of African-American applicants benefitting the most from Harvard's admissions policies, followed by Hispanics, Caucasians, and lastly, Asian Americans. Furthermore, Arcidiacono expressed his personal belief that his findings demonstrated "evidence of discrimination against Asian-Americans in the admissions process, both in how they rate applicants and in the decisions themselves."[5]

Admissions officers from Harvard insist that they have never rejected an applicant based on race. Harvard has claimed for years that they have admissions-related documents

4 Expert Report of Peter S. Arcidiacono at Students for Fair Admissions, Inc., v. President and Fellows of Harvard College et al., No. 1:14-cv-14176-ADB (D. Mass, filed Jun. 15, 2018).

5 Janelle Lawrence and Patricia Hurtado, *Harvard's Own Admissions Chart Comes Back to Haunt It in Trial*, BLOOMBERG (Oct. 25, 2018), https://www.bloomberg.com/news/articles/2018-10-25/harvard-s-own-admissions-chart-comes-back-to-haunt-it-in-trial.

proving that they do not engage in racial discrimination, but Harvard's administration has expressed concerns over disclosing details of their highly selective admissions process to the public.[6] As a result, there is a dearth of information regarding whether or not the university is taking race into consideration in the admissions procedure. Furthermore, Harvard has argued that a completely race-blind admissions process would cause the number of African American and Hispanic students on campus to rapidly decline, resulting in a significantly less diverse student body.[7]

While the case concerning Harvard University is far from being the first of its kind, it will likely be a landmark case with vast implications for Harvard University and higher education institutions in general if it reaches the Supreme Court. In order to properly understand the significance of the Harvard case, it is important to acknowledge that race has been a factor of the college admissions process for decades. It is equally important to note that the practice of giving

6 *Lawsuit Accusing Harvard of Asian-American Discrimination Goes to Trial*, MSNBC. (Oct. 15, 2018), https://www.msnbc.com/velshi-ruhle/watch/lawsuit-accusing-harvard-of-asian-american-discrimination-goes-to-trial-1344643139784?v=railb&.

7 Lawrence and Hurtado, *supra* note 5.

special preference to minority applicants began with noble intentions and a sincere desire to atone for the United States' history of callous discrimination against African American citizens.

In a memorable speech at Howard University in 1965, President Lyndon Johnson declared that equal opportunity alone could not undo the impact of discrimination against African Americans throughout United States history.[8] While President Johnson believed that ending segregation and inequality were necessary steps to ensure equal opportunity, true equality could not be fully reached until minority groups were given preferential consideration in higher education and the workforce. The sentiments behind President Johnson's desired vision, commonly referred to as affirmative action, inspired many higher education institutions to establish special admissions programs geared toward minority students.

Such was the case at the University of California at Davis Medical School. In order to attain a racially diverse

8 President Lyndon Johnson, Howard University Commencement Address (Jun. 4, 1965).

student body, the University created a special admissions program with sixteen out of one hundred spaces reserved for minority applicants.[9] These minority applicants were also eligible to fill one of the other eighty-four spaces in the general admissions program if they were not accepted into the special program. Caucasian applicants, on the other hand, could not compete for a spot in the sixteen-space special program, even if their academic qualifications were significantly higher than those of the minority applicants. As a result of this system, Allan Bakke, a Caucasian, was denied admission to the Davis Medical School twice.[9] He sued the school on the grounds that the school's use of this racial quota system barred him from competing against minority applicants with lower GPAs and test scores.

When Bakke's case eventually reached the Supreme Court, the Court ruled that the quota system at Davis Medical School unconstitutionally violated the Fourteenth Amendment and Title VI of the Civil Rights Act of 1964. However, the Court still supported the goals of affirmative action, claiming that racial preferences could be permitted

9 Regents of the University of California v. Bakke, 438 U.S. 265.

as long as race was being considered as just one factor out of many in the admissions process. Thus, the Court supported affirmative action generally, but ruled that Bakke was denied equal protection in this specific case.[9] This paper will argue that *Regents of the University of California v. Bakke* (1978) was decided rightly for two reasons: first, the Court correctly established that racial quotas are both discriminatory and in violation of the Equal Protection Clause in the Fourteenth Amendment. Second, the Court wisely affirmed that in certain circumstances, diversity is a compelling government interest that justifies the use of racial preferences.

The primary argument in support of the Court is that discriminatory racial quotas violate the Equal Protection Clause. In Justice Powell's plurality opinion, he claimed that the "fatal flaw" in the University's quota system is its failure to acknowledge the individual rights guaranteed by the Fourteenth Amendment.[5] The Equal Protection Clause of the Fourteenth Amendment declares that no state shall "deny to any person within its jurisdiction the equal protection of the laws."[10] This important clause was crafted with the intent of

10 U.S. CONST. amend. XIV, §1.

ending discrimination, defined as "the unjust or prejudicial treatment of different categories of people, especially on the grounds of race, age, or sex."[11] In an attempt to remedy past discrimination, the University promoted an idea often referred to as reverse discrimination. Those who practice reverse discrimination intend to show favoritism to previously disadvantaged minorities, but at the same time, they experience the adverse effects of discriminating against those considered to be in the majority.

Though the Court recognized the University's noble goal of undoing past discrimination towards African American citizens, they determined that reverse discrimination was still discrimination and, therefore, violated the Fourteenth Amendment. Powell argued that "The guarantee of equal protection cannot mean one thing when applied to one individual and something else when applied to a person of another color. If both are not accorded the same protection, then it is not equal."[12] Even though reverse discrimination is used in order to correct a past wrong, it is in and of itself

11 *Discrimination,* OXFORD ENGLISH LIVING DICTIONARY (2019).
12 *See* Bakke, 438 U.S. 265.

discrimination: unjust treatment of one group while favoring the other. In this case, reverse discrimination benefitted minority applicants but harmed majority applicants such as Allan Bakke.

The court therefore ruled correctly that this racial quota system was unfairly infringing on Bakke's Fourteenth Amendment rights by giving special privileges to minority applicants. While minority applicants were eligible to apply to fill one of one hundred spaces in either the special admission program or the general program, Caucasian applicants were only permitted to apply for one of the eighty-four spaces in the general program. Because Caucasian applicants were excluded from the special program solely based on their race, this system falls under the "unjust treatment" aspect of discrimination.

The key problem with racial quotas is that they always result in one group being subject to exclusion due to race. The idea of using reverse discrimination in order to benefit disadvantaged applicants of one group only perpetuates discrimination by excluding members of a different group. Therefore, "reverse discrimination" is not

actually reversing discrimination at all but rather making the problem worse. In his "Radio Address to the Nation on Civil Rights," Ronald Reagan made a similar argument, claiming that quota systems are "discrimination, pure and simple, and [are] exactly what the civil rights laws were designed to stop."[13] Though the University of California's efforts to admit more minority students were commendable, they failed to realize that favoring one group of people inevitably leads to hindering another. This form of favoritism toward minority applicants violates the Equal Protection Clause.

Justice Powell reasoned that, in addition to the fact that racial quotas violate the Equal Protection Clause, quota systems lead to several negative impacts on minorities and majorities alike. One undesirable impact is that Caucasian students are forced to bear the heavy burden of a past injustice – discrimination against African Americans – that they were not responsible for causing. Powell addresses this negative consequence, arguing that "There is a measure of inequity in forcing innocent persons in respondent's position to bear

13 President Ronald Reagan, Radio Address to the Nation of Civil Rights (1985).

the burdens of redressing grievances not of their making."[14] More importantly, the presence of a racial quota system can easily lead one to believe that all admitted minority students were not capable of getting into the University based on their own merits. Rather, many people would reason that minority students were only admitted because of their race and might secretly deem them inferior or unworthy. Powell raised this concern in his plurality opinion, stating that these programs "may only reinforce common stereotypes holding that certain groups are unable to achieve success without special protection based on a factor having no relationship to individual worth."[7] Based on Powell's argumentation, racial quotas would only perpetuate the issue of racial discrimination instead of serving as a solution. Racial quotas are therefore not only unconstitutional but harmful to society at large.

The second argument in support of the Court's decision is that the attainment of a diverse student body is a compelling government interest that justifies the use of affirmative action. Though the Court clearly rejected the

14 *See* Bakke, 438 U.S. 265.

University's use of a quota system, they did not want to completely discredit the goals of affirmative action. Rather, the Justices reasoned that under certain circumstances, there are compelling government interests that can justify the use of affirmative action. Powell applied the time-tested strict scrutiny standard to this case in order to determine the legality of the University's affirmative action program.[15] Strict scrutiny requires that any regulation that restricts a constitutional right must be narrowly tailored and must achieve a compelling government interest in the least restrictive way possible. While the University provided four "compelling interest" claims, the Court found that only one of these interests met strict scrutiny standards – the attainment of a diverse student body. [16]

The attainment of a diverse student body "clearly is a constitutionally permissible goal for an institution of higher education" due to the fact that academic freedom has long been considered to be connected to First Amendment rights.[17] Twenty years prior, Justice Frankfurter in *Sweezy v.*

15 *Id.*
16 *Id.*
17 *Id.*

New Hampshire (1957) similarly claimed that universities have freedom granted by the First Amendment to determine not only what they will teach, but whom they will teach.[18] The freedom of universities to admit whomever they please leads many universities to seek students who can add diversity to their campus. While referencing *Sweezy v. New Hampshire*, Powell notes that "The atmosphere of 'speculation, experiment and creation' – so essential to the quality of higher education – is widely believed to be promoted by a diverse student body."[8]

Powell's assertion is supported by a wide array of research pertaining to diversity in university settings. A study conducted by UCLA's Higher Education Research Institute, for example, found that students who interacted with racially and ethnically diverse peers both inside and outside of the classroom were more likely to be engaged in active thinking, be motivated to do well academically, and show the most growth in intellectual skills when compared to their peers.[19] Other studies demonstrate that there are

18 Sweezy v. New Hampshire, 354 U.S. 234 (1957) (Frankfurter, J., concurring).

19 Eve Fine and Jo Handelsman, *Benefits and Challenges of Diversity in*

countless advantages to having diversity in schools, including increased creative skills, enhanced cognitive development, and more engagement within the classroom.[20]

Importantly, research shows that completely race-neutral admissions policies often result in a huge lack of minority students. A separate study by UCLA School of Law found that enrollment rates of African Americans, Asians, and Native Americans fell by more than 70 percent after UCLA adopted a class-based admissions system that excluded race from consideration.[21] Without the presence of these students, UCLA forfeits the significant benefits that flow from having a racially diverse student body. It is reasonable to argue, therefore, that race should have a role in the admissions process for any university that wants to attain genuine diversity. This consideration led the Court to determine that racial preferences, rather than quotas, can be used in the form of giving minority applicants an extra

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Academic Settings, UNIV. OF WI-MDN (2010), https://wiseli.wisc.edu/wp-content/uploads/sites/662/2018/11/Benefits_Challenges.pdf.

20 Roy Y.J. Chua*, Sharpening Your Skills: Organizational Design*, HARVARD BUSINESS SCHOOL (Nov. 2011), https://hbswk.hbs.edu/item/sharpening-your-skills-organizational-design.

21 Richard H. Sander, *Experimenting with Class-Based Affirmative Action,* 47 Journal of Legal Education 4, 472-503 (1997).

"plus" due to their race.[22]

It is crucial to acknowledge that diversity is not strictly limited to racial and ethnic qualities. The Court agreed that race is a huge factor of diversity so that it can be considered as a "plus" in the admissions process but only on the condition that race is just one of many determining factors. Other examples of diversity that can be considered include personal talents, unique service or work experience, leadership potential, maturity, and any other qualification "deemed important" by the university. Applicants who possess any of these special factors are also eligible to receive a "plus." Notably, in his plurality opinion, Justice Powell referred to Harvard University as a perfect example of a university using the "plus" system in their admissions procedures.

It is best to explain the "plus" system with an example: Student A, an African American student, and Student B, a Caucasian student, are both applying to the same university. Both applicants are academically talented, both have exceptional leadership skills, and both are

22 *See* Bakke, 438 U.S. 265.

accomplished athletes in their high schools. Their college applications are essentially indistinguishable. While the university would be thrilled to admit both of these highly qualified students, they are only able to admit one. If the university is seeking to expand racial diversity on campus, they would likely choose to admit Student A rather than Student B. Student B was not being excluded due to his race. Rather, he simply lacked a desired trait that Student A held: the ability to contribute to racial diversity on campus. In this situation, race was one small factor considered alongside a plethora of others. Additionally, each student was given a fair chance considering that both were eligible to apply and neither was discriminated against. The "plus" system is a perfect example of how the criteria for admissions cannot be dependent upon race but can sometimes be associated with it.

There are many advantages that result from having a diverse student body, and it is crucial that universities seek to diversify their campuses in order to provide students with a well-rounded education. Affirmative action in the form of a "plus" system is an effective way to ensure that

universities can consider race in their admissions processes in addition to acknowledging the many other factors that make students unique. Unlike discriminatory racial quota systems, this model ensures that no student is being excluded on the sole basis of skin tone or other biological qualities. This system supports the goals of affirmative action by allowing universities to give minority students a "plus" on their applications, but it is still in accordance with the Equal Protection Clause in the Fourteenth Amendment, because all applicants are given a fair chance.

Therefore, rather than imposing unfair burdens on minority students, the Court's decision in this case prevents racial discrimination by ensuring that all students are treated as unique individuals with diverse qualities and skills. While diversity is a worthy goal of any higher education institution, the use of discriminatory racial quotas for the sake of attaining a more diverse student body is in clear violation of the Equal Protection Clause in the Fourteenth Amendment and often leads to negative outcomes. Thus, the Court correctly concluded that universities could continue to consider race and ethnicity in their admissions processes,

granted that they also consider the many other factors that contribute to diversity.

Conclusion

The Court's decision in *Regents of the University of California v. Bakke* set a judicial precedent for several affirmative action cases decided in following years. The two most notable Supreme Court cases that were greatly influenced by the *Bakke* case are *Grutter v. Bollinger*[23] in 2003 and *Fisher v. University of Texas*[24] in 2016. Similar to Justice Powell's approach when contemplating the *Bakke* case, the opinions delivered by Justice Sandra Day O'Connor in *Grutter v. Bollinger* and Justice Anthony Kennedy in *Fisher v. University of Texas* utilized the strict scrutiny standard while evaluating the merits of each case. In *Grutter v. Bollinger*, for example, the Court determined that the University of Michigan Law School could legally use race as a factor in admissions decisions because the University effectively demonstrated that they had a narrowly

23 Grutter v. Bollinger, 539 U.S. 306 (2003).

24 Fisher v. University of Texas at Austin, 579 U.S. __ (2016).

tailored purpose of expanding diversity in the student body.[23] In *Fisher v. University of Texas*, the Court relied on the strict scrutiny test again when they held that the University of Texas' Top Ten Percent Plan was narrowly tailored to serve a compelling state interest of expanding racial diversity in higher education.[24] Conversely, the Court has utilized the strict scrutiny framework in order to demonstrate unconstitutional practices pertaining to affirmative action. In the desegregation case *Parents Involved in Community Schools v. Seattle School District No. 1*[25] in 2007, for example, Justice John Roberts argued that the school district's plan to prevent racial imbalances in their schools lacked a clear, narrowly tailored purpose; therefore, the school district's "racial balancing" plan was found to be in violation of the Equal Protection Clause of the Fourteenth Amendment. Overall, while there are a few exceptions, the Supreme Court justices have generally voiced support for using the strict scrutiny test when handling affirmative action cases.

Currently, many scholars and journalists speculate

25 Parents Involved in Community Schools v. Seattle School Dist. No. 1, 551 U.S. 701 (2007).

that the Harvard case will eventually reach the Supreme Court, as both the plaintiff and the defendant have stated that they will appeal the Federal District Court decision if they lose. Given the fact that the Court has historically relied on *Bakke* as a precedent when critiquing other affirmative action cases, it is reasonable to expect that the Court will rely on *Bakke* while evaluating Harvard University's' admissions procedures. If provided the opportunity to hear the Harvard case, the Supreme Court justices should acknowledge the precedent set in the *Bakke* case. Justice Powell's use of the time-tested strict scrutiny framework provides an effective way for the Court to handle the delicate balancing act between allowing universities to expand racial diversity on campus and preventing abuses of the anti-discriminatory language of the Fourteenth Amendment. Additionally, this method has been utilized not only in *Bakke*, but also in several other affirmative action cases that have taken place within the past few decades. In order to achieve diversity in a fair manner, Harvard University and universities nationwide should continue to adhere to the Court's guidelines established in *Regents of the University of California v. Bakke*.

TAX CUTS AND JOBS ACT OF 2017: SUCCESS OR FAILURE?

Richard W. Snyder, J.D., L.L.M.

ABSTRACT: *This article examines the implications and likelihood of accomplishing the stated objectives of the Tax Cuts and Jobs Act of 2017. After reviewing certain limited economic impacts realized to date, an evaluation of the positions of business and individuals as to whether the law properly addresses the global and domestic tax issues of the times follows. This paper also compares the approach taken in 2017 to that adopted in prior tax legislation. In conclusion, the 2017 approach has a high degree of achieving the desired results but in all likelihood will have to make necessary adjustments as dictated by actual results and future events.*

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I. Introduction[1]

In the current debates over looming U.S. and global issues such as infrastructure, healthcare, and climate change, discussions inevitably and inexplicably circle back to the enactment of the Tax Cuts and Jobs Act of 2017 (the "2017 Act"). In the eyes of many, the 2017 Act represents misguided priorities and economic mismanagement.

The purpose of this article is to offer a preliminary assessment of the likelihood of the 2017 Act's success. Results should be judged against the law's stated objectives of (1) tax relief for middle-income families, (2) simplification of the personal income tax code, (3) economic growth through tax relief and increased domestic investment and (4) repatriation of overseas earnings.

Notwithstanding the limited passage of time since the 2017 Act's enactment on December 22, 2017, the battlefield

1 I would like to acknowledge Grove City College accounting students Alexandria Rapson and Alec Allison for their excellent and timely tax research. The editors of this *Journal* also deserve much praise for their essential oversight and constructive suggestions. I owe a special thanks to Thomas Marchland, Esq. for his final reading of this paper as well as for his valued friendship spanning many decades.

testing of the 2017 Act after the 2018 corporate reporting and individual filing seasons provides objective evidence to demonstrate whether it has achieved its intended outcomes as well as unintended consequences. A short wish list herein presents suggestions for potential tax law amendments.

II. Relevant History

Tax reform has been brewing since the last major overhaul of the Internal Revenue Code (the "Code) in 1986. A review of other recent attempts to achieve a substantial rewrite lends help in better understanding the 2017 Act. As always, the attendant political, economic and social environment affected the shaping of, legislative path to and enactment of the final provisions comprising the 2017 Act.

A. Camp Proposal (2014)

Former Republican Senator David Camp and his working committee represented the most serious effort to enact true tax reform post-1986. He attempted comprehensive tax reform but focused primarily on converting the taxation of international operations from a worldwide concept to a

single country or "territorial system" of taxation as followed by many developed countries.

This effort culminated in 2014 with the Camp Proposal. It contained concepts of a one-time, low-tax, deemed repatriation of earnings (an idea borrowed from 2004 tax legislation) coupled with a complete conversion to a territorial tax system.

With a divided government, the proposal failed to gain traction. There was Democratic interest espoused by then-President Obama in only limited tax reform focusing solely on middle-class individual relief with offsetting increases to the corporate tax base. With this deadlock, the Camp Proposal was pushed aside but initiated a philosophical change to the U.S. approach to taxing multinational companies.

B. The Republican Tax Blueprint (2016)

Senator Camp passed the torch for championing the Republican version of tax reform to former Republican Representative and Speaker of the House Paul Ryan. Eminently qualified and versed in tax matters, Rep. Ryan had previously chaired the House Ways and Means Committee.

His working group set about crafting a long-term strategic plan for overhauling the nation's tax code with the overall objective of reducing budget deficits.

Primary targets for tax amendments were elimination of individual deductions for mortgage interest and state and local taxes. Entitlements, including social security and Medicare, would have been slashed as they represent a substantial percentage of annual federal expenditures. Although such proposals constituted political suicide for any candidate, the Republicans had nothing to lose since the chances of adoption at this time were nil. Significantly, the Republican Tax Blueprint initiated the discussion of eliminating certain individual itemized deductions as "pay-fors" in subsequent tax reform efforts.

C. Rush to Pass the Legislation (2017) –

"The Big Six"

The election of Candidate Donald J. Trump as President of the United States, along with existing Republican majorities in both houses of Congress, provided the alignment of political forces to enable enactment of

meaningful tax legislation. These unexpected events left the Republican party in total control of government but with limited time to deliver on the opportunity before the 2018 midterm elections. Furthermore, the Republicans lacked a cohesive legislative proposal for ready adoption. Given this dynamic, Congress fell back upon previous plans – the Senate on the Camp Proposal and the House on the Republican Tax Blueprint – as the only meaningful substantive works-in-progress.

With time and political capital wasted on a failed Obamacare repeal, a tax working group formed that summer to confidentially draft an outline of tax reform. This committee of six members (the "Big Six") was comprised of two members each from the Executive Branch, the House of Representatives and the Senate. Following were the Big Six members:

- Gary Cohn, National Economic Council Director
- Steven Mnuchin, Treasury Secretary
- Paul Ryan, Speaker of the House
- Kevin Brady, House Ways and Means Committee Chairman

- Mitch McConnell, Senate Majority Leader
- Orrin Hatch, Senate Finance Committee Chairman

Throughout the summer and fall of 2017, the Big Six experimented with various term sheets of their ideas. After gauging presidential, congressional, public and private reactions to their proposals, they reconvened to separately redraft the substance of what would eventually become the outline for the Ways and Means Committee and Finance Committee to propose separate tax reform legislation. Cuts to entitlement programs that were a cornerstone of Ryan's Republican Tax Blueprint were eventually taken off the table completely. Even ideas introduced by Rep. Brady to scale back tax incentives for employee benefit programs such as 401(k) plan savings were quickly scuttled. President Trump weighed in to attempt to control the dialogue surrounding the appropriate level of corporate income tax-rate cuts; thereby trying to deliver on a signature campaign promise. He would add significant non-tax amendments, such as permitting oil and gas drilling in the Alaska National Wildlife Area

Refuge (ANWAR), in the final stages of the 2017 Act further complicating the effort.

D. Budget Reconciliation Process

Owing to the small amount of time remaining before the perceived year-end deadline imposed by President Trump, the legislative calendar was extremely condensed, leaving no room for errors or missteps in the legislative process. Republican Senator Pat Toomey became the chief architect of utilizing the budget reconciliation process to get the tax legislation finalized. Through deft negotiation, he convinced his colleagues to agree up front to a total limit on the impact resulting from enacting tax reform via this process. This resulted in an essential caveat: the tax reforms could not be "scored" by the Congressional Budget Office (CBO) with a projected deficit in excess of $1.5 trillion over the prescribed ten-year scoring period (2018-2027). President Obama used this same approach to pass his signature healthcare overhaul just prior to seating of the 2010 class of incoming Senators that changed control of the Senate. Through this mechanism, the somewhat disparate 2017 House and Senate tax versions,

although separately adopted, would be reconciled. Identified differences were to be resolved by limited negotiations occurring between designated members of both houses of Congress. However, due to scoring by CBO that showed a deficit in excess of the cap, the bill was rewritten several times prior to and during reconciliation. The House and the Senate would then vote upon the compromise bill and it would finally be sent to the President for signature. This is exactly how the process played out in late 2017.

E. Lack of Bipartisanship

Final enactment of the 2017 Act contrasted with that attendant to passing the 1986 Tax Reform. In 1986, Democrat Dan Rostenkowski chaired the House Committee on Ways and Means. Republican Bob Packwood chaired the Senate Committee on Finance. Through partisan negotiation, they achieved comprehensive tax reform with the stated goals of tax reduction and simplification. Technical corrections followed within a reasonable time. The legislative blue book reflected the high level of cooperation between both major parties while also reflecting different philosophies on the

purpose of a particular tax revision. The 1986 law became part of President Reagan's legacy along with his initial Economic Recovery and Tax Act of 1981.

Contrast 1986 with the acrimony and dysfunction of the 2017 Congress. Although Republicans controlled both the legislative and executive branches, consensus on legislation was not assured. The Conservative Tea Party in the House and Republican presidential primary contenders Senators Ted Cruz and Marco Rubio each held their own views on what constituted meaningful tax reform. To gain votes from key senators, as well as the President, the bill was amended many times to add things such as Section 529 plan disbursements for pre-college tuition and enhanced childcare tax credits.

Acting as the spoiler, the Democratic offer and approach remained to fix the individual tax system first, and address the corporate and international wish list later. Not surprisingly, the Democrats were totally cut out of the process leading to clearly one-sided drafting and adopting of the new law. When the Republicans' intent to exclusively pursue their own vision of tax reform became clear, the

Democrats made it their sole mission to obstruct, undermine, and publicly spin the 2017 Act as an attack on middle-class America via giveaways to the wealthy and substantial corporate tax cuts and enhanced incentives. This centerpiece of the Democratic platform for the 2018 midterm elections met with great success.

The 2017 Act could not be finalized without drama. Toward the end of the process, a colloquy in the Senate between retiring Senator Hatch and Democrat Ron Wyden deteriorated into a perceived personal attack on Hatch's integrity alleging overall deceit on the American public. Adding insult to injury, the bill contained technical violations of the Senate's "Byrd Rule" applicable to budget reconciliation that required tweaks to the statutory wording. The President considered delaying the actual signing until January 2018 to deal with these finer points of order in the Senate Chamber. Democrats seized this moment to contend that the President could not, in fact, deliver on his promise of tax legislation by year-end. Thus, a hastily arranged signing by the President was orchestrated on the morning of December 22, 2017, with a minimally-attended

ceremony taking place that afternoon. Interestingly, Messers. McConnell and Ryan were not present for the signing event in the Oval Office. This brought an inglorious end to an expedited and convoluted process, but one that resulted in the most significant tax reform legislation in over thirty years. Moreover, the finalization of the 2017 Act still represents the most significant legislation passed by President Trump.

III. Results to Date

Several reports have been issued regarding the economic results of the 2017 Act. These include the Economic Report of the President, the Tax Policy Center and the Tax Foundation. The reports contain different and even disparate statistics in an attempt to shape the narrative. Nonetheless, the data presented does indicate certain financial trends resulting from enactment of the 2017 Act. Following is a summary of the various reports in an attempt to reach certain tentative conclusions regarding the effectiveness of the 2017 Act.

A. Increased U.S. Fiscal Deficits

The CBO scored the 2017 Act at a cumulative ten-year deficit of $1.5 trillion through 2027. Certain congressmen, including Senator Pat Toomey, predicted an even more robust economy. Results to date actually show increased U.S. fiscal deficits in 2018 of $779 billion. This represents a $113 billion, or 17%, increase in the overall deficit, constituting 3.9% of GDP (0.4% increase).[2]

Presently, the costs are much greater than revenues, with certain observers concluding that the overall increases in debt and deficits are unsustainable. Updated estimated increased deficits of $1.9 trillion by 2028 have been predicted by the CBO. At that rate, the 2028 federal debt would be 105% of GDP, its highest since World War II. Further extensions of tax sunset provisions would exacerbate the issue.[3]

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2 *Treasury: 2018 Deficit was $779 Billion* COMMITTEE FOR A RESPONSIBLE FEDERAL BUDGET, https://www.crfb.org/blogs/treasury-2018-deficit-was-779-billion (last visited Apr. 27, 2018).

3 Benjamin H. Harris and Adam Looney, *The Tax Cuts and Jobs Act: A Missed Opportunity To Establish A Sustainable Tax Code,* URBAN INSTITUTE AND BROOKINGS INSTITUTION 4 (2018), https://www.brookings.edu/wp-content/uploads/2018/05/es_20180524_harris-looney_taxreform.pdf.

B. Retained/Created More U.S. Jobs

Job retention and creation represented a centerpiece of the President's campaign for tax reform. An estimated 155,000 jobs were created in 2018.[4] Companies used tax savings to invest in workers immediately after the tax law came into effect. Other labor market effects showed increased average household income of between $3,400 and $9,900 with an average raise of $5,500. The issue is whether these were just one-time bonuses or ongoing base-wage increases. Data from the Bureau of Labor Statistics' Job Openings and Labor Turnover Survey says there was a sharp increase in labor demand directly after passing the law. Worker wage growth changed from a pre-enactment rate of 5.4% per year to a post-adoption rate of 9.3% per year. Such effects are expected to grow over time as a result of increased capital spending, raising the amount of capital invested per worker, labor productivity, and wages. However, there could be unfavorable impacts by the tax sunset policies expiring (see *infra*). Lastly, the enhanced child tax credit could encourage

4 Nichole Kaeding, *The Tax Cuts and Job Act After a Year,* TAX FOUNDATION (Dec. 17, 2018), https://taxfoundation.org/tcja-one-year-later/.

the birth rate and lead to a larger labor supply.[5]

C. Uses of Repatriated Funds

Many debates center upon whether corporations use the repatriated monies for "good or bad" purposes. Particular scrutiny was directed at "give backs," share repurchases, and capital distributions to shareholders. A major criticism of the tax law is that monies distributed to shareholders detract from expenditures that would otherwise grow the economy. This highlights an "agency conflict" that arise between shareholders and corporate managers. Firms have substantial cash flow in excess of that required to fund all projects having positive net present values when discounted at the relevant cost of capital. Essentially, share repurchases happen because firms have no projects worth pursuing, as the repurchases present no risk. Simultaneously, there has been an overall decrease in foreign investment in the U.S. representing outbound repatriation of U.S. investment. Along with the increase in domestic capital spending, there

5 ECONOMIC REPORT OF THE PRESIDENT, EXEC. DOC., 54-61 (2019).

has been a decrease in investments abroad.[6]

D. Growth in GDP of the U.S. Economy and Capital Spending

Deficits are driven by the impacts on overall Gross Domestic Product (GDP) caused by tax reform. Those estimates vary significantly from an average .3% (Moody's Analytics) to 2.1% (Tax Foundation) for the ten-year scoring period.[7]

Economic output and investments have improved with increases in capital spending. The 2017 Act increased the United States' GDP higher than the 2.0% projected for 2018 at an actual growth of 3.0%. The original CBO 2017 pre-enactment estimate was 2.5% lower than current projection. Its 2017 estimate was also 1.2% lower than the current projection.[8]

Regarding tax revenue, the CBO still estimates a deficit increase between $480 to $600 billion over ten years.[9] Tax revenue as a percentage of GDP is also enjoying

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6 ECONOMIC REPORT *supra* note 5, at 67-69.
7 Harris and Looney, *supra* note 3, at 7.
8 ECONOMIC REPORT *supra* note 5, at 47-50.
9 *Id.*, at 49-50.

a relative increase. Benchmark rates referenced for different time periods include:

1962 to 2016:	17.4%
2018-2022:	16.7
2028 (without sunset provisions):	18.5
2028(with sunset provisions):	17.5[10]

IV. Benefits

A. Update needed for Internal Revenue Code to reflect changes in global business practices and to make the United States more competitive and fairer through lower tax rates

Dramatic changes have occurred in business since 1986, due to technological innovation and electronic commerce. At the same time, sophisticated and systematic tax-avoidance techniques have placed stress on taxation systems. Additionally, globalization of business caused more foreign direct investment to take place outside of the United States. Multinationals were seeking low-cost labor and

10 *How Did the TCJA Affect the Federal Budget Outlook?* TAX POLICY CENTER, https://www.taxpolicycenter.org/briefing-book/how-did-tcja-affect-federal-budget-outlook (last visited Apr. 27, 2018).

cheaper raw materials in foreign countries. This resulted in U.S. companies' willingness to outsource and offshore both manufacturing and service jobs. Thus, the 2017 Act aimed to solve two major issues: rising international capital mobility and increasingly uncompetitive U.S. business taxation relative to the rest of the world.[11]

Foreign countries' aggressive lowering of income tax rates to attract inbound investment away from the U.S. led to a wave of corporate inversions since 2000. Certain Obama Executive Orders reacted to the proliferation of outbound transactions coupled with leveraging of US-based operations. The 2017 Act focused on this harmful tax planning and had an immediate and large effect on business.[12]

B. Removed Impediments that Kept Foreign Earnings Offshore

The U.S. moved from a worldwide system of taxation to a nominally territorial one. The old system discouraged companies from repatriating foreign profits. Prior to the 2017 Act, the law encouraged companies to move legal

11 ECONOMIC REPORT *supra* note 5, at 62-67.
12 *Id.*

headquarters out of the U.S. through inversions and other tax planning techniques.

The new approach relies upon a borrowed "participation exemption" concept that exempts from domestic taxation most foreign remittances to the U.S. Foreign dividends paid to U.S. parent corporations are exempt because they are fully deductible, subject to certain conditions, including ownership and holding period. No exemption is allowed if the dividend also received a tax benefit in the other country, such as a foreign tax deduction.[13]

The "deemed repatriation" required that accumulated foreign earnings were remitted to the US, albeit at a lower tax rate payable over a number of years. Liquid assets deemed repatriated were assessed at a 15.5% tax with a lower rate on non-liquid assets of 8%. Of the estimated $4.3 trillion held abroad, approximately $571 billion has been repatriated in the first three quarters of 2018. Importantly, there have been a number of inbound transactions. This represents assets coming back to the U.S. due to the perceived adverse

13 Kyle Pomerleau, *A Hybrid Approach: The Treatment of Foreign Profits Under the Tax Cuts and Job Act,* TAX FOUNDATION (May 3. 2018), https://taxfoundation.org/treatment-foreign-profits-tax-cuts-jobs-act/#_ftn4.

Global Intangible Low-Taxed Income (GILTI) and beneficial Foreign Derived Intangible Income (FDII) tax provisions.

Overseas profits purportedly are finding their way back to the US. Although pessimistic on the 2017 Act, Mark Whitehouse of Bloomberg offered:

> Before 2018, U.S. nonfinancial corporations tended to add about $50 billion to earnings held abroad every three months. But in the first three months of 2018, that number turned to a negative $158 billion, according to the Federal Reserve. That's the biggest reversal on record going back to 1946, and much more than companies brought back in 2005, the last time the government tried something similar.

Procter & Gamble (P&G) spokesperson Ms. Jennifer Corso said P&G actually repatriated about $7 billion back to the U.S. in the 2018 fiscal year or 14% of its $49 billion held offshore. The P&G money was repatriated in the form of dividends ($7.3 billion), share buybacks ($7 billion) and capital spending ($400 million increase).

C. Encourage Domestic Innovation without Exporting Intellectual Property

New tax incentives mimic the Irish tax structure in an attempt to retain intellectual property domestically versus

exporting via buy/sell and research and development cost share arrangements with foreign affiliates. Under the new tax FDII provision, a corporation pays an effective rate of 13.125%, rather than 21%, on its above-routine income arising from foreign markets. A taxpayer claiming FDII is eligible for a deduction of 37.5% for taxable years beginning after December 31, 2017 through taxable years beginning before January 1, 2025. This results in an effective 13.125% tax rate (the 21% corporate tax rate multiplied by (1 - 0.375)). After December 31, 2025, the deduction declines to 21.875%, resulting in a rate of 16.406% (21% multiplied by (1 - 0.21875)). [14]

Traditionally, the U.S. has relied upon a tax incentive to promote exports. Some argue that this is fundamentally opposed to normal tax principles. However, FDII only applies to "C" corporations. The subsidy is zero for export income earned by "S" corporations, partnerships, limited liability companies, and individuals. As an export incentive,

14 Jane Gravelle and Donald Marples, *Issues in International Corporate Taxation: The 2017 Revision (P.L.115-97),* CONGRESSIONAL RESEARCH SERVICE (May 1, 2018), https://fas.org/sgp/crs/misc/R45186.pdf.

FDII is viewed as favoring pharmaceutical and technology companies over manufacturing.[15] Finally, the deduction for FDII can be viewed as a destabilizer that does not provide tax benefits when businesses need them the most.[16]

D. Flexibility Afforded via Future Tax Rate Adjustments as Needed

The corporate income statutory tax rate was dramatically reduced from 35% to 21%. Yet, future tax rates can be adjusted in either direction as appropriate. This is similar to post-1986 tax reform, where marginal individual rates were raised to 39.6% and the corporate rate was adjusted to 35%. Already, it has been suggested that Congress immediately reverse these 2017 windfall tax cuts and move towards a traditional broad-base income tax at the individual, corporate and shareholder levels.[17]

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15 Martin Sullivan, *Economic Analysis: What Economic Purpose Does FDII Serve?* TAX NOTES (Oct. 16, 2018), https://www.taxnotes.com/tax-reform/economic-analysis-what-economic-purpose-does-fdii-serve.

16 Tim Dowd and Paul Landefeld, *The Business Cycle and the Deduction for Foreign Derived Intangible Income: A Historical Perspective,* 71 NATIONAL TAX JOURNAL, 729, 729-750.

17 Harris and Looney, *supra* note 3, at 4-5.

E. Simplification of Individual Taxation Through Increasing the Standard Deduction

Substantial simplification resulted from increasing individual tax allowances, standard deductions and credit incentives. In effect, the 2017 Act swapped personal exemptions for generous child tax credits and resulted in a huge increase in the number of persons taking the standard deduction to the 90% level (a 20% increase). It is estimated that this reduces compliance costs by $3 billion to $5 billion.[18] An increase of real disposable income per household also resulted from this, although estimates vary widely.[19]

F. Appropriate response to Organization for Economic Cooperation and Development (OECD) Base Erosion and Profit Shifting (BEPS) by installing U.S. Base Erosion Anti-abuse Tax (BEAT)

18 Kaeding, *supra* note 4.

19 Harris and Looney, *supra* note 3, at 4-5.

The Europeans had implemented a tax regime to prevent moving income to low-tax jurisdictions and creating mismatches of income and deductions to reduce the overall tax base. The U.S. has responded with the BEAT adoption. BEAT only applies to "C" corporations and with a gross receipts threshold. A significant exception exists based upon the level of the cost of goods sold thereby befitting manufacturing companies.[20] BEAT starts at 5% beginning with the 2018 calendar year, then ratchets up to 10% after that first year and jumps again in 2026 to 12.5%.[21] BEAT becomes more complex once FDII and the GILTI tax (see below) and subsidiary companies are layered into the calculations.

Some fear that BEAT threatens to impact the finances of insurance companies when they are most vulnerable when paying out claims. "It's going to drive up premiums and it's going to make it more expensive for

20 Luis Abad, et al., *Tax Reform May Be the Epicenter, But Be Wary of Trade and Customs Aftershocks,* BLOOMBERG BNA (March 9, 2018), http://src.bna.com/BV2.

21 Kimberly Majure and John DerOhanesian, *INSIGHT: Fundamentals of Tax Reform: BEAT,* BLOOMBERG (Sept. 21, 2018), https://www.bna.com/insight-fundamentals-tax-n73014482752/.

property and casualty insurance," said Bernie Pastille, tax partner at Morrison & Forester LLP.[22] Others believe that it will penalize transactions that are already under scrutiny for transfer pricing compliance. This is one reason why foreign governments are likely to challenge BEAT.[23]

Detractors notwithstanding, many believe that BEAT is working as intended. The Coalition for American Insurance states that "It already has helped to prevent base erosion, level the playing field and stop companies from leaving the United States through inversions." The usual critiques of BEAT involve often illogical hypotheticals with an extremely low likelihood of actually occurring.[24] As expected, the U.S. Treasury Department has promised regulations spelling out guidance. Lawmakers have also said they are listening to companies' concerns and considering potential changes. One particular area of ambiguity concerns

22 Ezequiel Minaya and Nina Trentmann, *A Tax Change Threatens to Hit Insurers When Most Vulnerable,* THE WALL STREET JOURNAL (Aug. 21, 2018), https://www.wsj.com/articles/a-tax-change-threatens-to-hit-insurers-when-most-vulnerable-1534843801.

23 Elizabeth Stevens and Peter Barnes, *INSIGHT: BEAT Strikes the Wrong Note,* BLOOMBERG (March 16, 2018), http://www.capdale.com/files/22787_insight_beat_strikes_thewrong_note.pdf.

24 Harry Ballan, *U.S. WTO Violations: Will This Time Be Different?* 9 COLUM. J. TAX L. TAX MATTERS 14 (2018).

purchases from non-US companies and whether the tangibles and intangibles have to be separated for the BEAT.[25]

G. World Trade Organization (WTO) Scrutiny of FDII and BEAT

There is a decades-long history of the WTO successfully challenging U.S. export incentives. First came the Domestic International Sales Corporation (DISC), then Foreign Sales Corporation (FSC) which was replaced with Extraterritorial Income Exclusion (ETI). The WTO successfully challenged all of them. The Bush-era replacement using the Section 199 deduction was suspect. At the very least, adoption of FDII and BEAT will allow time for the U.S. to continue to protect its domestic businesses[26].

Potential violations by FDII revolve around whether FDII is a prohibited export subsidy under WTO rules. The Agreement on Subsidies and Countervailing Measures (SCM) bars "prohibited subsidies," which include "the allowance of special deductions directly related to exports or export performance, over and above those granted in respect

25 Minaya and Trentmann, *supra* note 22.
26 Gravelle and Marples, *supra* note 14.

to production for domestic consumption."[27] Under OECD and SCM standards, FDII could violate the minimum standard for preferential regimes. Specifically, it may violate the OECD BEPS Action 5 recommendations on substantial activity requirements for intellectual property (IP) incentive regimes. Digging in, the U.S. Treasury believes that the FDII rules comply with the BEPS Action 5 recommendations.[28] Some argue that FDII should never have been enacted due to its added complexity. Others support making FDII elective so that firms operating in certain countries do not have to use FDII**.** Still other ideas include making FDII limited to just royalties.[29]

H. Repeal of the Corporate Alternative Minimum Tax (AMT)

For decades, individuals and corporations alike have reviled the AMT for its complexity and failure to index for inflation until after 2012. Minimum Tax Credits (MTCs)

27 Ballan, *supra* note 25.

28 Robert Sledz, *European Commission Says U.S. BEAT and FDII Rules May Violate Int'l Standards,* THOMSON REUTERS (June 20, 2018), https://tax.thomsonreuters.com/blog/european-commission-says-u-s-beat-and-fdii-rules-may-violate-intl-standards/.

29 Gravelle and Marples, *supra* note 14.

were stockpiling for certain cyclical industries typically in the heavy manufacturing sector. Congress responded by eliminating the corporate AMT but left the individual AMT intact albeit subject to certain new indexing and exemption rules. Further, following the lead of the 1986 Tax Reform vis-a-vis investment tax credits, unused MTCs were "cashed out" pro rata for corporations. The total benefits realized by both the 2017 corporate AMT repeal and refunds are substantial and represent a vast improvement from a tax administration viewpoint over the prior AMT regime. Eliminating the AMT was important but, ultimately, updating the outdated international tax regime with a global minimum tax was the overall goal, e.g. GILTI.[30]

V. Detriments

A. Increased the budget deficit by more than $1.5 trillion over the next ten years

Recently, the U.S. Economic Council admitted that the optimistic view for maintaining reasonable budget deficits

30 Harris and Looney, *supra* note 3, at 4-5.

may not be sustainable. New estimates (CBO: Congressional Budget Office) under differing methods reveal the extent of expected deficits. Under a "Conventional" method, the deficit is projected at a cumulative $1.9 trillion. Outlier estimates include those calculations pursuant to a "Dynamic" method at the low end of $1.4 trillion but factoring in extra debt service costs takes both the Conventional method to $2.3 trillion and Dynamic method at $1.9 trillion. The consensus is that this needs increased tax revenue. In order to stabilize debt in the long term, the Treasury requires revenue of 21% of GDP and more incentives toward labor supply and investment.[31]

Many are concerned that this is only the realization of one-time benefits. This remains an unanswered question. The overriding problem is whether there is just temporary economic growth causing the economic impetus from tax stimulus to be overstated.[32]

31 ECONOMIC REPORT *supra* note 5, at 46-48.

32 Harris and Looney, *supra* note 3, at 1-29.

B. Sunset provisions versus Long-Term Benefits of Certain Incentives

Owing largely to CBO scoring constraints, certain significant business incentives such as bonus depreciation and immediate expensing of fixed assets purchased will expire after only five years. The following sunset provisions (for the period from Jan. 31, 2017 to Jan. 1, 2026) are scheduled:

- New income tax rates and brackets
- Standard deduction increase
- Personal exemption set to zero
- New limitation on "excess business loss"
- Deduction for personal casualty and theft losses not allowed
- Gambling loss limitation modified
- Child tax credit increase
- SALT deduction
- Mortgage and home equity indebtedness interest deduction limited
- Medical expense deduction threshold temporarily reduced (ends Jan. 1, 2019)
- Charitable contribution deduction limitation increase

- Miscellaneous itemized deduction not allowed
- Overall limitation ("Pease" Limitation) on itemized deductions not applicable
- Qualified bicycle commuting exclusion not applicable
- Exclusion for moving expense reimbursements not applicable
- Moving expenses deduction not applicable
- AMT retained, with higher exemption amounts
- ABLE account changes
- Student loan discharged on death or disability
- Estate and gift tax retained, with increased exemption amount
- Temporary 100% cost recovery of qualifying business assets (ends Jan. 1, 2023/2024)
- New credit for employer-paid family and medical leave
- New deduction for pass-through income (Qualified Business Income (QBI))
- Deduction for FDII and GILTI
- Election with respect to foreign tax credit limitation[33]

33 *Tax Cuts and Jobs Act: Overview of Provisions that Sunset (Expire)*, MAXWELL LOCKE & RITTER (Jan 11, 2018) https://www.mlrpc.com/articles/tax-cuts-jobs-act-overview-provisions-sunset-expire/.

The estimated upside from making the sunset provisions permanent is that the U.S. could see its long-term growth go from 2.6% to 5.7% of GDP.[34] The potentially harmful impact from the various sunset provisions is caused by uncertainty about the future. This allows hard decisions to be punted to future administrations.[35]

C. Complexity Added

As expected from legislative initiatives, the goals may be straightforward but the approach and solution can become convoluted in application. Unsurprisingly, enforcement of the 2017 Act is proving complicated. Many provisions are unclear and require clarification through the issuance of detailed regulations. [36]

The BEAT, GILTI and FDII provisions are exceedingly complex, leaving many technical questions unanswered, and they remain a large part of the regulation projects and technical corrections. Lawmakers claim that they are listening to companies' concerns and considering

34 ECONOMIC REPORT *supra* note 5, at 53-54.
35 Harris and Looney, *supra* note 3, at 1-2.
36 *Id.*

potential changes. Ambiguity is especially prominent for BEAT. For example, practitioners are asking if the tangibles and intangibles have to be separated for BEAT for any purchase of a non-U.S. company.

D. Contains Significant Worldwide Taxation of Global Intangible Low-Taxed Income

An outcome of the 2017 Act was updating an international tax with a global minimum tax system. The GILTI rules added by new Sections 250 and 951A, and revised Section 960. The GILTI inclusion for a tax year equals the excess of the shareholder's net Controlled Foreign Corporation (CFC) tested income over its deemed tangible income return. A company would not owe additional U.S. tax if it was being taxed at the 13.125% threshold rate of foreign taxation. The drafters wrapped GILTI into the existing architecture for foreign tax credits. Many companies, however, are finding that they're paying more than 13.125% in foreign tax, but also facing a significant tax liability to the U.S. government under the GILTI regime. It particularly affects the technology, pharmaceutical,

manufacturing and banking/financial services industries. Unintended consequences include the potential loss of foreign tax credits. The 2017 Act was not designed to account for timing differences between U.S. and foreign taxes. It imposes tax on a current basis on active foreign income without deferral. Because it penalizes U.S. companies that have been acquired, it could discourage future mergers and acquisition transactions. Of the newly enacted taxes, GILTI creates the most burden in terms of financial impacts (40%) and compliance difficulty. Thankfully, GILTI only applies to gross income when subpart F does not apply to gross income.

Already, companies have lodged complaints about impacts from adverse GILTI taxation. Cincinnati-based P&G's CFO, Jon Moeller, indicates that GILTI discourages local job creation. P&G might be forced to move some of its operations overseas in order to compete and avoid an extra 2-3% U.S. tax on of its foreign earnings. So far, P&G claims that its domestic employment has been reduced by approximately 3,000 workers. Its effective tax rate of 36.6% has not changed from 2017 to 2018. Apple has repatriated $252.3 billion in foreign cash without a major tax impact

and is planning to use the excess for dividends. It seems that both P&G and Apple have been seen utilizing these new funds in the U.S. for the betterment of the company and its shareholders. P&G has used the money funneled back to the U.S. for dividends and capital spending. Apple seems to be planning to use the extra cash for dividends. This represents an immense benefit for the American economy. What has not happened, however, is the creation of jobs. Apparently, neither of these companies, nor any other large companies, have utilized this money for new jobs. In fact, P&G has decreased its U.S. workforce in the past year. The ultimate question may be who the more important stakeholder is: the companies, U.S. government, investors, local communities, or employees?

E. Done Hastily and in Need of Substantial Technical Corrections/Revisions

Consensus among experts is that there are difficulties with this tax reform. The legislation was passed by Republicans without any Democratic support. Amending or correcting the 2017 Act requires consensus among the

Joint Committee of Taxation, U.S. Treasury Department, Senate Finance Committee and the House Ways and Means Committee. The Senate has to deliver 60 votes in order to pass the technical corrections package over a Democratic filibuster. Senate Democrats believe the tax reform was enacted without their input and created bad policy by favoring tax breaks for corporations over individuals. Thus, a much-needed and timely technical corrections bill is not assured.

Many groups have weighed in on needed changes. For example, the AICPA suggested guidance in the following areas.

- Net operating losses (NOLs) need rules to change from tax years ending after December 31, 2017, that date, in order to accommodate fiscal year taxpayers.
- Qualified improvement property (QIP) is not mentioned in Section 168(e)(3)(E).
- Depreciation provisions also need to allow for bonus depreciation, leaving some property with a life of 39 years.
- Charitable contribution deduction has drafting errors in Section 170(b)(1)(G)(iii) regarding the gross income and charitable deduction limitation. The current wording does not allow for the 60%

deduction as Congress had intended but instead still limits it to 50%. [37]

F. Shifted the Tax Burden to the States Through Limiting Certain Itemized Deductions

Even prior to enactment, the relationship between the Federal government and the states had become toxic. State and local tax (SALT) deductions were pared back substantially, generating rushed, aggressive tax strategies advanced in 2017 and 2018 by state governments. In response, the IRS barred prepayment of 2017 and 2018 state tax. Various state workarounds were concocted. In exchange for tax credits on their residents' state tax returns, New York designed "charitable funds" for education and other services. Proposed NY legislation allowed charitable contribution – to generate SALT credits earned in a roundabout manner by allowing related contribution deduction. One by one, these gimmicks are being shut down by IRS notices and

37 *AICPA Sends Congress Recommended Technical Corrections to New Tax Law,* AICPA (Feb. 22, 2018), https://www.aicpa.org/press/pressreleases/2018/aicpa-sends-congress-corrections-to-new-tax-law.html.

regulation.[38]

Individual impacts were acknowledged and conceivably could have had intended targets. The limitations mainly affected high-income individuals in high-tax states, in primarily the top 20% of income earners. It is also hurting median income house owners (average income level of $65,000) as $4,000 personal exemption and mortgage interest deductions were also lost. The new law includes limitations on deducting interest on HELOCs (Home Equity Lines of Credit). Some worry whether it may indirectly cause issues with home ownership among lower income families.[39]

G. Enacted Corporate Tax Reductions but Less for Individuals

Many contend that the middle class and below are

38 Kelly Smith, *Changes to the State and Local Tax (SALT) Deduction Hitting Taxpayers Hard,* BANKRATE (Apr. 10, 2019), https://www.bankrate.com/taxes/salt-tax-deduction-cap-hitting-taxpayers-hard/ and THOMSON REUTERS CHECKPOINT, https://checkpoint.riag.com/app/login?usid=2c93a2x138d1f&feature=ttoc&lastCpReqId=2fe46c8&lkn=lloginAllParm&server=18476&tempId=D9E43DAD1F20111B19A3B060A12FD87Dhhlbv6347562.t.20190420-133438 (last visited Apr. 27, 2018).

39 Kyle Pomerleau, *Eliminating the SALT Deduction Cap Would Reduce Federal Revenue and Make the Tax Code Less Progressive,* TAX FOUNDATION (Jan. 4, 2019), https://taxfoundation.org/salt-deduction-analysis/.

not realizing any tax benefits. Right or wrong, Democrats have effectively marketed and convinced the public that only the top 1% of Americans are receiving significant tax breaks. Public sentiment provides the greatest risk to the longevity of the 2017 Act. Already, 2020 Democratic presidential candidate Kamala Harris is pledging "day one" repeal of the law.

VI. Comparison to Other Recent Tax Acts

A review of significant past tax acts going back to the Reagan years and continuing through the Obama presidency provides insight into the structure and approach in the 2017 Act. New concepts of sunsetting, indexing and bonus depreciation are now combined in the 2017 Act with traditional up/down tax rate adjustments and capital gain taxation. The ebb and flow of Republican- and Democrat-controlled governments over the past thirty years also reveals political strategies, such as use of the budget reconciliation process. A common thread is the reaction to the times by each government as present-day crises required immediate

attention. Short as well as long-term policy decisions became embodied in the various tax legislation enacted.

A. Economic Recovery Tax Act of 1981 (ERTA)

Representing newly-inaugurated President Reagan's first signature legislation, ERTA reduced the top two individual tax brackets from 70% to 14%, and from 50% down to 10%. ERTA also slashed estate taxes, capital gains, and corporate taxes. Safe-harbor leasing became a method to shift depreciation deductions to those companies that benefited most from them. ERTA's avowed purpose and signature accomplishments were directed at the struggling economy Reagan inherited. ERTA succeeded in jump-starting that economy and taming inflation. On the downside, it introduced parameters for indexing the tax code for inflation and created issues with bracket creep. Critics argued that ERTA worsened federal deficits (although actually more a result of increased defense spending), whereas supporters correctly emphasized how it bolstered the economy.[40]

40 Economic Recovery Tax Act of 1981 (ERTA). Pub. L. No. 97-34 (1981).

B. Tax Equity and Fiscal Responsibility Tax Act of 1982 (TEFRA)

TEFRA contained provisions primarily for the U.S. health care system. Reversing prior incentives, it repealed scheduled increases in accelerated depreciation deductions, tightened safe-harbor leasing rules, required taxpayers to reduce basis by 50% of investment tax credits, instituted 10% withholding on dividends and interest paid to individuals, tightened completed contract accounting rules and increased the Federal Unemployment Tax Act (FUTA) wage base and tax rates. Its purpose primarily was to address issues with ERTA. Actual results included an increase of tax revenues by almost 1% of GDP. However, promised budget cuts of $3 reducing spending for every $1 of tax revenue raised never happened. Passage of the bill was controversial. The House version would have lowered taxes, while the Senate version added a variety of provisions which increased taxes. Eventually, President Reagan signed the Senate bill into law. Noteworthy, as a case of first impression, a lawsuit was filed by a private citizen Garrison R. Armstrong who claimed a

violation of the Origination Clause that requires revenue bills to originate in the House. Ultimately, the courts ruled in favor of the government saying that the Senate did not exceed its authority by adding such provisions. Unflatteringly, it is the largest peacetime tax increase in history achieved primarily through the cancellation of tax cuts.[41]

C. Tax Reform Act of 1986 (TRA 1986)

TRA 1986 represented the first major rewrite of the Code since 1954 thereby earning the right to rename it the "Internal Revenue Code of 1986." Its avowed purpose was to simplify the tax code, broaden the tax base and eliminate tax shelters. TRA 1986 achieved the following :

- Lowered tax brackets from 50% to 38.5%
- Increased standard deduction
- Increased personal exemption
- Increased earned income credit
- Made only mortgage interest deductible
- Added low-income housing tax credit
- IRA deduction severely restricted

41 Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA) Pub. L. No. 97-248 (1982).

- Restricted depreciation deductions
- Defined contribution pension plan deductions were curtailed
- Added general nondiscrimination rules to 403(b) plans
- Required SSN for children claimed as dependents
- Expanded AMT to hurt tax shelters even more
- Passive loss adopted[42]

D. Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA)

EGTRRA's purpose was to deliver on a tax cut as promised in Bush's campaign with Clinton era surpluses to allow reduced taxes. A partisan bill, it passed through the budget reconciliation process. EGTRRA first introduced sunsetting provisions and allowed for tax rebates, income brackets with 10% being the lowest bracket and 39.6% highest bracket to be lowered to 35% by 2006, increased standard deduction, capital gains tax reduced from 10% to 8% for those in the 15% income bracket, qualified retirement

42 Tax Reform Act of 1986 (TRA). Pub. L. 99-514 (1986).

plans, educational savings incentives and estate and gift tax rules.[43]

E. Jobs and Growth Tax Relief Reconciliation Act of 2003 (JGTRRA)

Simply put, JGTRRA was singularly focused as a tax cut to help the economy recover from the lingering effects of the 9/11 tragedy. Despite being a partisan bill, it barely passed with the Vice President having to break the Senate tie. The act spurred capital spending via accelerated credits and rate reduction achieved by lowered tax brackets to 10% and 35%, increased percentage rates of depreciation, decreased capital gains tax to 5% and 15% and by instituting the concept of "Qualified Dividends."[44]

F. Homeland Investment Act of 2004 (HIA)

HIA's purpose was to increase investment in America by building plants, increasing research and development and creating jobs. That act's main impact was to allow a one-time

43 Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA). Pub. L. 107-16 (2001).

44 Jobs and Growth Tax Relief Reconciliation Act of 2003 (JGTRRA). Pub. L. 108-27 (2003).

cash dividend at a reduced effective rate. Specifically, money was not to be used to raise dividends. Actual remittances amounted to approximately $300 billion that came back with 92% constituting taxable dividends. Repatriations surged from an average of $62.2 billion per year from 2000-2004 to $298.7 billion in 2005 under the tax holiday, before falling to $91.1 billion in 2006. Consensus was that HIA still benefited the U.S. economy even though the funds were not actually used as intended, for capital expansion and job creation.[45][46]

G. Tax Increase Prevention and Reconciliation Act of 2005 (TIRPA)

Serving a housekeeping purpose, TIRPA prevented several sunsetting policies from expiring. Largely a partisan bill, controlling Republicans were in favor of a tax cut for the wealthy. The bill included an extension of reduced rates on capital gains and AMT tax, a two-year extension

45 Dhammika Dharmapala, et al., *Watch What I Do, Not What I Say: The Unintended Consequences of the Homeland Investment Act,* NAT. BUREAU OF ECON. RESEARCH (Jun. 2009), https://www.nber.org/papers/w15023.pdf.

46 Floyd Norris, *Tax Breaks for Profits Went Awry,* NEW YORK TIMES (Jun 4, 2009), https://www.nytimes.com/2009/06/05/business/05norris.html.

of enhanced Section 179, of capital gain tax treatment on self-created musical works, taxation of passive income of minors, conversions to Roth IRAs, as well as changes to the foreign income exclusion. [47]

H. American Recovery and Reinvestment Act of 2009 (ARRA)

The onset of the Great Recession necessitated more tax relief to save existing jobs and create new ones, provide temporary relief for those most affected by the recession and invest in infrastructure, education, health, and renewable energy. Under President Obama, and with Democratic control of both the House and Senate, ARRA was an understandably Democratic bill, focusing on individual tax relief and subsidizing renewable energy initiatives. The bill's "Buy American Provision" particularly angered Canadian businesses. Many economists supported the stimulus; some supported an even larger package. Other economists disagreed with the bill's Keynesian principles. It mostly provided tax incentives for individuals.

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47 Tax Increase Prevention and Reconciliation Act of 2005 (TIRPA). Pub. L. 109-222 (2005).

There were limited tax incentives for companies in recognition of the accumulation of huge net operating losses (NOL) starting in 2009. There were now NOL carrybacks for five years, renewable energy credits, repeal of bank credits and more bonus depreciation allowances.[48]

I. Tax Relief, Unemployment Insurance Reauthorization, Job Creation Act of 2010

This bill extended sunsetting provisions from the "Bush Tax Cuts" in ARRA for two more years. Although it became a bipartisan bill, it was nonetheless opposed by conservative Republicans who objected to growing deficits. It also addressed some companies' difficulties updating payroll taxes. As is customary, the IRS had to update their systems to handle the new itemized deduction changes. In addition to extending the Bush Tax Cuts and ARRA, it patched AMT, gave a 13-month extension on FUTA benefits and a one-year reduction of FICA payroll taxes.[49]

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48 American Recovery and Reinvestment Act of 2009 (ARRA). Pub. L. 111-5 (2009).

49 Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (2010 Tax Relief Act). Pub. L. 111-312 (2010).

J. The American Taxpayer Relief Act of 2012

This law represented a compromise: it further extended the Bush tax cuts while incorporating Obama's insistence on maintaining higher taxes on the wealthy. At the time, it was projected to add $3.9 billion to the deficit.

Although it passed with Republican Senate support, House Republicans voted against it. Overall, it passed successfully. In a way, it was the biggest tax cut in history. If this had not passed, 2013 rates would have been much higher. [50] Called a "Republican fiscal dream" by New York Times (NYT),[51] the Committee for Responsible Federal Budget said it averted an economic disaster, but failed to fix many issues such as deficit spending.[52] Paul Krugman of the NYT said that revenue needed to be increased more and deficits needed to be reduced by 2% of GDP to stabilize the long-run debt situation.[53]

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50 American Taxpayer Relief Act of 2012 (ATRA). Pub. L. 112-240 (2012).

51 Jonathan Weisman, *Lines of Resistance on Fiscal Deal,* NEW YORK TIMES (Jan. 1, 2013), https://www.nytimes.com/2013/01/02/us/politics/a-new-breed-of-republicans-resists-the-fiscal-deal.html.

52 *The Good, the Bad, and the Ugly in the Fiscal Cliff Package,* COMMITTEE FOR A RESPONSIBLE FEDERAL BUDGET (Jan. 1, 2013), http://www.crfb.org/blogs/good-bad-and-ugly-fiscal-cliff-package.

53 Paul Krugman, *Perspective on the Deal.* NEW YORK TIMES (Jan. 1, 2013), https://krugman.blogs.nytimes.com/2013/01/01/perspective-on-the-

VII. Conclusion

Based upon its stated objectives, the results to date are mixed but generally favorable in terms of realized benefits and potential economic upside.

A. Tax Relief

Successes include both the individual taxpayer and corporate changes. Middle-class relief was actually found in the increased standard deduction and enhanced childcare tax credits. Complaints about smaller 2018 tax refunds reflect more on flawed withholding economic policy and implementation than on actual tax liabilities. Clearly, the top 1% of taxpayers enjoyed substantial tax benefits, both directly and indirectly, through business tax incentives like immediate expensing of purchased assets. However, they also suffered under the SALT and mortgage interest expense limitations. The fact that many "Blue" states were hit hard by these provisions is perhaps more collateral damage and coincidence than political vindictiveness. Nonetheless, it is

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deal/ and Paul Krugman, *That Bad Ceiling Feeling,* NEW YORK TIMES (Jan. 2, 2013), https://krugman.blogs.nytimes.com/2013/01/02/that-bad-ceiling-feeling/.

possible President Trump believes that the punitive regional and political impacts constitute rough justice.

Corporate tax relief was realized through AMT repeal and the overall lowering of corporate tax rates. Capital investment incentives became prolific under the 2017 Act. Last-minute retention of the exemption for municipal bonds further facilitates financing of those investments.

B. Simplification

Simplification was clearly and substantially achieved on the individual side through a reduction in required record-keeping for itemized deductions. However, taxpayers can now game the system by bundling charitable contributions and alternating the years of taking the standard deduction followed by itemizing in the higher charitable contribution years. Further, the individual income tax return "postcard" promise for taxpayers was a ruse. Under renewed pressure from Trump and the Treasury Secretary, the IRS carved up the previous Form 1040 into a cover page followed by five new supplemental schedules. These changes did little for enhanced compliance. Lastly, instead of simplification, the

creation of the transition tax, GILTI, FDII and BEAT tax regimes added complexity in the corporate area.

C. Economic Growth and Enhanced International Compatibleness

This will need substantive work, as GILTI traps too many multinational companies. Those affected companies did not outsource offshore jobs for any other purpose than to serve a foreign market by maintaining a local manufacturing presence. Reform did effectively crack down on outbound inversion transactions by limiting domestic interest deductions, and lowering the corporate tax rate. President Obama had accomplished those similar ends through Executive Orders, though these have since been revoked by President Trump.

Over time, international tax changes can be a game-changer by combining lower tax rates with a nominally territorial foreign tax system. Thus, this remains a world-wide tax system. Foreign governments are now less motivated to assess U.S. multinationals solely to take advantage of the U.S. foreign tax credit system. The companies will now be

more motivated to fight such tax assessments, given that an offsetting foreign tax credit is no longer so readily available.

D. Repatriation

Here, the 2017 Act enjoyed its most success. Measured by the volume of actual repatriations, the funds can now be effectively redeployed by corporations and its investors. Whether that occurs with U.S.-based investment remains to be seen. However, the new law removes a significant tax barrier to repatriation of overseas earnings that were previously trapped.

VIII. Recommendations

A. Control Budget Deficits

Unless entitlement reform occurs (not likely), the deficits will loom large and become unsustainable. Supply side economics can only go so far to raise additional tax revenue. The likelihood is high that subsequent amendments will be required to roll back some of the tax incentives and raise overall rates.

B. GILTI Revisions

Experience will show that this new international minimum tax on multinationals is detrimental. Raising the threshold for permitted overseas returns substantially above the current ten percent would greatly help to lessen this anti-competitive GILTI tax.

C. FDII and BEAT

FDII will eventually be deemed an illegal export subsidy by the WTO. Based upon past experience with DISC, FSC and ETI, the U.S. will achieve little more than buying time. Eventually, resurrecting the Section 199 approach may prove to be more sustainable and defensible. BEAT has a good chance of surviving international scrutiny; especially given the BEPS initiative by the European Union. Administration of BEAT will be tricky and require substantial and detailed regulations to effectively achieve its intended oversight of abusive intercompany transactions.

D. Business Expensing of Asset Purchases.

This expensing will prove much too generous. It may not incentivize capital spending that much more than limited

expensing and bonus depreciation did before. There can be no question that a project's return on investment is greatly enhanced by these immediate write off provisions, but capex should not be overwhelmingly driven by the overall tax benefits. Such an incentive results in moral hazard whereby marginal investments can be undertaken and justified with any overall loss reduced by substantial tax benefits.

E. One-time Repatriation

It was prudent to have low rates; one for liquid assets and a second for all other deemed distribution of earnings and profits. However, permitting the actual tax payment to be spread over eight years was far too generous. Despite being retroactive, Congress should deplore the legality of retroactively accelerating the tax payment timing.

F. Net Operating Losses

The 2017 Act unwittingly traded off granting an unlimited carryforward period in exchange for a new 80% limitation on the use of net operating losses. Most economic theories support granting maximum tax benefits to companies while in the midst of their economic downturns. This new

approach is counterproductive and has not worked well in other foreign countries. It is strictly a revenue raiser.

In summary, the Internal Revenue Code of 1986 and ERTA, like their architect and chief advocate, Ronald Reagan, set the bar high for subsequent tax reform. The 2017 Act will not measure up to this lofty standard; among other problems, it lacks a Great Communicator to send an effective message to the American public. However, the 2017 legislation does effectively address the problems of the times. Subsequent amendments and adjustments will be needed to enhance its overall effectiveness. While it may not single-handedly make America great again, the 2017 Act will nonetheless play a substantial role.