

## ARTICLE

# Experts, Democracy, and the Historical Irony of U.S. Tax Policy: Thomas S. Adams and the Beginnings of the Value-Added Tax

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*In the early 1920s, legal and economic experts in the U.S. Treasury Department played a pivotal role in developing U.S. fiscal policy. Thomas S. Adams was one such expert and a key architect of the World War I fiscal state. After the war, Adams envisioned an innovative business tax that could have been the first broad-based, national consumption tax in the United States but was rejected by populist lawmakers. Later, Adams would be identified as one of the intellectual pioneers of the modern value-added tax (VAT)—a tax that has been adopted in nearly every developed country in the world except the United States and has also come to underwrite expansive, progressive social-welfare spending. How did a tax that began with an American expert fail to take hold in the United States? Democratic forces in the shape of organized political and economic interests both facilitated and frustrated the development of seemingly rational tax laws and spending policies crafted by fiscal experts. While Adams learned firsthand how these democratic forces influenced the relationship between expertise and state capacity, this missed opportunity to enact a comprehensive national consumption tax also influenced the peculiar development of the modern American fiscal and social-welfare states.*

In the spring of 1921, legal and economic experts in the U.S. Treasury Department faced a serious challenge. A newly elected Republican president and Congress had come to power with a perceived mandate to reduce World War I public debt, rationalize the tax regime, and restore order to a global economy still devastated by the dislocations of the Great War. The Treasury experts, many holdovers from Woodrow Wilson's Democratic administration, were asked to help incoming President Warren G. Harding return the country to "normalcy." Harding appointed Andrew W. Mellon, the Pittsburgh banker and businessman, to lead the Treasury Department. One of Mellon's primary duties was to dismantle the robust wartime tax regime.

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The expert administrators in Mellon's Treasury Department were thus called upon to do what they could to bring back the good old days. It was no easy task.<sup>1</sup>

Among the leading economic experts working in the Treasury Department at the time was Thomas S. Adams, a Yale University professor of political economy and former Wisconsin tax administrator, who had been one of the key architects of the World War I fiscal state. Adams was initially appointed in 1917 by President Wilson as a temporary advisor to the Treasury Department and the Bureau of Internal Revenue, the forerunner of today's Internal Revenue Service. But Adams soon became a powerful fixture in Treasury. He helped draft many of the wartime revenue acts that financed U.S. participation in the conflict. He was a frequent Treasury Department spokesperson before congressional committees. And he conducted rigorous studies of the economic effects of new fiscal laws and policies. Along with his legal counterparts, such as the former Wall Street lawyer Russell C. Leffingwell, Adams not only helped build the administrative infrastructure that underwrote the successful U.S. war effort, but he was also among the Wilson Treasury officials who remained in Washington after the armistice to ensure a smooth postwar transition.<sup>2</sup>

During and immediately after WWI, the United States was indebted to experts like Adams. The modern nation-state, as scholars have documented, has had a tremendous interest in economic and legal knowledge—both as producer and consumer—especially during periods of national crisis.<sup>3</sup> Treasury department experts such as Adams collected, analyzed, and disseminated economic data, and conducted studies that helped guide American lawmakers during and after the war. In the process, these government administrators helped create the political and legal institutions that processed and distilled the economic ideas brought before policy analysts and federal legislators. Little-known public officials like Adams were thus pivotal players in “one of the most fundamental relationships in twentieth-century politics: the co-evolution of federal institutions and the experts who eventually staffed them.”<sup>4</sup>

The rise of professional experts and the emergence of a national regulatory, administrative, fiscal state may well have gone hand-in-hand. But the relationship was hardly simple or linear. Beyond Weberian “ideal-types” about the development of Western bureaucratic rationality, the real-world historical symbiosis was often complicated, contested, and uneven. Trained economic specialists, such as Adams, facilitated American political and economic development.

<sup>1</sup>Adam Tooze, *The Deluge: The Great War, America, and the Remaking of the Global Order, 1916–1931* (New York, 2015); David J. Goldberg, *Discontented America: The United States in the 1920s* (Baltimore, 1999).

<sup>2</sup>A. E. Holcomb, “Thomas Sewall Adams (1873–1933),” *Bulletin of the National Tax Association* 18, no. 7 (Apr. 1933): 194–201; Lawrence L. Murray, “Bureaucracy and Bi-Partisanship in Taxation: The Mellon Plan Revisited,” *Business History Review* 52, no. 2 (Summer 1978): 200–25; Michael J. Graetz and Michael M. O’Hear, “The ‘Original Intent’ of U.S. International Taxation,” *Duke Law Journal* 46, no. 5 (Mar. 1997): 1021–109. On Adams’s influence on wartime tax laws, see also, Folders 1-5, box 1, Amendments to the Revenue Bill of 1918, Thomas Sewall Adams Papers (MS 31), Manuscripts and Archives, Sterling Memorial Library, Yale University, New Haven, CT [hereafter TSAP].

<sup>3</sup>Michael A. Bernstein, *Perilous Progress: Economists and Public Purpose in Twentieth-Century America* (Princeton, NJ, 2001); Mary O. Furner and Barry Supple, eds., *The State and Economic Knowledge: The American and British Experiences* (New York, 2002); Michael J. Lacey and Mary O. Furner, eds., *The State and Social Investigation in Britain and the United States* (New York, 1993). See also Daniel Ernst, “Law and the State, 1920–2000: Institutional Growth and Structural Change,” in *The Cambridge History of Law in America, vol. III: The Twentieth Century and After (1920–)*, eds. Michael Grossberg and Christopher Tomlins (New York, 2008), 1–33.

<sup>4</sup>Brian Balogh, *The Associational State: American Governance in the Twentieth Century* (Philadelphia, 2015), 91; W. Elliot Brownlee, “Economists and the Formation of the Modern Tax System in the United States: The World War I Crisis,” in *The State and Economic Knowledge: The American and British Experiences*, eds. Mary O. Furner and Barry Supple (New York, 2002), 401–34; William J. Barber, *From New Era to New Deal: Herbert Hoover, the Economists, and American Economic Policy, 1921–1933* (New York, 1988); Daniel P. Carpenter, *The Forging of Bureaucratic Autonomy: Reputations, Networks, and Policy Innovation in Executive Agencies, 1862–1928* (Princeton, NJ, 2001).

These experts in turn benefited from the growth of national political institutions. An increasingly rationalized legal and economic system valued experts like Adams, and bestowed upon them enormous resources, power, and prestige.<sup>5</sup>

Yet there were frequently other factors, such as democratic forces, which influenced the co-evolution of professional expertise and national state building. At certain times, the preferences of everyday Americans, voiced through organized political interests, challenged the aims and objectives of professional experts. Indeed, political thinkers and social critics have long observed the tension between American democracy and expert policymaking, particularly during the early twentieth century. While some have sided historically with Walter Lippmann, who urged elected officials to rely on social scientific experts to help run the government, others have been more skeptical of the alleged disinterested “objectivity” of scientific authority. John Dewey, in response to Lippmann, famously noted that experts had their own interests, and that democracy could devolve into an oligarchy of experts if “the masses do not have the chance to inform the experts as to their needs.”<sup>6</sup>

At other times, scientific experts were able to harness the public will and learn from popular opinion about how to advance the cause of democratic administration. Dewey himself noted how the Great War could clear the way for a new type of professional social science that advanced progressive reforms; he called for a “science of ideas in action which will trust ... to positive energy, to intellectual competency, to competency of inquiry, discussion, reflection and invention organized to take effect in action in directing affairs.”<sup>7</sup> Other progressives similarly balanced their preference for specialized public administration with an insistence that experts act as servants “guiding democratic control.”<sup>8</sup> Adams himself referred to this balancing process as an “essential part of financial democracy.”<sup>9</sup> In this sense, Adams shared Dewey’s pragmatic conviction that experts ought to adapt their ideas to democratic forces. Experts needed to do much more than simply dispense knowledge in the name of science; they needed to engage in a process of deliberation and discussion with the broader community. Organized political and economic interests could both facilitate and at times frustrate the development of seemingly rational tax laws and spending policies crafted by fiscal experts. Liberal democracy and bureaucratic administration were thus not always and everywhere antithetical forces.<sup>10</sup>

Nowhere perhaps was the complex relationship between democracy and expertise more evident than in the realm of early twentieth-century U.S. fiscal policy. For it was during debates over taxation and spending during this period that historically determined political and economic interests complicated the development of fiscal policy. The business community, organized labor, and agrarian interests were among the most influential groups shaping tax policy at the time. Adams was not oblivious of the importance of these democratic forces. In fact, he firmly believed that socioeconomic conflicts determined tax law and policy—for better or worse. “Modern taxation or tax-making, in its most characteristic aspect,” Adams

<sup>5</sup>Max Weber, *Economy and Society: An Outline of Interpretive Sociology*, ed. Guenther Roth and Claus Wittich, trans. Ephraim Fischer et al. (New York, 1968).

<sup>6</sup>Walter Lippmann, *Public Opinion* (New York, 1922); John Dewey, *The Public and Its Problems: An Essay in Political Inquiry* (New York, 1927), 208. See also Leon Fink, *Progressive Intellectuals and the Dilemmas of Democratic Commitment* (Cambridge, MA, 1999).

<sup>7</sup>John Dewey, “A New Social Science,” *The New Republic*, Apr. 6, 1918, 294.

<sup>8</sup>“Training for Public Service,” *The New Republic*, July 8, 1916, 216.

<sup>9</sup>Thomas S. Adams, “Should the Excess Profits Tax Be Repealed?” *Quarterly Journal of Economics* 35, no. 3 (May 1921): 363–93, here 370.

<sup>10</sup>James T. Kloppenberg, *Uncertain Victory: Social Democracy and Progressivism in European and American Thought, 1870–1920* (New York, 1988), 381–94. For more on the compatibility of expertise and democracy in progressive thought, see K. Sabeel Rahman, *Democracy Against Domination* (New York, 2017), 101–3; William J. Novak, “The Progressive Idea of Democratic Administration,” *University of Pennsylvania Law Review* 167, no. 7 (Jun. 2019): 1823–48; and William J. Novak, *New Democracy: The Creation of the Modern American State* (Cambridge, MA, 2022).

noted toward the end of his career, “is a group contest in which powerful interests vigorously endeavor to rid themselves of present or proposed tax burdens. It is, first of all, a hard game in which he who trusts wholly to economics, reason, and justice, will in the end retire beaten and disillusioned. Class politics is the essence of taxation.”<sup>11</sup>

The democratic forces of class politics were particularly salient during the 1920s, when U.S. fiscal policy faced dramatic challenges as part of an attempted “return to normalcy.” The “roaring twenties” was a decade of rising economic inequality matched only by the late nineteenth-century’s Gilded Age. It was the decade of the Great Bull Market, “when Fordism put American capitalism over the top.”<sup>12</sup> It was also a time when greater calls for public assistance and increased federal social-welfare spending, including in the form of a WWI Veterans’ Bonus, first began to germinate. For an earlier generation of historians, the decade’s changes were seen as a radical rupture from the past, a period when a surging economy, fueled by a new system of mass production and consumption, led to a return of laissez-faire law and political economy, marked by pro-business government policies and generous tax cuts for the wealthy.<sup>13</sup>

In contrast to the earlier depiction of the 1920s as a reactionary rollback of prewar progressive commitments, recent revisionist accounts have uncovered and stressed the institutional connections and continuity that existed from the progressives to the Wilson administration’s robust WWI tax regime to the so-called “conservative” 1920s and beyond.<sup>14</sup> Indeed, there is now a growing scholarly literature on the historical importance of the 1920s as a critical juncture in the path-dependent history of U.S. tax law and policy and its implications for American state building. More specifically, scholars have identified several factors to explain why continuity, rather than rupture, characterizes this highly contested era. Some have noted how heavy WWI public debts created a structural floor that prevented the complete retrenchment of the wartime fiscal state. Others have argued that the tremendous administrative burden of levying novel and complex wartime taxes, and also bipartisan faith in existing bureaucratic officials, led to stability in fiscal policy, despite the changing political winds. Still others have pointed to the mounting political and social pressures for a postwar veterans’ bonus to show that lawmakers were constrained in their ability to slash taxes. The recent revisionist scholarship has, in short, helped us re-evaluate 1920s fiscal policymaking.<sup>15</sup>

Although the new literature challenges long-held historical assumptions about the meaning of post-WWI fiscal policymaking, we still know little about the other possible alternatives that

<sup>11</sup>Thomas Sewall Adams, “Ideals and Idealism in Taxation,” *American Economic Review* 18, no. 1 (Mar. 1928): 1–8, here 1.

<sup>12</sup>Thomas Piketty, *Capital in the Twenty-First Century*, trans. Arthur Goldhammer (Cambridge, MA, 2014); Jonathan Levy, *Ages of American Capitalism: A History of the United States* (New York, 2021), 329.

<sup>13</sup>For earlier conventional accounts of the 1920s as a period of retrenchment, see Arthur M. Schlesinger, *The Age of Roosevelt: The Crisis of the Old Order, 1919–1933* (Boston, 1957); William E. Leuchtenburg, *The Perils of Prosperity, 1914–1932* (Chicago, 1958); and Gene Smiley and Richard H. Keehn, “Federal Personal Income Tax Policy in the 1920s” *The Journal of Economic History* 55, no. 2 (June 1995): 285–303.

<sup>14</sup>W. Elliot Brownlee, *Federal Taxation in America: A History*, 3rd ed. (New York, 2016). For more on early-twentieth-century continuities in U.S. history, see the essays in Brent Cebul, Lily Geismer, and Mason B. Williams, eds., *Shaped by the State: Toward a New Political History of the Twentieth Century* (Chicago, 2019).

<sup>15</sup>Examples of the accounts stressing continuity include Benjamin G. Rader, “Federal Taxation in the 1920s: A Re-examination,” *Historian* 33, no. 3 (May 1971): 415–35; Murray, “Bureaucracy and Bi-artisanship in Taxation”; Anne L. Alstott and Ben Novick, “War, Taxes, and Income Redistribution in the Twenties: The 1924 Veterans’ Bonus and the Defeat of the Mellon Plan,” *Tax Law Review* 59, no. 4 (Summer 2006): 373–438; M. Susan Murnane, “Selling Scientific Taxation: The Treasury Department’s Campaign for Tax Reform in the 1920s,” *Law & Social Inquiry* 29, no. 4 (Autumn 2004): 819–56; Kimberly J. Morgan and Monica Prasad, “The Origins of Tax Systems: A French-American Comparison,” *American Journal of Sociology* 114, no. 5 (Mar. 2009): 1350–94; George K. Yin, “James Couzens, Andrew Mellon, the Greatest Tax Suit in the History of the World, and the Creation of the Joint Committee on Taxation and Its Staff,” *Tax Law Review* 66, no. 4 (Summer 2013): 787–879; Ajay K. Mehrotra, *Making the Modern American Fiscal State: Law, Politics, and the Rise of Progressive Taxation, 1877–1929* (New York, 2013), ch. 6.

existed during this pivotal period, and even less about those available routes that were not pursued. One of the alternative fiscal options that American lawmakers considered but foreclosed was the adoption of a broad-based national consumption tax. After the war, Adams proposed a highly innovative levy that could have been the first comprehensive U.S. national consumption tax—a tax on what individuals and businesses consume or buy rather than earn. Simultaneously, several national lawmakers also recommended a variety of consumption taxes framed as individual “sales taxes,” though for reasons dramatically different from Adams. Any of these national consumption tax proposals might have evolved eventually into a modern VAT, but all of them, including Adams’s pioneering tax, were rejected by Congress in 1921.<sup>16</sup>

Meanwhile, other countries in post-WWI Europe, notably France and Germany, began to experiment with and refine their use of rudimentary federal consumption taxes. Although none of the 1921 U.S. sales tax proposals was adopted by Congress, Adams’s creative recommendation would eventually become the conceptual foundation for a revolutionary new tax regime—one that by the end of the twentieth century would sweep across much of the globe. Indeed, decades after the Great War, scholars worldwide would identify Adams as one of the intellectual fountainheads of the modern “value-added tax” (VAT)—a business-based consumption tax that has been adopted in nearly every developed country in the world, except the United States.<sup>17</sup>

This article explores the historical irony of how a tax that began with an American economist has failed to take hold in the United States, and what that failure might tell us about the uneasy relationship between administrative expertise and participatory democracy. It examines the intellectual beginnings of the VAT and the early American social and political resistance to broad-based national consumption taxes. Where did the idea of imposing taxes on businesses for the value they added to the production and distribution of goods and services come from? And why was Adams’s novel 1921 proto-VAT proposal rejected in the United States? This article seeks to address these important historical questions in order to understand the complex relationship between democratic forces and the co-evolution of expertise and American state building. Several secondary sources have identified Adams and the German businessman Wilhelm Von Siemens as the two individuals who independently devised the concept of a modern VAT.<sup>18</sup> But scholars have not explored in depth the meaning and development of their ideas. What these two individuals shared was a practical desire to reform the then-existing taxation of businesses, and a political realism about the futility of their ideas. Yet today we know little about the genealogy of their ideas, and even less about the origins of Adams’s specific U.S. proposal and why it was rejected.

Adams’s particular vision for a proto-VAT came from his earlier experiences as a Wisconsin state tax expert. He learned then that creating an effective administrative framework—one that

<sup>16</sup>Thomas S. Adams, “Fundamental Problems of Federal Income Taxation,” *Quarterly Journal of Economics* 35, no. 4 (Aug. 1921): 527–56; Joseph J. Thorndike, “Early Proposals for an American VAT,” *Tax Notes*, July 6, 2009, 75–82; Steven A. Bank, “The Progressive Consumption Tax Revisited,” *Michigan Law Review* 101, no. 6 (May 2003): 2238–60; Steve C. Wells and Tonya K. Fleisher, “Lessons for Policy Makers from the History of Consumption Taxes,” *Accounting Historians Journal* 26, no. 1 (June 1999): 103–26.

<sup>17</sup>Kathryn James, *The Rise of the Value-Added Tax* (Cambridge, UK, 2015); Clara K. Sullivan, *The Tax on Value Added* (New York, 1965). Today a variety of VATs exists in 170 countries and they account for roughly 20 percent of worldwide tax revenue. Organization of Economic Cooperation and Development, *Consumption Tax Trends 2020: VAT/GST and Excise Rates, Trends and Policy Issues* (Paris, 2020); Alan Schenk and Oliver Oldham, *Value Added Tax: A Comparative Approach*, rev. ed. (New York, 2007); Allan A. Tait, *Value Added Tax: International Practice and Problems* (Washington, DC, 1988); Sijbren Cnossen, “Global Trends and Issues in Value Added Taxation,” *International Tax and Public Finance* 5, no. 3 (Jul. 1998): 399–428. For an example of how the VAT operates, see Leonard E. Burman and Joel Slemrod, *Taxes in America: What Everyone Needs to Know* (New York, 2020), 98–100.

<sup>18</sup>James, *The Rise of the Value-Added Tax*, 1; Sullivan, *The Tax on Value Added*, 12; John F. Due, *Sales Taxation* (Urbana, IL, 1957), 138.

prevented the potential for double taxation—was critical to the success of any new tax. Yet Adams’s scholarly and practical insights were not enough to ensure the success of what would have been the U.S.’s first broad-based, national consumption tax. Organized political interests, led mainly by populist lawmakers, rejected the national consumption tax proposals because of their potential adverse economic effects on working-class Americans. As a result, a creative new tax envisioned by an American economist was ultimately rejected by the American people.

This seemingly narrow study about the historical irony of U.S. tax law and policy may inform wider historical investigations about comparative law, society, and political economy, as well as present-day concerns about economic inequality and the role of fiscal policy in mitigating growing concentrations of wealth and opportunity.<sup>19</sup> As scholars of comparative law and political economy have shown, there is a high degree of correlation across space and time between regressive national consumption taxes like the VAT and robust, progressive social-welfare spending. Throughout the twentieth century, nation-states that have relied on comprehensive national consumption taxes for revenue have countered the regressivity of such levies with highly progressive social-welfare spending.<sup>20</sup> Understanding why there is no value-added tax in the United States may shed light on broader questions about U.S. political preferences, social values, and the peculiar development of the modern American fiscal and social-welfare states.<sup>21</sup> Understanding how and why Americans have supported certain taxes while rejecting others may tell us something about how we choose to tax and spend. Why no VAT in the U.S. may thus be a variant of the classic Werner Sombart query: why no socialism in the United States? Or the more pragmatic contemporary question: why so little direct social-welfare spending in the United States?<sup>22</sup>

### The Education of Thomas S. Adams—“A Scholar in Politics”

Thomas Adams was not a typical early-twentieth-century academic expert. Although he shared with many of his mentors and progressive colleagues a religiously infused sense of social reform, Adams seemed to be most comfortable traversing between the academic world of ideas and the rough-and-tumble arena of politics and policy making—something he did regularly throughout his career. Tall, thin-lipped, with prominent ears and piercing eyes, Adams was an ambitious and intense individual who made an impression on nearly everyone he met. Educated at the Johns Hopkins University, Adams spent the early part of his career

<sup>19</sup>Interdisciplinary legal scholars have recently revived an interest in exploring how law and democratic statecraft can reconnect “with the longstanding, broad, and deep literatures of political economy.” See Angela Harris and James J. Verelias III, “Introduction: Law and Political Economy in a Time of Accelerating Crises,” *Journal of Law and Political Economy* 1, no. 1 (Fall 2020): 1–27; Jedediah Britton-Purdy et al., “Building a Law-and-Political-Economy Framework: Beyond the Twentieth-Century Synthesis,” *Yale Law Journal* 129, no. 6 (Apr. 2020): 1784–835; and Jeremy Bearer-Friend et al. “Taxation and Law and Political Economy,” *Ohio State Law Journal* 83, no. 3 (2022): 471–528.

<sup>20</sup>Junko Kato, *Regressive Taxation and the Welfare State: Path Dependence and Policy Diffusion* (Cambridge, UK, 2003); Monica Prasad, *The Land of Too Much: American Abundance and the Paradox of Poverty* (Cambridge, MA, 2012).

<sup>21</sup>By exploring the peculiar evolution of the American fiscal state, this article joins the growing interdisciplinary literature questioning the notion that the United States is a weak state. See William J. Novak, “The Myth of the ‘Weak’ American State,” *American Historical Review* 113, no. 3 (Jun. 2008): 752–72; and Christopher Howard, *The Hidden Welfare State: Tax Expenditures and Social Policy in the United States* (Princeton, NJ, 1997).

<sup>22</sup>Werner Sombart, *Why Is There No Socialism in the United States?*, ed. C. T. Husbands, trans. Patricia M. Hocking and C. T. Husbands (New York, 1976); Seymour Martin Lipset and Gary Marks, *It Didn’t Happen Here: Why Socialism Failed in the United States* (New York, 2000); Alberto F. Alesina, Edward Glaeser, and Bruce Sacerdote, “Why Doesn’t the United States Have a European-Style Welfare State?” *Brookings Papers on Economic Activity*, no. 2 (Fall 2001): 187–277.

immersed in gathering empirical data and assisting lawmakers. He began teaching in 1901 at the University of Wisconsin–Madison, where he was imbued with the “Wisconsin Idea,” the principle that a research university existed to serve the broader public.<sup>23</sup>

During his years in Madison, Adams demonstrated his commitment to the Wisconsin idea and learned firsthand about the potential tension between democracy and expertise by working closely with the state’s tax commission. He moved to Yale in 1916, and in the following year President Wilson called him into service as a U.S. Treasury Department advisor where he remained until well after the war. Adams returned to Yale after his government service, but he remained a frequent special counselor to the Treasury Department, as well as a sought-after private consultant. By the end of his career, Adams came to be known by his contemporaries as a “shining example” of a “scholar in politics,” and as “a liaison officer between the world of thought and the world of action.”<sup>24</sup>

Thomas Sewall Adams was born in 1873, and raised in Baltimore, Maryland, the third son of a native, Congregationalist family with deep roots in the area. As a student at the prestigious Baltimore City College, one of the oldest public high schools in the nation, “Tommy” Adams distinguished himself as a serious student, and gained admission to the recently created Johns Hopkins University, where he received his undergraduate and graduate training. Adams’s early ambitions, as described on his college application, included taking “statistical political courses” as a “good foundation for [the] profession of law or journalism.”<sup>25</sup>

Adams attended Hopkins at a formative moment in the university’s history. By the time he enrolled in 1893, Hopkins had established itself as an intellectual leader of higher education, especially in the field of political economy. The university’s first president, Daniel Coit Gilman, hired several prominent academics including historian Henry Baxter Adams (no relation to Thomas) and political economist Richard T. Ely. Together, these European-trained, professional scholars imported the German “seminary” style of education to Hopkins’s Department of Historical and Political Science.<sup>26</sup>

Ely and his cohort of young, maverick, American academics were unafraid to challenge the status quo. They were eager to pave a new path for the emerging professional social sciences. While at Hopkins, Ely hurled one of the first salvos against the traditional “old school” of laissez-faire political economy, calling for a “new school” that embraced empirical and inductive methods and sought to inform policymaking. Ely and his “new school” colleagues envisioned a burgeoning and varied economics discipline and profession that would be responsive to popular calls for state action and progressive reform—a profession that could potentially use scientific means to advance egalitarian ends and thus resolve tensions between expertise and democracy. Ely’s bold and ambitious claims about the methodological and normative aims of political economy set off an intramural war within the nascent economics discipline,

<sup>23</sup>For more on Adams’s influence on policy making, see Brownlee, “Economists and the Formation of the Modern Tax System in the United States”; Brownlee, “Social Investigation and Political Learning in the Financing of World War I,” in *The State and Social Investigation in Britain and the United States*, eds. Michael J. Lacey and Mary O. Furner (New York, 1993), 323–64; Graetz and O’Hear, “The ‘Original Intent’ of U.S. International Taxation”; and Thomas Earl Geu, “Professor T. S. Adams (1873–1933) on Federal Taxation: Déjà Vu All Over Again,” *Akron Tax Journal* 10 (1993): 29–45.

<sup>24</sup>Holcomb, “Thomas Sewall Adams (1873–1933),” 194, 196. For more on Adams’s private consulting practice, see the materials contained in Folder 11, box 1–folder 3, box 5 American Gas Association Survey and Folder 4, Box 5–folder 8, box 7, Cement Survey, TSAP.

<sup>25</sup>Roy G. Elliott, “Dean of Tax Experts,” *Credit Monthly*, Mar. 1921, 21; Thomas Sewall Adams, Application for Admission, Johns Hopkins University, Oct. 3, 1893, box 1, subgroup 1, series 2, Records of the Office of the Registrar (RG 13-010), Special Collections, Sheridan Library, Johns Hopkins University, Baltimore, MD [hereafter JHUSC].

<sup>26</sup>William J. Barber, “Political Economy in the Flagship of Postgraduate Studies: The Johns Hopkins University,” in *Economists and Higher Learning in the Nineteenth Century*, ed. William J. Barber (New Brunswick, NJ, 1993), 203–24; Daniel T. Rodgers, *Atlantic Crossings: Social Politics in a Progressive Age* (Cambridge, MA, 1998).

and likely precipitated his departure from Hopkins. But Ely's call to arms also attracted many young graduate students to the university, including a young Woodrow Wilson. Indeed, during Gilman's tenure, Hopkins produced far more PhDs than any other university, and it swiftly established itself as a leading incubator of reform-minded academics.<sup>27</sup>

After his undergraduate training, Adams remained at Hopkins to pursue a doctorate in political economy. Although Ely had left Hopkins for the University of Wisconsin by the time Adams began his education, the university remained a magnet of activity for established and aspiring political economists, including many who were active in policy making. At the same time, Gilman appointed, as visiting lecturers, some of the country's leading economic and legal thinkers including Columbia University economist John Bates Clark, Michigan Supreme Court Justice Thomas M. Cooley, and Hopkins alumnus Henry Carter Adams (PhD 1878, no relation to Thomas). Thus, throughout his formal education T. S. Adams was part of a vibrant intellectual community that attempted to meld theory and practice and reconcile any possible tension between expertise and democracy.<sup>28</sup>

Unlike many of his mentors, Adams did not travel to Germany after his formal education. Instead, he opted for practical experience. Adams began his professional career by immersing himself in U.S. Census data. Working as a statistician at the Census Bureau, Adams confronted the challenges of collecting, standardizing, and analyzing a wealth of information about the U.S. population, mortality rates, and changes in the agricultural and manufacturing sectors. Meanwhile, Adams began his research in labor relations and taxation. In 1900, he translated the French economist Emile Levasseur's *American Workman* and published a report on Maryland taxation.<sup>29</sup>

The Maryland tax study was part of a larger research project contrasting the economic conditions and fiscal capacity of various U.S. states. The project was led by Jacob H. Hollander, a junior Hopkins professor who became an early mentor to Adams sparking his interest in "fiscal science." Adams learned two important lessons from this initial tax study. First, the detailed analysis of differing social, political, and economic conditions taught him that systematic empirical studies were a prerequisite for scientific understanding and practical reform. Second, he learned that there was no universal blueprint for fiscal reform—that each community had particular differences that needed to be respected. This early research interest in state-level taxation was followed by a year of practical experience when Hollander hired Adams as his assistant in creating Puerto Rico's first tax system under U.S. sovereignty. These early practical experiences prepared Adams to identify potential strains between economic expertise and democratic pressures.<sup>30</sup>

In 1901, Adams returned to the academy when he began teaching economics and statistics at the University of Wisconsin. Hired by Richard Ely as one of Ely's first external appointees, Adams was attracted to the connections between the university and the state's progressive politics. This was, of course, the historical period when the "Wisconsin Idea" was taking hold. The notion of producing research to serve the public was attractive to Adams, John R. Commons, and many

<sup>27</sup>Dorothy Ross, *The Origins of American Social Science* (New York, 1991), 109–17; Mary Furner, *Advocacy and Objectivity: A Crisis in the Professionalization of American Social Science, 1865–1905* (Lexington, KY, 1975), ch. 3. Hopkins produced nearly 600 PhDs during Gilman's 25 years as president, twice as many as its closest rival in graduate education, Harvard. Barber, "Political Economy in the Flagship of Postgraduate Studies," 224.

<sup>28</sup>A portion of Adams's 1899 doctorate was published as T. S. Adams, "Index Numbers and the Standard Value," *Journal of Political Economy* 10, no. 1 (Dec. 1901): 1–31.

<sup>29</sup>Emile Levasseur, *The American Workman*, ed. Theodore Marburg, trans. Thomas S. Adams (Baltimore, 1900); Thomas Sewall Adams, "Taxation in Maryland," in *Studies in State Taxation with Particular Reference to the Southern States*, ed. J. H. Hollander, Johns Hopkins University Studies in Historical and Political Science, ed. Herbert Baxter Adams, vol. 18 (Baltimore, 1900), 13–75.

<sup>30</sup>Holcomb, "Thomas Sewall Adams (1873–1933)"; Thomas Sewall Adams, "The Financial Problems of Porto Rico," *The Annals of the American Academy of Political and Social Science* 17, no. 3 (May 1901): 444–53; Jacob H. Hollander to M. D. Connor, Feb. 1, 1939; Hollander to Alfred E. Holcomb, June 21, 1933, box 15, subseries 5, series 10, Records of the Department of Political Economy/Economics (RG04-140), JHUSC.



others who arrived in Madison in the early 1900s. This was also a time when the broader landscape of American politics was shifting from the mass-mobilization of parties to the rise of interest group pluralism. Although Adams may not have realized it at the time, his first teaching position at Wisconsin gave him an exceptional opportunity to pursue the path of a scholar in politics, and to learn firsthand how voluntary associations influenced expert policy making.<sup>31</sup>

Adams's early academic career also unfolded at a time when the economics profession was still grappling with its identity. While the neoclassical, marginal utility analysis advanced in the United States by John Bates Clark became the dominant disciplinary paradigm of the twentieth century, the ascendancy of a competing school of institutionalism—embodied in the works of Thorstein Veblen, Commons, Wesley Mitchell, and others—would pose an early and formidable challenge to American marginalism. Responding to the growing economic inequality of the Gilded Age, the early American institutional economists stressed how changing cultural, social, and legal institutions shaped the development of modern industrial capitalism. By contrast, marginalists sought to hold onto the universalist precepts of neoclassical price theory, contending that marginal utility was the key in understanding value.<sup>32</sup>

Adams did not fit neatly into either of these competing intellectual camps. As a public finance specialist who traversed between the academy and policy making, Adams was able to tread a middle ground between the orthodox theories of neoclassicism and the heterodoxy of institutionalism. As an Ely protégé, Adams leaned toward the institutionalist camp, but that did not mean that he rejected all aspects of marginalism. Indeed, Adams's dual role as a scholar and policymaker provided him with a unique type of intellectual autonomy: his allegiance was to developing sound and coherent theories that could be tested by experience and translated into practical laws and policies. Thus, he was not beholden to either of the two camps that were competing for control of the economics discipline. In this sense, Adams may have been the last of a dying breed of political economists before the growing intellectual specialization and quantification of the discipline left little room for such individuals in the academy.<sup>33</sup>

In the early 1900s, the Wisconsin economics department itself was a hotbed of early policy engagement. It was an institution that sought to use economic expertise to address democratic calls for progressive reform; it also fell victim to some of the less egalitarian motives of Progressive Era economics including eugenics and real estate red lining.<sup>34</sup> During his time in Madison, Adams further developed his scholarly and practical interests in public finance and in industrial relations by publishing several articles on taxation and labor unions.<sup>35</sup> With Ely's assistance, Adams also co-authored, with Helen L. Sumner, a 1905 undergraduate textbook

<sup>31</sup>Fred R. Fairchild, "Thomas Sewall Adams," *Dictionary of American Biography Volume XXI, Supplement One*, ed. Harris E. Starr (New York, 1944), 9–10. John Commons later noted that Adams "first put our teaching of labor movements, taxation and statistics on a sound and thrilling basis to which our economics department always looks back for its standards." Alfred E. Holcomb, ed., *In Appreciation of Thomas Sewall Adams* (Madison, WI, 1933), 11. J. David Hoeweler, *John Bascom and the Origins of the Wisconsin Idea* (Madison, WI, 2017); Elisabeth S. Clemens, *The People's Lobby: Organizational Innovation and the Rise of Interest Group Politics in the United States, 1890–1925* (Chicago, 1997).

<sup>32</sup>Yuval P. Yonay, *The Struggle over the Soul of Economics: Institutional and Neoclassical Economists in America between the Wars* (Princeton, NJ, 1998); Ross, *Origins of American Social Science*; Furner, *Advocacy and Objectivity*; Mary S. Morgan and Malcolm Rutherford, eds., *From Interwar Pluralism to Postwar Neoclassicism* (Durham, NC, 1998); Malcolm Rutherford, *The Institutional Movement in American Economics, 1918–1947: Science and Social Control* (Cambridge, UK, 2011).

<sup>33</sup>Ross, *Origins of American Social Science*; Furner, *Advocacy and Objectivity*; Rutherford, *The Institutional Movement in American Economics*.

<sup>34</sup>Thomas C. Leonard, *Illiberal Reformers: Race, Eugenics, and American Economics in the Progressive Era* (Princeton, NJ, 2016), 109–11; LaDale C. Winling and Todd M. Michney, "The Roots of Redlining: Academic, Governmental, and Professional Networks in the Making of the New Deal Lending Regime," *Journal of American History* 108, no. 1 (Jun. 2021): 42–69.

<sup>35</sup>Richard T. Ely et al., *Outlines of Economics*, rev. ed. (New York, 1910); Rutherford, *Institutionalist Movement in American Economics*, ch. 7.

on *Labor Problems*.<sup>36</sup> While he was in Madison, Adams also served for many years on the Wisconsin Tax Commission, where he helped lead the enactment of the first effective state-level, progressive income tax in 1911, and where he witnessed directly how Wisconsin's democratic impulses were channeled through commission governance.<sup>37</sup>

### Building Administrative Capacity from Madison to Washington

Adams's service on the Wisconsin Tax Commission was a formative experience. There he worked closely with other professional experts, organized political interests, and concerned citizens in improving the ailing state and local tax system. Collaborating with lawyers such as Nils P. Haugen, a progressive legislator, Adams came to understand the importance of administrative capacity for a well-functioning system of public finance. His many years with the commission taught him that amending state constitutions and reforming laws were only the first steps in improving the formal tax system; lasting reform required a change in the administrative infrastructure—to enforce new laws and constitutional provisions—and perhaps even more importantly a change in legal culture or legal consciousness among citizens and taxpayers.<sup>38</sup>

While other tax experts were skeptical that Wisconsin or any state could effectively collect a personal income tax, Adams predicted that the experiment would succeed not only in raising badly needed revenue but in addressing the growing concentration of wealth. He was confident that Wisconsin lawmakers had established the key administrative innovations, including creating a crude form of “information withholding,” which required banks and other financial intermediaries to report the payment of interest, dividends, and other forms of income. This new method of information sharing and the filing of self-reported income that accompanied it, Adams contended, would soon help educate Wisconsin's citizens about their fiscal obligations to the state. Law and administration would be used to forge a sense of fiscal citizenship, whereby everyday citizens, as taxpayers, would become more engaged with state and local statecraft.<sup>39</sup>

While in Wisconsin, Adams also learned about the importance of using technical aspects of tax law to ameliorate thorny practical problems. These lessons, particularly the use of “tax credits,” would inform his views on his proto-VAT a decade later and even his subsequent vision for an effective international tax regime. One of the key obstacles to the 1911 Wisconsin income tax was that it could potentially double-tax personal property such as business inventory, household items, or even agricultural livestock. Indeed, small businesses and farmers initially opposed the Wisconsin income tax because they believed that they would be paying a personal property tax on their inventory and livestock, and a second tax on the income generated by such property. To address the potential problem of double taxation, Adams urged Wisconsin lawmakers to consider a tax “credit” or “offset” that allowed those who paid a personal property tax to reduce their income tax liability dollar-for-dollar by the amount of the personal property tax paid. Thus, as Adams explained, a taxpayer “with an income tax of \$100 and a personal property tax of \$70, pays his personal property tax and only \$30 as income tax.”<sup>40</sup>

<sup>36</sup>Thomas Sewall Adams and Helen L. Sumner, *Labor Problems: A Text Book* (New York, 1905). Sumner was one of the few women graduate students in economics at the time, and she quickly became a leading expert on child labor laws. Department of Labor, Children's Bureau, *Administration of Child Labor Laws*, by Helen L. Sumner et al. (Washington, DC, 1915).

<sup>37</sup>T. S. Adams, “Mortgage Taxation in Wisconsin,” *The Quarterly Journal of Economics* 22, no. 1 (Nov. 1907): 1–27; W. Elliot Brownlee, *Progressivism and Economic Growth: The Wisconsin Income Tax, 1911–1929* (Madison, WI, 1974).

<sup>38</sup>T. S. Adams, “The Significance of the Wisconsin Income Tax,” *Political Science Quarterly* 28, no. 4 (Dec. 1913): 569–85; Ajay K. Mehrotra, “Forging Fiscal Reform: Constitutional Change, Public Policy, and the Creation of Administrative Capacity in Wisconsin, 1880–1920,” *Journal of Policy History* 20, no. 1 (2008): 94–112.

<sup>39</sup>Adams, “Significance of the Wisconsin Income Tax”; Brownlee, *Progressivism and Economic Growth*.

<sup>40</sup>Adams, “Significance of the Wisconsin Income Tax,” 570.

Initially, Adams was wary, at least conceptually, of a personal property tax “credit.” In a series of letters with a state lawmaker, Adams explained that he feared such a “credit” would undermine the revenue raising capacity of an income tax. Instead, Adams had hoped that the income tax would completely replace the personal property tax, eliminating the potential double tax and thus the need for such a tax credit. Adams’s more radical proposal of completely eliminating the personal property tax faced strong opposition from lawmakers who were loath to abolish an important source of public funds. Thus, when his ideal position proved untenable, Adams turned to the use of a tax credit as a viable and practical compromise. Eventually, Wisconsin lawmakers adopted the personal property tax credit as an equitable way to implement a novel and untried state-level income tax while maintaining the personal property tax. Adams seemed to learn the critical lesson that the ideas and ideals of bureaucratic experts often had to bend to meet the realities of policymaking. Adams’s willingness to mold his ideal position to fit practical conditions would also shape his view of a comprehensive national consumption tax a decade later.<sup>41</sup>

Reflecting back on the new Wisconsin income tax, Adams realized that his initial fears about the personal property tax credit were unfounded. The effective use of tax “credits” would, in time, become an essential part of Adams’s future tax reform proposals. His 1920 proto-VAT would make use of such “credits” to allow businesses to calculate the value they added to the production of manufactured goods, and hence the amount they owed under a VAT. Similarly, Adams’s future international tax reform proposals also relied on “foreign tax credits” to ensure that U.S. multinational corporations did not pay double tax on income earned abroad. The Wisconsin income tax soon became a huge success mainly because of the law’s administrative innovations. The use of “information withholding” and property tax “credits” demonstrated that state governments could create the infrastructure to levy a workable income tax—one that attacked growing inequality in a fair and effective manner.<sup>42</sup>

Adams shared his confidence in the Wisconsin income tax experiment and his faith in administration with other leading tax experts. Writing to Edwin R. A. Seligman, the Columbia University economist who was then the dean of American tax experts, Adams professed his views on tax reform and criticized others, such as Seligman, who focused on the formal substance of tax laws while neglecting the administrative infrastructure.<sup>43</sup> Seligman did not take kindly to this rebuke from a junior colleague, and he insisted that the 1911 Wisconsin experiment was doomed to failure. Just three years later, however, income tax revenues were flowing into the Wisconsin Treasury and economic experts like Seligman conceded that Adams had been correct: Wisconsin had created the administrative framework to collect the first effective state-level, graduated income tax. The ultimate success of the Wisconsin income tax was, thus, one example where academic specialists such as Adams were able to harness democratic forces to advance the co-evolution of professional expertise and state building.

Two years after Wisconsin adopted its income tax, the federal government followed suit. Following the ratification of the Sixteenth Amendment, the 1913 national income tax was a modest levy aimed principally at the country’s wealthiest citizens. It was one way to address the growing economic inequality of the times. Adams, once again, was among the economic experts

<sup>41</sup>T. S. Adams to Nils P. Haugen, Apr. 1, 1910; Adams to Haugen, Mar. 30, 1911; Adams to Haugen, Dec. 24, 1910; Adams to Haugen, Apr. 27, 1911, all in Box 56, Nils Pederson Haugen Papers (M89-095), Division of Library Archives and Museum Collections, Wisconsin Historical Society, Madison, WI; Nils P. Haugen, *Pioneer and Political Reminiscences* (Evansville, WI, 1930), 159–60.

<sup>42</sup>Adams, “Fundamental Problems of Federal Income Taxation”; Graetz and O’Hear, “The ‘Original Intent’ of U.S. International Taxation.”

<sup>43</sup>T. S. Adams to Edwin R. A. Seligman, Aug. 9, 1911, folder 11, box 14, Miscellaneous Papers on Taxation, 1900–1933, TSAP; Edwin R. A. Seligman, *The Income Tax: A Study of the History, Theory, and Practice of Income Taxation at Home and Abroad*, 2nd ed. (New York, 1914), 421–8.

backing the new income tax law. His experience with the Wisconsin income tax proved useful. He used evidence from Wisconsin to counter those economists who opposed the national income tax and to make the case for direct and progressive taxes as tools to combat the growing concentrations of wealth. “Carefully formulated and efficiently administered income and inheritance taxes do equalize the distribution of wealth and do not, in an appreciable degree, set into motion any subtle, subterranean, or remote economic forces of an objectionable kind, such as the professional economist so dearly and so properly loves to analyze and evaluate,” he announced in a 1915 presentation before the American Economic Association (AEA). Even at this relatively early career stage, Adams was not afraid to challenge the discipline’s conventional wisdom.<sup>44</sup>

At the same time, Adams remained a steadfast political realist. His pragmatist intuition and his experience with the Wisconsin Tax Commission had taught him to respect the popular will that shaped fiscal policymaking. He learned that there were administrative limits to the power of taxation. Graduated taxes were, for Adams, neither a cure-all nor something to be avoided at all costs. Rather, they were tools to be fashioned for a variety of fiscal and social democratic ends.<sup>45</sup>

Five years after he helped enact the Wisconsin income tax, Adams moved to Yale University, and before he settled into New Haven, Woodrow Wilson tapped him to be an expert advisor to the Treasury Department in 1917. Adams quickly became an essential figure in the department. He led a Treasury study of the incidence, or ultimate liability, of the controversial 1918 “excess profits” tax—a levy aimed at large corporations that were allegedly exploiting wartime economic conditions. Initially, Adams had been ambivalent about the excess profits tax. Before U.S. entry in the war, he was skeptical that the levy could curb wartime profiteering. During the conflict, however, he became one of the few economists who supported the excess profits tax both as a revenue raiser and as a regulatory tool to combat war profiteering. And toward the end of the war, after he conducted his Treasury study, Adams became convinced that the excess profits tax had the unintended consequence of taxing smaller businesses more than the large corporations it was designed to attack. Adams’s study helped convince some of the most recalcitrant lawmakers to reconsider their support for the excess profits tax.<sup>46</sup>

To be sure, Adams was not the only academic economist who left the academy for Washington during the Great War. Indeed, well over 100 academic experts put aside their teaching to take on “war work.” In the process, these scholars-turned-policymakers accelerated the interdependence of professional expertise and governmental institutions. In his 1918 presidential address to the AEA, Irving Fisher—Adams’s Yale colleague—noted that the war emergency had been a catalyst in transforming the economics profession. The war forced economists to break free of their “academic aloofness,” as Fisher explained, to provide “genuine public service.” In the process, economists learned to depend less “on books and official reports” and more on “the pulse of real events.” With the end of the war approaching, Fisher believed the profession now had a unique opportunity to shape the new world order. “It is given to us as to no previous generation of economists to share in fixing the foundations for a new economic organization and one which shall harmonize with the principles of democracy,” Fisher announced. Adams, of course, was one of the pioneering experts taking economics out of the academy and into the trenches of democratic policymaking.<sup>47</sup>

<sup>44</sup>T. S. Adams, “Effect of Income and Inheritance Taxes on the Distribution of Wealth,” *American Economic Review* 5, no. 1 (Mar. 1915): 234–44, here 243.

<sup>45</sup>Adams, “Effect of Income and Inheritance Taxes on the Distribution of Wealth.”

<sup>46</sup>Brownlee, “Economists and the Formation of the Modern Tax System in the United States,” 415–7; Mehrotra, *Making the Modern American Fiscal State*, 334–7.

<sup>47</sup>Irving Fisher, “Economists in Public Service: Annual Address of the President,” in “Papers and Proceedings of the Thirty-First Annual Meeting of the American Economic Association,” *American Economic Review* 9, no. 1, S1 (Mar. 1919): 5–21; Barber, *From New Era to New Deal*, 2; Brownlee, “Economists and the Formation of the Modern Tax System in the United States.”

Adams's tenure in the wartime Treasury Department, like his experiences with the Wisconsin Tax Commission, influenced his views of tax reform. Unlike the other economists who enlisted for the first time and temporarily during the war, Adams had long been committed to applying his ideas to practical policy making—to “the pulse of real events,” as Fisher put it. He believed firmly in the pragmatic process of critical inquiry, of testing and verifying his tax reform ideas against the lived experience of history. His willingness to remain flexible in the face of contradictory evidence—as demonstrated by his experience with the Wisconsin income tax and the WWI excess profits tax—illustrated his commitment to disinterested, neutral, and objective expertise in the service of the state. Adams's open-mindedness was not lost on his colleagues. Robert Murray Haig, who would go on to become a leading postwar public finance economist in his own right, was a junior colleague in the Treasury Department working for Adams. Haig later recalled that Adams's mind “never ossified.” He “distrusted broad dogmatic generalizations. He preferred tentative hypotheses,” Haig noted. “It was because of this mental quality of elasticity and receptivity that men found him so stimulating.”<sup>48</sup>

Although Adams's mental elasticity may have endeared him to like-minded policy analysts, these traits were often disparaged by others. Historians have depicted Adams as a political conservative, preoccupied with administrative procedures and hence oblivious to the distributional aspects of taxation.<sup>49</sup> Even contemporaries such as Seligman—Adams's longtime interlocutor and occasional rival—chided Adams for getting too close to the political process and thus tainting the academic purity of “fiscal science.” In his memorial to Adams, Seligman noted that Adams was “a shining example” of “a scholar in politics.” But he also lamented that because of his tireless commitment to policymaking, Adams never found the time “to turn his attention to the elaboration of some *magnum opus*,” which, in Seligman's estimation, would have given his departed colleague “a lasting and international scientific reputation.”<sup>50</sup>

For Adams, such distinctions between theory and practice, or expertise and democracy, or policymaking and publishing, were false choices. Adams was not a mere tax technician concerned only with the administrative apparatus of fiscal policy; nor did he believe that his policy work compromised his scholarship. His support for progressive taxes was informed by a substantive concern about growing inequality and the popular desire for a fair and equal distribution of fiscal burdens. Neither the Wisconsin income tax, which taxed large-scale manufacturers more than small farmers, nor the federal excess profits tax aimed at war profiteering, was blind to the democratic calls for economic justice. Toward the end of his career, he reflected back on his decades of public service without any regret about placing his policy work above his academic scholarship. Writing to his friend and fellow economist Allyn Young, Adams counseled that “a big scientific career” meant much more than publishing. “You can do your work through your students, occasional articles, [and] public service.”<sup>51</sup>

Public service was, in the end, a central part of Adams's “big scientific career.” Although he wrote his share of articles and mentored several students and junior colleagues, his work with the Wisconsin Tax Commission and the U.S. Treasury Department were the highlights of his career. Despite these achievements, Adams's greatest impact on the history of tax policy and its relationship to democracy and state building may have been an idea that was ahead of its times, an idea that would one day sweep across the globe and affect nearly every country—except Adams's own.

<sup>48</sup>Fairchild, “Thomas Sewall Adams”; Robert Murray Haig in Holcomb, *In Appreciation of Thomas Sewall Adams*, 9.

<sup>49</sup>Joseph Dorfman, *The Economic Mind in American Civilization, Volumes Four and Five, 1918–1933* (New York, 1959), 214–22; C. K. Yearley, *The Money Machines: The Breakdown and Reform of Governmental and Party Finance in the North, 1860–1920* (Albany, NY, 1970), 236, 249.

<sup>50</sup>Edwin R. A. Seligman in Holcomb, *In Appreciation of Thomas Sewall Adams*, 6–7.

<sup>51</sup>T. S. Adams to Allyn A. Young, Jan. 4, 1923, quoted in Perry G. Mehrling, *The Money Interest and the Public Interest: American Monetary Thought, 1920–1970* (Cambridge, MA, 1997), 18.

### A New Tax: Adams's Proto-VAT Proposal

Adams crafted his innovative, broad-based national consumption tax during a tumultuous period in American history. The armistice ending the Great War was signed on November 11, 1918. Soon thereafter, the collapse of wartime aggregate demand and the return of over 2 million demobilized troops sent the nation into a severe, albeit brief, economic recession. Banks failed, factories closed, and businesses were liquidated. From the end of the war to 1921, the unemployment rate soared from roughly 5 percent to a decade high of nearly 9 percent. Monetary policy guided by the nascent Federal Reserve Bank only seemed to make matters worse; high interest rates exacerbated the economic decline and fueled price deflation. Resulting labor strikes and general social unrest, including a veteran's movement for a postwar bonus, added to the turmoil and uncertainty. "The crisis of 1921," Treasury Secretary Mellon recounted, "was one of the most severe this country has ever experienced."<sup>52</sup>

The turbulence of the postwar years provided commentators, policymakers, and legislators with an opportunity to reshape the future trajectory of American fiscal policy. Some influential business leaders and conservative politicians wanted to use the postwar economic crisis to turn back the clock on progressive reforms, including the graduated income tax. Their central objective was to dismantle the robust wartime fiscal state. They sought to slash income tax rates and eliminate the excess profits tax and replace it with a general sales tax, a specific form of consumption tax on everyday spending. Conservative U.S. Senator Reed Smoot (R-UT) introduced several "spending tax" bills that sought to replace the wartime profits tax, including one proposal that seemed vaguely similar to Adams's proto-VAT. Other anti-tax legislators welcomed such proposals as antidotes to the wartime trend toward steeply progressive taxes, or what one lawmaker referred to as the "modern legislative adaptation of the Communistic doctrine of Karl Marx."<sup>53</sup>

By contrast, progressive reformers sought to leverage the plasticity of the postwar period to consolidate their gains. Some tax experts wanted to maintain and bolster the profits tax as a regulatory tool to combat monopoly power. Treasury economist Robert Murray Haig contended that with the right administrative support, the United States could make a moderate business profits tax a permanent part of the postwar tax regime. "Though designed as a tank," wrote Haig, "this tax can be made to operate efficiently as a tractor."<sup>54</sup> Populist lawmakers such as Claude Kitchin (D-NC), the former chair of the U.S. House Ways & Means Committee, seemed to agree with Haig. And even some reform-minded Republicans feared that replacing the profits tax with an untried and uncertain sales tax would not only jeopardize the government's ability to repay unprecedented wartime debts; a regressive sales tax might also have adverse distributional consequences.<sup>55</sup>

Adams stepped into the middle of this political debate with his characteristic concern for effective administration. He had always been deeply ambivalent about the excess profits tax. By the end of the war, his single greatest objection to the excess profits tax was that it was undermining the potential durability of the fledgling progressive income tax—a levy that had its roots in combatting

<sup>52</sup>Goldberg, *Discontented America*; David Cannadine, *Mellon: An American Life* (New York, 2006), 278.

<sup>53</sup>"O.H. Kahn Criticizes Excess Profits Tax," *New York Times*, Jan. 22, 1920, 24; *Congressional Record*, 67 Cong., 1 sess., Apr. 12, 1921, 151–2; Roy G. Blakey and Gladys C. Blakey, *The Federal Income Tax* (New York, 1940), ch. 8.

<sup>54</sup>Robert Murray Haig, "British Experience with Excess Profits Taxation," in "Papers and Proceedings of the Thirty-Second Annual Meeting of the American Economic Association," *American Economic Review* 10, no. 1, S1 (Mar. 1920): 1–14; Robert Murray Haig and George E. Holmes, "The Taxation of Excess Profits in Great Britain: A Study of the British Excess Profits Duty in Relation to the Problem of Excess Profits Taxation in the United States," *American Economic Review* 10, no. 4, S1 (Dec. 1920).

<sup>55</sup>David Friday et al., "The Excess Profits Tax: Discussion," *American Economic Review* 10, no. 1, S1 (Mar. 1920): 19–32; *Congressional Record*, 67 Cong., 1 sess., Aug. 17, 1921, 5141 (statement of Wisconsin Republican Congressman James Frear).

inequality. "I find the deepest reason for the repeal of the excess profits tax in the conviction that its continuance would endanger the life of the income tax itself," wrote Adams in 1921. "No federal administration, in my opinion, is capable during the next five or six years of carrying with even moderate success two such burdens as the income tax and the excess profits tax."<sup>56</sup>

Unlike conservative lawmakers who objected to both the excess profits tax and the graduated income tax, Adams sought to preserve the income tax. "A successfully administered income tax," he argued, was "an essential part of financial democracy." From his time on the Wisconsin Tax Commission through his tenure in the WWI Treasury, Adams had come to value how effectively administered fiscal policies could have significant distributional effects, leading to substantive socioeconomic equality. Thus, the total elimination of a graduated income tax would be, for him, "something in the nature of political tragedy." Indeed, Adams was confident that the successful wartime administration of a robust, progressive income tax demonstrated the levy's resilience. "Looking at the matter impersonally and historically, it seems inevitable that the income tax shall fill an important, if not the primary, part of our system of federal finance," Adams predicted. "We must succeed with it."<sup>57</sup>

What would it take to succeed with the income tax? If success meant repealing the excess profits tax, how else could the federal government tax American businesses and replace the lost revenue from an abolished excess profits tax? To address these questions, Adams turned unsurprisingly to administrative simplicity. "If I followed my personal predilections," Adams wrote, "I should vote for simplicity and inequality, selecting many simple taxes at light rates rather than more equitable but more complex taxes at heavier rates."<sup>58</sup>

To achieve such simplicity, Adams recommended supplementing a lower income tax with an innovative business sales tax. Initially, Adams was ambivalent about sales taxes. He publicly opposed some of the early proposals.<sup>59</sup> But as the postwar tax reform debate unfolded, Adams began to conceptualize a new type of consumption tax, what he referred to as a "modified business sales tax" that could ease administrative burdens while complementing the existing progressive tax regime. Lost revenue from the repeal of the excess profits tax could be replaced by taxing manufacturers, wholesalers, and retailers on, what Adams referred to as, their "modified gross income," by which he meant the value that businesses added in the process of making, distributing, and selling certain goods. "In the case of producers and sellers of 'goods, wares, and merchandise' further simplicity could be achieved," explained Adams, "by giving the tax the form of a sales tax with a credit or refund for taxes paid by the producer or dealer (as purchaser) on goods bought for resale or for necessary use in the production of goods for sale." This aspect of Adams's proposal was arguably one of the first conceptual articulations of a modern "credit invoice" type of value-added tax.<sup>60</sup>

The basic concept of taxing businesses on their gross receipts was a common part of what were known at the time as "turnover" taxes. Adams's crucial innovation was the use of a "credit or refund" to determine the precise tax liability while preventing double taxation; this was an idea apparently derived from his Wisconsin income tax experience. At the time, several countries levied a tax on business sales, in one form or another. Some of these duties were often referred to as "turnover taxes" because they were levied on the transfer or "turnover" of property in the production and distribution of goods. Thus, the concept of taxing businesses, all throughout the supply chain, on their gross receipts was not new. In fact, such levies became

<sup>56</sup>Adams, "Should the Excess Profits Tax be Repealed?" 370.

<sup>57</sup>Ibid., 370–1.

<sup>58</sup>Adams, "Fundamental Problems of Federal Income Taxation," 553.

<sup>59</sup>T. S. Adams, *Needed Tax Reform in the United States* (New York, 1920).

<sup>60</sup>Adams, "Fundamental Problems of Federal Income Taxation," 553; John F Due, "The Value-Added Tax," *Western Economic Journal* 3, no. 2 (Spring 1965): 165–71, here 165. For more on the current "credit-invoice" VAT, see Schenk and Oldham, *Value Added Tax*, 34–9.

increasingly popular during WWI as a simple way to raise revenue with limited administrative capacity.<sup>61</sup>

These turnover taxes, however, created the problem of pyramiding or cascading taxes, whereby there was a tax on a tax. Thus, multiple taxes could potentially be levied on the same product. This was a problem familiar to Adams from his Wisconsin experience. The cascading effect of turnover taxes mirrored the potential double taxation of personal property with a new income tax. One way to resolve this problem was to provide businesses with a “credit” for the taxes already paid on the inputs of production. Just as Wisconsin taxpayers could use the property taxes they had paid as a credit against their income tax liability to avoid double taxation, businesses—under Adams’s new plan—could subtract the taxes paid on their inputs from their gross receipts to arrive at a net tax base that avoided cascading taxes. The notion of using a “credit” to measure more accurately the precise “value added” by different businesses in the production process appeared to be Adams’s true innovation and contribution, but one that seemed ahead of its time.<sup>62</sup>

Portions of Adams’s proposal influenced policymakers. His criticism of the excess profits tax facilitated the levy’s ultimate repeal. But other parts seemed unlikely to be adopted. Indeed, Adams appeared to have an uncanny sense of the political futility of his more bold and ambitious recommendation for a proto-VAT or his “modified gross income” tax on businesses. “The plan has little chance of adoption,” Adams conceded. Still, he believed failure served “the useful purpose of illustrating the futility of basing one’s principles on one’s personal experience”:

It demonstrates the supreme necessity of subordinating administrative logic and personal predilections to the great political and social forces which control the evolution of tax systems. These forces must be accepted as facts. The historical fact is that modern states prefer equity and complexity to simplicity and inequality. The cry for equality and justice is louder and more unanswerable than the demand for certainty and convenience. You may think it sentimental and stupid, but that does not alter the fact.<sup>63</sup>

Indeed, Adams did not believe that the democratic clamor for equality and justice was either sentimental or stupid. With his historical sensibilities, he was aware of how “great political and social forces” influenced expert-driven policy making. Respect for democratic forces was, part and parcel, of his pragmatist approach to policy making. Indeed, Adams had seen it firsthand on the Wisconsin Tax Commission, as well as in his experience with the WWI excess profits tax.

For Adams and other progressive reformers, the income tax seemed to have its own internal democratic dynamics and institutional inertia borne out of the sequence of historical events. “The income tax, whose complexity is not exaggerated by its critics, spreads and grows,” wrote Adams, “it has a deeper and wider following with the passing generations.” Evoking the recent history of the federal income tax, Adams identified how the levy seemed to have a special appeal in liberal democracies like the United States. The income tax “seems to be particularly irresistible in a democratic state in which customs, excise or sales taxes (whose burden is or is believed to be regressive) constitute the backbone of the tax system,” wrote Adams. “Replace the complexities of the income tax with the simplicities of the sales tax tomorrow, and within ten years the income tax would be back. In the light of financial history ‘simplicity’

<sup>61</sup>Alfred G. Buehler, “Recent Developments of the General Sales Tax,” *Journal of Political Economy* 36, no. 1 (Feb. 1928): 83–99; Carl Shoup, *Public Finance* (Chicago, 1969), 207.

<sup>62</sup>John F. Due, *Indirect Taxation in Developing Economies: The Role and Structure of Customs Duties, Excises, and Sales Taxes* (Baltimore, 1970), ch. 6; Andrew Chamberlain and Patrick Fleenor, “Tax Pyramiding: The Economic Consequences of Gross Receipts Taxes,” *Tax Foundation Special Report* 147 (Dec. 2006).

<sup>63</sup>Adams, “Fundamental Problems of Federal Income Taxation,” 554.



is a lesser god.”<sup>64</sup> Like other social democrats and progressives, Adams understood that the democratic principle of equality went well beyond the political sphere to encompass other parts of society and economy. Adams’s remarks about “the great political and social forces” accurately described the chronology and historical development of U.S. tax law and policy from an era of nineteenth-century regressive tariffs and excise taxes to the modern progressive income tax.<sup>65</sup>

At first blush, it might seem surprising that Adams, the technocratic expert, preferred the simple solution to maintaining an effective tax system. Experts, with their technical skills and advanced knowledge, often embrace complex answers to intricate social challenges. But Adams had learned from his prior administrative experiences that a well-functioning fiscal state relied on harnessing popular opinion. Ultimately, Adams’s comments about the historical development and institutional inertia of American tax policy proved prescient. His comments foreshadowed the American resistance to a comprehensive national sales tax in 1921 and for many decades to come.

### The Origins of the French and German VATs

Adams, to be sure, was not the only tax expert contemplating novel ways to stabilize the postwar political economy and rationalize the tax system. Across the Atlantic, European commentators were proposing their own ideas, including versions of broad-based consumption taxes that would gradually evolve into proto-VATs. France and Germany were two leading examples. Like many of the other WWI combatants, France and Germany adopted a modern income tax during the conflict, but earlier consumption taxes continued to dominate in both countries, including into the postwar decades. The WWI French income tax was riddled with administrative complications that, combined with the country’s popular resistance to a centralized state, forced the French government to rely heavily on consumption taxes and loans, rather than income or wealth-transfer taxes, to underwrite the war. The United States pursued the opposite path, relying mainly on income and profits taxes and much less on excise taxes and bonds.<sup>66</sup>

After the conflict, the French consolidated their reliance on consumption taxes. The country’s longstanding social antipathy toward an “inquisitorial income tax” and its historical dependence on sale and excise taxes led to the adoption in 1920 of a general consumption or turnover tax, *taxe sur les chiffres d’affaires* (TCA), which was levied on nearly all transactions related to the production and distribution of goods and services. In the following decades, incremental revisions and improvements to the French TCA would lead eventually to the adoption of the first modern VAT in 1954. As Columbia University economist and longtime VAT supporter Carl Shoup explained, the VAT’s gradual emergence in France illustrated “the process by which a sort of continuing ferment of improvisation now and then gives rise to an invention of the first order.”<sup>67</sup>

Like France, Germany also relied on consumption taxes during and after the war. Because the German constitution restricted the direct taxation of income to provincial governments, it was not until WWI that the German Reich acquired the power to levy a national income tax.

<sup>64</sup>Ibid., 555.

<sup>65</sup>Ibid., 554; Kloppenberg, *Uncertain Victory*, 6.

<sup>66</sup>Henri-Simon Bloch, “The Evolution of French Taxation—An Historical Sketch,” *Bulletin of the National Tax Association* 25, no. 9 (June 1940): 266–73; Robert Murray Haig et al., *The Public Finances of Post-War France* (New York, 1929); Morgan and Prasad, “The Origins of Tax Systems”; Hugh Rockoff, *America’s Economic Way of War: War and the US Economy from the Spanish-American War to the Persian Gulf War* (New York, 2012), ch. 5.

<sup>67</sup>Carl S. Shoup, “Taxation in France,” *National Tax Journal* 8, no. 4 (Dec. 1955): 325–44, here 328; Carl S. Shoup, *The Sales Tax in France* (New York, 1930); Mirja Salo, “The Ideas of Maurice Lauré on VAT in the 1950s,” *World Journal of VAT/GST Law* 3, no. 2 (2014): 130–40.

Given this delay, the German government and many of the country's regional regimes had come to rely heavily on a variety of consumption taxes. In 1918, Germany adopted a new turnover tax to help fund the war. This tax was levied at a relatively high rate on both everyday commodities and services, and at an even higher rate on luxury goods. Subsequently, the inertia of earlier consumption taxes, together with the 1918 turnover tax, carried over into the postwar period. Reflecting back on the partial success of the French and German consumption taxes, Columbia economist Shoup observed that "France can be said to share with Germany the achievement of demonstrating that the general turnover tax is workable as a peacetime fiscal measure."<sup>68</sup>

While the turnover tax may have been a "workable" fiscal measure, it was not without its flaws. A turnover tax levied on each stage in the production and distribution of goods led to a tax on a tax. This pyramiding effect troubled German manufacturers and business leaders because of their relatively high turnover tax rate, and because a cascading tax encouraged businesses to combine vertically to limit their turnover tax liability. At roughly the same time that T. S. Adams was making the case for his proto-VAT, the German businessman and politician Carl Friedrich von Siemens authored a 1921 pamphlet arguing for a "refined turnover tax" that would address the pyramiding problem. Von Siemens's publication was a popularization of ideas first proposed by his older brother Wilhelm von Siemens, the longtime leader of the Siemens Corporation.<sup>69</sup>

The Siemens brothers contended that the existing "gross turnover tax" was unfair because it "unevenly taxed businesses" by favoring vertically integrated firms and because the pyramiding effect distorted prices. With the German government about to double the already high turnover tax rate, the 1921 pamphlet explained the logic of how a "net turnover tax"—one that subtracted "the prior turnover" of inputs from a taxpayer's "gross turnover"—could both raise sufficient revenue and treat German businesses fairly.<sup>70</sup> This proposal was remarkably similar to Adams's "modified gross income" tax on businesses. Like Adams, the Siemens brothers emphasized the simplicity of their proposal. All that was necessary was for a business to maintain accurate accounting of input costs and its gross receipts. "At the end of the fiscal year the prior turnovers are to be added together and deducted from the total value of the gross turnover; the remaining balance (the net turnover) is subject to tax," the pamphlet explained. "Otherwise, nothing essential needs to be changed."<sup>71</sup>

Like Adams, Siemens also understood the historic need for fundamental tax reform and its potential political challenges. "In the weakened state of our manufacturing capacity," they wrote, "we must be eager to arrange the taxation of goods production so economically that it brings about the greatest yield possible at the lowest cost possible." Yet, they also knew that German officials would be reluctant to experiment with any radical changes to the turnover tax during the post-WWI economic crisis, when the country's fiscal stability remained precarious. As Carl Friedrich von Siemens concluded, his brother's "net turnover tax" was rejected by German officials "for reasons whose cogency of proof is unintelligible."<sup>72</sup> Nonetheless, though Germany did not

<sup>68</sup>Carl S. Shoup, "Taxation in France," 328; Alzada Comstock, "The German Turnover Tax," *Barron's* Sept. 25, 1922, 3, 8; Buehler, "Recent Developments of the General Sales Tax." For more on the history of turnover taxes, see Richard D. Pomp, "Turnover Taxes: Their Origin, Fall from Grace, and Resurrection," *Journal of State Taxation* 40, no. 1 (2021): 17–20.

<sup>69</sup>Carl Friedrich von Siemens, *Veredelte Umsatzsteuer* [Refined Sales Tax] (Siemensstadt, 1921); Schenk and Oldman, *Value Added Tax*; Siemens Historical Institute et al., *Shaping the Future: The Siemens Entrepreneurs 1847–2018* (Hamburg, Germany, 2018).

<sup>70</sup>Siemens, *Veredelte Umsatzsteuer*, 3.

<sup>71</sup>*Ibid.*, 7, 10–1.

<sup>72</sup>*Ibid.*, 18. Some American tax scholars have speculated that Adams may have read German, and thus developed his proto-VAT ideas after encountering the work of Carl Friedrich von Siemens. Richard W. Lindholm, "The Value Added Tax: A Short Review of the Literature," *Journal of Economic Literature* 8, no. 4 (Dec. 1970): 1178–89. There

adopt the proto-VAT advocated by Siemens, it strengthened its reliance on the turnover tax, which, like its French counterpart, evolved gradually into a modern VAT decades later.<sup>73</sup>

The economic and social dislocations of the immediate postwar years provided nearly all countries engaged in the Great War an opportunity to re-evaluate seriously their tax systems. Germany and France solidified their reliance on consumption taxes through different forms of turnover taxes that eventually evolved into the world's first modern VATs. By contrast, the United States rejected broad-based national consumption taxes and strengthened its commitment to income taxes, just as Adams had predicted. The power of American democratic forces overwhelmed the ideas of experts like Adams. But Adams's proto-VAT proposal was not the only consumption tax proposal circulating among policy analysts and lawmakers. Several other "spending taxes" were debated at the time. If any of them had been adopted, perhaps the United States would have followed France and Germany in shifting the balance of its national tax base toward consumption rather than income—and perhaps over time, like France and Germany, the United States would have joined the rest of the industrialized world and enacted its own national VAT to fund more muscular social-welfare spending.

### The Rejection of the 1921 U.S. Consumption Tax Proposals

Adams proposed his proto-VAT amid a post-WWI legislative debate over tax reform. On one side, conservative Republican legislators, such as Senator Reed Smoot, were advocating a general sales tax to replace the excess profits tax and the steeply graduated income tax. On the other side, populist political leaders like Rep. Claude Kitchin and progressive Senator Robert M. LaFollette (R-WI) sought to bolster the income tax and the excess profit tax as permanent parts of a postwar fiscal regime, and thus avoid any consideration of sales taxes. Adams found himself somewhere in the middle. He did not believe the excess profits tax was an effective levy, yet he was also not an unequivocal supporter of a general sales tax. His "modified gross receipts" tax on business was his attempt at a creative, though admittedly idealistic, compromise.<sup>74</sup>

Even before Republicans took control of Washington, Adams shared his initial skepticism of a broad national sales tax. In a series of summer 1920 articles in the popular *New York Evening Post* and congressional testimony, Adams articulated his general views on tax reform. Like many mainstream economists and lawmakers, Adams supported the elimination of the excess profits tax and a reduction in the top individual rates, mainly to ease administrative burdens and save the income tax. But Adams did not believe that a general sales tax levied on all spending was a suitable replacement. Adams admitted that a sales tax had benefits. It "would carry a very low rate; it would be highly productive, and the taxpayer would know with certainty the amount which he was expected to pay," he wrote.<sup>75</sup>

But Adams believed the different consumption taxes under consideration had several flaws. Even a simple sales tax would be a new levy that would strain the government's already stretched administrative resources. Replacing taxes on income and profits with a consumption tax would also likely shift the burden of taxation from capital to labor, from those with the greatest ability to pay to

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is little evidence, however, that Adams either knew German or that he had any direct contact with the Siemens brothers. It is equally likely that many experts were re-evaluating turnover taxes during this time period.

<sup>73</sup>Berhard Grossfeld and James D. Bryce, "A Brief Comparative History of the Origins of the Income Tax in Great Britain, Germany and the United States," *American Journal of Tax Policy* 2 (Spring 1983): 211–51; Claus Staringer, "Tax in History: GAAR-dians of the Tax Galaxy: A 100-Year GAAR Journey from Germany to Austria and Back to the EU," *Intertax* 47, no. 11 (Nov. 2019): 986–8.

<sup>74</sup>A general sales tax would be administered as a retail sales tax and thus different from Adams's VAT, which would tax businesses all along the supply chain of production and distribution. For more on the differences between a VAT and a retail sales tax, see Burman and Slemrod, *Taxes in America*, 100–1.

<sup>75</sup>T. S. Adams, "Sales Tax Favorite Remedy for All the Ills of the Taxpayer," *New York Evening Post*, Aug. 2, 1920, 9.

the least.<sup>76</sup> At a time when popular opinion was already railing against the high cost of living, a new tax that was passed on to ordinary consumers would only inflame opposition to taxes. “While the cost of living remains so high,” wrote Adams, “the sales tax is probably a political impossibility.”<sup>77</sup> Finally, Adams opposed a “turnover” sales tax because of the problems associated with pyramiding taxes. A turnover tax would accumulate taxes on taxes, and it would provide an incentive for firms to combine vertically, rewarding business combinations or “trusts.”<sup>78</sup>

Surprisingly, however, Adams did not mention—either in his congressional testimony or newspaper articles—the use of a credit to address the pyramiding problem of a turnover tax. Perhaps describing his proto-VAT was too technical for general audiences or reluctant legislators. Perhaps Adams had not yet formulated the specific design of his “credit invoice” proto-VAT. Regardless, Adams concluded his newspaper commentary with the suggestion that if lawmakers were committed to taxing consumption, “why not carry the tax to its logical outcome—a tax on articles of consumption other than necessities, levied preferably on a few large industries which deal in non-essentials of widespread consumption in order that the tax may be effectively and cheaply administered.”<sup>79</sup> Adams’s focus on limiting any new sales tax to non-essentials demonstrated his awareness of the potential regressivity of consumption taxes, as well as his concern about inequality. A year before he formally described his credit-invoice, proto-VAT in the *Quarterly Journal of Economics*, Adams appeared open to a specific kind of comprehensive sales tax, one that excluded everyday necessities.

Although Adams was a key Treasury Department official when he shared his tax reform ideas, he appeared to be one of the few administration officials interested in a sales tax of any kind. President Harding himself did not care much about taxes. In an April 1921 address to Congress, the president barely mentioned tax reform, beyond stating that “the country does not expect and will not approve a shifting of burdens.”<sup>80</sup> Even Treasury Secretary Mellon was indifferent to a sales tax. From the start, Mellon was eager to design a bipartisan “Mellon Plan” for “scientific” tax reform focused on tax cuts for the wealthy. As Mellon explained, “Tax revision should never be made the football either of partisan or class politics but should be worked out by those who have made a careful study of the subject in its larger aspects.”<sup>81</sup> Ultimately, he pushed for a tax reform plan that focused on slashing income tax rates with little to no attention to sales tax proposals. Mellon was no foe of experts crafting and implementing fiscal policies, as long as they were his experts.<sup>82</sup>

If the sales tax was an afterthought for Mellon and the Harding administration, it was a top priority for Senator Smoot and his allies. Several sales tax proposals were circulating at the start of the Spring 1921 legislative session; yet by the summer, Smoot’s proposal emerged as the most popular. Smoot, in fact, proposed several different types of sales taxes during the legislative session, including one that was vaguely similar to Adams proto-VAT. Smoot seemed unconcerned with the potential regressivity of a sales tax and was focused primarily on eradicating the income tax by finding a suitable replacement. Concern for the great political and social forces that troubled Adams seemed to be missing from Smoot’s calculus.<sup>83</sup>

<sup>76</sup>On the importance of “ability to pay” as a conceptual foundation for the income tax, see Mehrotra, *Making the Modern American Fiscal State*, 9–10.

<sup>77</sup>Adams, “Sales Tax Favorite Remedy,” 9.

<sup>78</sup>Ibid. See also U.S. Congress, House of Representatives, Committee on Ways and Means, *Revenue Revision: Hearings before the Committee on Ways and Means*, 66 Cong. 3rd sess., Dec. 13–14, 1920, 3–42.

<sup>79</sup>Adams, “Sales Tax Favorite Remedy,” 9.

<sup>80</sup>*Congressional Record*, 67 Cong., 1 sess., Apr. 12, 1921, 170.

<sup>81</sup>Andrew W. Mellon, *Taxation: The People’s Business* (New York, 1924), 11.

<sup>82</sup>For more on Mellon’s plan for “scientific” taxation, see Cannadine, *Mellon*, 315–6; Murnane, “Selling Scientific Taxation”; Smiley and Keehn, “Federal Personal Income Tax Policy in the 1920s”; and Isaac William Martin, *Rich People’s Movements: Grassroots Campaigns to Untax the One Percent* (New York, 2013).

<sup>83</sup>*Congressional Record*, 67 Cong., 1 sess., Nov. 4, 1921, 7295; “Smoot Offers Substitute Proposal,” *Wall St. Journal*, Nov. 2, 1921, 11.

Unsurprisingly, the reception to Smoot's sales tax was mixed. The business community was divided, unsure how the tax would impact the bottom line of many different industries. Agrarian associations and labor unions were opposed to the levy on the grounds that its incidence would be regressive, shifting the ultimate tax from producers to consumers and adding to the already high cost of living—just as Adams had predicted. And some progressive lawmakers would only cede to a sales tax if it was earmarked to pay for a soldier's bonus.<sup>84</sup>

The divisions within the business community were a fatal blow to Smoot's proposal. Although a consumption tax was championed initially by influential commercial leaders such as the New York banker Otto Kahn, other powerful business associations were fragmented in their support. Those industries that were directly affected by the wartime luxury excise taxes were eager to have a general consumption tax replace the excess-profits tax and the special high-end sales taxes that were disproportionately affecting their industries. These luxury taxes, they argued, were "unjust, unfair, discriminatory and un-American." Business backers of the general sales tax even created special organizations, such as the Business Men's National Tax Committee and the Tax League of America, to endorse Smoot's bill and develop a coordinated, though ultimately unsuccessful, public relations campaign in favor of the sales tax. Several conservative lawmakers heeded these calls and welcomed the opportunity, as Senator Moses (R-NH) explained, to "strike down the vicious principle of graduated taxation."<sup>85</sup>

By contrast, many other businesses were deeply ambivalent about Smoot's sales tax. As early as February 1921, the U.S. Chamber of Commerce supported the repeal of the excess-profits tax but opposed the sales tax. Likewise, industries with slim profit margins, from retailers to grocers and food processors, opposed the new and untried sales tax because they were uncertain of how it would affect their profits. Tax experts and industry leaders debated the levy's incidence, whether a sales tax would be absorbed by businesses or shifted to consumers. The National Association of Credit Men, influenced by Adams's research, vigilantly opposed the sales tax because of its potential negative impact on profits. In Congress, these industries were represented by Senators such as Irvine Lenroot (R-WI), who proclaimed that "if the tax can not be passed on to the consumer, a 1 per cent tax ... will impose a tax of from 30 to 50 or 60 percent on the net income of those corporations" susceptible to the new levy.<sup>86</sup>

Other business groups were reluctant to support a regressive sales tax for social and political reasons. The political optics of replacing highly progressive income and profits taxes with a regressive sales tax appeared too dangerous. One of the country's most influential commercial groups, the National Industrial Conference Board, created a special committee to consider the tax and concluded that supplanting progressive income and profits taxes with a regressive sales tax was "indefensible." The distributional consequences of the shift belied any sense of corporate fiscal citizenship. The committee explained:

We haven't the nerve, as good citizens of the country—which we believe we are and are trying to be—to say to a body of business men in this country, who are suggesting that business be relieved from a billion dollars of excess profits tax, that we propose a tax which will cause the billion to be paid by the ultimate consumer.... That is such a violent divergence from the principle of payment upon the basis of ability to pay, that we cannot ask this body of business men to get behind that sort of tax.... We don't think that is good

<sup>84</sup>"Fordney Puts Ban on Sales Tax Now," *Washington Post*, Nov. 3, 1921, 1; "Bar Sales Tax Now, Want It for Bonus," *New York Times*, Nov. 3, 1921, 1.

<sup>85</sup>"Excess Profits Tax or Sales Tax?" *New York Times*, May 30, 1920, XX2; "Manufacturers Favor Smoot Plan of General Tax Levy," *Wall Street Journal*, Sep. 17, 1921, 7; "Fur Men for Sales Tax to Replace Excise," *Women's Wear*, May 24, 1921, 1, 34. For more on the Tax League of America, see Murnane, "Selling Scientific Taxation," 843–51; and Martin, *Rich People's Movements*, ch. 2.

<sup>86</sup>"Business Favors Profit Tax Repeals," *Washington Post*, Feb. 27, 1921, 3; "Dr. Adams Warns Credit Men on Turnover Tax," *Chicago Daily Tribune*, Feb. 18, 1921, 4; *Congressional Record*, 67 Cong. 1 sess., Nov. 3, 1921, 7243.

citizenship; and we don't think that is good economics. That is the real reason that we ... rejected the sales tax, upon the assumption that the tax is paid by the ultimate consumer.<sup>87</sup>

With the business community fragmented, opponents of consumption taxes sought to defeat the sales tax proposals. The opposition was led by organized agricultural and labor associations and their congressional representatives. As petitions from farm federations and labor unions opposing the sales tax poured into congressional offices, leaders of these organizations testified before Congress about the unfairness of shifting to a consumption tax. "I believe that if the general sales tax ... were substituted for the higher surtax brackets and the excess profits tax," proclaimed H. S. McKenzie of the American Farm Bureau Federation, "you would be putting an undue burden on the people who are already heavily burdened under the present tax rate." T. C. Atkeson of the National Grange, likewise, contended that the sales tax "adds an unfair burden to all purchasers without reference to their ability to pay."<sup>88</sup>

Labor unions similarly objected to shifting the tax base from producers to consumers. "Big business not being satisfied in reducing the workers' standard of living is now attempting to shift the burden of war and the cost of Government from their shoulders onto the backs of the working men and women of this country," declared Edward F. McGrady, a representative for the American Federation of Labor.<sup>89</sup> Lawmakers representing these key constituents echoed the concerns about distributional inequities, noting how a sales tax had the potential to fall "on everything we eat and wear, whereby every man, woman, and child in this country would be taxed."<sup>90</sup> Ultimately, Smoot's sales tax proposals were defeated in Congress due mainly to the power of key lawmakers from regions with a strong labor presence and from the agricultural bloc. Political reporters succinctly summarized that Smoot's general sales tax proposals stood "no ghost of a show of enactment, not because the idea is bad but because legislators believed that it is politically inexpedient.... They believe that the farmers and the laboring men are against it."<sup>91</sup> Just as Adams had anticipated, the democratic cries for "equity and complexity" triumphed over "simplicity and inequality."

The congressional defeat of the 1921 sales tax proposals marked the end of the first significant attempt at a broad-based national consumption tax in American history. Adams did not introduce the specifics of his proto-VAT into the popular or political debates of the time, but he did publicly favor a moderate sales tax on non-essentials to ease the administrative burdens on the income tax. For him, this was a first step toward a rational and sensible tax system. And, over time, even a crude national consumption tax might have evolved into a VAT, as it did in France and Germany.

Yet, Adam suspected that even a modest U.S. sales tax, let alone his more subtle proto-VAT, was "impossible" given the country's postwar economic and social conditions and the broad historical development of American tax law and policy. The organized political interests that shaped economic policy confirmed Adams's conjecture. A fragmented business community

<sup>87</sup>National Industrial Conference Board, *Proceedings of the Second National Industrial Tax Conference: Special Report No. 17* (New York, 1920), 40–1.

<sup>88</sup>U.S. Congress, Senate, Committee on Finance, *Internal-Revenue Hearings on the Proposed Revenue Act of 1921*, 66 Cong. 1<sup>st</sup> sess., May 9–27, 1921, 310, 342. As an example of the many petitions sent to Congress, see generally, John J. Quinlivan to William W. Chalmer, Apr. 29, 1921, Petitions and Memorials, Resolutions of State Legislatures, and Related Documents which Were Referred to the Committee on Ways and Means during the 67th Congress, Petitions and Memorials, 1799–1966, Records of the U. S. House of Representatives, RG 233, National Archives and Records Administration, Washington, DC.

<sup>89</sup>"Labor Warns Against Sales Tax Program," *Baltimore Sun*, May 25, 1921, 2.

<sup>90</sup>*Congressional Record*, 67 Cong. 1 sess., Aug. 17, 1921, 5141.

<sup>91</sup>"Sales Tax and the Farmers," *Wall Street Journal*, June 23, 1921, 1; "Agriculture Bloc Opposes Tax Bill," *Atlanta Constitution*, Oct 6, 1921, 1; "Smoot Sales Tax Defeated," *Detroit Free Press*, Nov 4, 1921, 1. For succinct retrospective summary of Smoot's sales tax, see generally, Buel W. Patch, "Sales Taxes: Federal, State, and Foreign," *Editorial Research Reports* (1931): 861–80.

and the strong opposition from organized labor and farmers defeated the nation's first possible experiment with a federal consumption tax. Adams was not surprised. Indeed, he had predicted it. The rejection of the 1921 sales tax reflected what Adams referred to as the power of "the great political and social forces which control the evolution of tax systems."<sup>92</sup>

## Conclusion

Thomas S. Adams was, above all, a political realist. His proposal for a proto-VAT was an aspirational goal. It was an idea that he framed for an academic audience, not a popular one. Consequently, Adams's proto-VAT was not specifically debated as part of the 1921 Revenue Act. Nonetheless, any one of the national sales tax proposals considered at the time might have evolved eventually into a modern VAT and perhaps even into the credit-invoice VAT that Adams envisioned, just as other crude consumption taxes had done in France, Germany, and elsewhere. For Adams and other experts, adopting a modest, broad-based, national consumption tax—such as a general sales tax—might have been an early solution to the country's post-WWI fiscal woes. It might have eased the administrative burdens on the income tax, as Adams suggested. It might have provided a robust source of revenue to replace the lost receipts from the repeal of the excess profits tax. And perhaps most importantly it might have provided a new source of federal funding to underwrite new social-welfare spending, including the elusive WWI veteran's bonus.<sup>93</sup>

Instead, during the subsequent decades, the federal government reaffirmed U.S. reliance on progressive income taxes. At the same time, state and local governments began to experiment with consumption taxes in the form of narrow excise taxes on gasoline and other specific commodities. Once the Great Depression forced subnational governments to search for alternatives to declining income and property tax revenues, the initial excise taxes gradually grew into more general retail sales taxes, which, by the mid-century, became significant sources of state and local tax revenues. There was social and political resistance to state and local consumption taxes, to be sure. But the altered economic and political conditions of the 1930s and the differing historical development of subnational taxes provided state and local officials with the unique circumstances to overcome the popular resistance to regressive consumption taxes. By the mid-twentieth century, comprehensive consumption taxes became the prerogative of state and local governments, just at a time when mass merchandising and advertising were fast becoming the pillars of a new "consumer's republic." These state and local sales taxes would soon become obstacles to the subsequent calls for a broad-based national consumption tax of any kind, let alone a VAT.<sup>94</sup>

Without a broad national consumption tax in the 1920s, the United States missed an opportunity to develop the foundation for a robust source of future federal revenues. The rejection of a comprehensive national consumption tax at a critical juncture in the path-dependent process of policy making had an enduring impact on the future development of the modern American fiscal and social-welfare states. There were, to be sure, other factors that shaped the unique historical trajectory of American social spending, including the legacies of a "liberal tradition," the lack of working-class political parties, and of course racial politics.<sup>95</sup> But the historical resistance to a robust source of funding, such as a VAT, is an equally important, if often overlooked,

<sup>92</sup>Adams, "Fundamental Problems of Federal Income Taxation," 554.

<sup>93</sup>Michael Keen and Ben Lockwood, "Is the VAT a Money Machine?" *National Tax Journal* 59, no. 4 (Dec. 2006): 905–28; Liam Ebrill et al., *The Modern VAT* (Washington, DC, 2001).

<sup>94</sup>Robert M. Haig and Carl Shoup, *The Sales Tax in the American States* (New York, 1934); Carl-Henry Geschwind, *A Comparative History of Motor Fuels Taxation, 1909–2009* (Lanham, MD, 2017); Lizabeth Cohen, *A Consumer's Republic: The Politics of Mass Consumption in Postwar America* (New York, 2003).

<sup>95</sup>Lipset and Marks, *It Didn't Happen Here*; Alesina et al. "Why Doesn't the United States Have a European-Style Welfare State?"

factor. The reliance on highly salient progressive income taxes, combined with the peculiar and stealth nature of “hidden,” “divided,” and “submerged” social-welfare spending, have fueled popular skepticism about progressive social democracy. Thus, this story about missed opportunities not only chronicles the history of early twentieth-century U.S. tax law and policy; it also helps explain the long-term features of the modern American state, and perhaps even the limits of fiscal policy in addressing contemporary concerns about growing inequality.<sup>96</sup>

The complicated relationship between experts and democracy undergirded this peculiar and distinctive history of American state-building. The rejection of a national consumption tax illustrates that the alliance between scientific knowledge and the modern fiscal state was fragile and contingent. Experts could not simply select the optimal policy solution to economic and social problems without considering organized political interests. “Class politics,” as Adams noted, “is the essence of taxation.”<sup>97</sup> In the battle over the 1921 sales tax proposals, class politics triumphed. Without a unified business community behind the new sales tax proposals and with organized labor and farmers opposed to the new tax, there was little chance that a potentially regressive levy would be accepted by ordinary Americans or their elected representatives. As a result, an innovative tax developed by an American economist—a tax that could have generated sufficient revenue to pay for the elusive WWI veterans’ bonus and possibly many other social-welfare benefits—was defeated in the United States.

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<sup>96</sup>Howard, *The Hidden Welfare State*; Jacob S. Hacker, *The Divided Welfare State: The Battle over Public and Private Social Benefits in the United States* (New York, 2002); Suzanne Mettler, *The Submerged State: How Invisible Government Policies Undermine American Democracy* (Chicago, 2011); Molly Michelsmore, *Tax and Spend: The Welfare State, Tax Politics, and the Limits of American Liberalism* (Philadelphia, 2012).

<sup>97</sup>Adams, “Ideals and Idealism in Taxation,” 1.