

The Emperor's New Clothes: A New Democrat Critique of the Bush Tax Plan

President George W. Bush's \$1.6 trillion tax cut plan is fiscally irresponsible, dangerous for the economy, blind to America's future needs (especially those associated with the retirement of the baby boomers), and heavily targeted towards benefits for the wealthy Americans who least need tax relief. It represents the age-old and thoroughly discredited conservative idea that reducing marginal tax rates on the highest of high earners is the key to long-term economic growth -- an idea that led in the 1980s to the accumulation of trillions of dollars in public debt that we are still struggling to pay off. It also represents a 180-degree reversal of the successful economic and fiscal policies of the last eight years, which produced the best economy since the 1960s, rising incomes for every category of Americans, and the very budget surpluses that make tax relief possible today.

In other words, the Bush tax proposal represents a clear choice between the tax policies and economic strategies of the 1980s and the 1990s. The Administration and Congressional Republicans are trying to dress up this familiar choice in new clothes, using dubious surplus projections, irresponsible economic scare tactics, misleading anecdotes about the benefits to "real people," and train-leaving-the-station logrolling. The following are a series of talking points in response to the case Republicans are trying to make.

GOP Claim: Future budget surpluses are so large that we can afford the President's tax cut while paying down the national debt, keeping Social Security and Medicare solvent, and dealing with other national priorities.

New Democrat Response: The Bush tax plan relies on shaky surplus estimates that do not include the President's own spending promises and do not reflect the enormous costs associated with the retirement of the baby boom generation. If the estimates are wrong, the Bush plan would sacrifice fiscal discipline, debt payment, Social Security and Medicare solvency, and bipartisan domestic initiatives for tax cuts.

- Future budget surplus estimates are just that: estimates based on a whole host of economic assumptions which change constantly. Tax cuts, by contrast, are permanent changes in law that directly affect revenue collections. According to the Congressional Budget Office, a reduction in the rate of economic growth of 1 percent a year coupled with a 1 percent annual increase in health costs would reduce future budget surpluses by \$4 trillion over the next ten years. That would wipe out the projected non-Social Security surplus of \$3.1 trillion and create a deficit of \$500 billion. Moreover, the CBO projections were already inflated because CBO is required by law to assume that defense and domestic spending will grow only as fast as inflation (in recent years Congress has appropriated funds for those purposes at twice that pace) and that expiring tax provisions will not be extended (though most of them will).

- Even if you use current surplus estimates with all their uncertainties and omissions, the Administration's budget numbers just don't add up. According to CBO, there's a \$3.1 trillion non-Social Security surplus if all goes well. After subtracting the Medicare surplus of almost \$400 billion -- which both sides in Congress have repeatedly voted to protect -- and the \$120 billion cost of extending expiring tax breaks, that leaves roughly \$2.6 trillion. Bush's tax cut is pegged at \$1.6 trillion, plus at least \$300 billion in extra interest payments. Making the tax cut retroactive to January 1, 2001 -- as Bush has proposed -- would add another \$400 billion to the total, plus more interest. That pretty much wipes out the surplus.
- But where is the money going to come from to pay for *the campaign promises President Bush himself made*? Just to cite a few of the President's top priorities, the Bush tax scheme assumes there will be no increase in federal education funding to ensure that "no child is left behind;" no effort to reduce illiteracy; no prescription drug benefit under Medicare; no progress on extending health coverage to the 43 million uninsured Americans; no new funds to address military readiness or adopt new defense technologies; no deployment of a missile defense system; no housing or environmental or energy initiatives. If the President is willing to forego all these campaign promises in pursuit of a tax cut, he should admit it; if not, he should revise his own estimates.
- The risk involved in enacting this particular tax cut is actually understated by all these ten-year numbers, because *soon after the tax cut is fully implemented, surpluses start turning into large deficits after the baby boom generation begins to retire*. There is an estimated \$3 trillion gap between the amount of revenues that will be available to pay for the Social Security benefits we will owe the baby boomers, not to mention Medicare, whose future costs could balloon if health costs continue to rise.
- While a prudent budget can and should provide for some tax relief, there's not "plenty of money around" for the particular plan promoted by the President, unless the country is willing to run the risk that we will not be able to pay down the national debt; keep Social Security and Medicare solvent; pay for critical national priorities like education reform, a prescription drug benefit, a strong national defense, expanded health insurance and the investments in infrastructure and basic research we need to keep the economy strong. If the Administration really believes in its own numbers, it should readily accept the idea -- proposed by Federal Reserve Board Chairman Alan Greenspan in his recent testimony to the Senate Budget Committee, and since proposed by a bipartisan group of Senators led by DLC Chairman Evan Bayh -- that **any tax cut scheme should include a "trigger" that makes it contingent on continued economic growth and continued progress in paying down the national debt.**

GOP Claim: The Bush tax plan is fair because it reduces everyone's tax rates.

New Democrat Response: The Bush plan is unfair because it grossly favors the wealthy in the taxes it cuts, the rates it reduces, and the actual tax relief it provides.

- The Bush tax plan focuses almost exclusively on three kinds of taxes: the estate tax, the gift tax, and the income tax. The first two by definition only affect people with significant wealth (for example, estates under \$600,000 in value are already exempt from taxation, a figure that is about to rise to \$1 million under current law). Indeed, only about 43,000 Americans pay any estate tax each year. And while all Americans are subject to income taxes, three-fourths of Americans, including most low-to-middle income families, pay more in Social Security and Medicare payroll taxes than in income taxes, which the Bush plan does not deal with at all.
- The Bush plan reduces most income tax rates, but the big cuts are at the top of the income ladder, especially the reduction of the top rate from 39.6% to 33%. By contrast, those currently taxed at a 28% rate receive a reduction to 25% -- half the top reduction -- and the 15% tax bracket is *not reduced at all* for married couples with taxable incomes between \$12,000 and \$45,000 (or single people with incomes between \$6,000 and \$32,000). This is not equal treatment even in terms of marginal tax rates.
- Many low-to-middle income taxpayers will see little or nothing in rate reductions. The neediest working Americans -- those with no current federal income tax liability -- will get no help at all, even though they suffer from the heaviest federal payroll tax burden of any citizens. And roughly 12 million additional middle-class taxpayers will see their rate reductions cancelled entirely because they will fall under the alternative minimum tax, which the Bush plan does not properly address.
- Most importantly, the actual tax relief produced by the Bush plan's rate reduction is wildly unequal, with the taxpayers who are already doing extremely well under current tax rates obtaining the lion's share of dollars. According to the Citizens for Tax Justice, the top 1 percent of American families -- who have incomes over \$300,000, will receive 40 percent of the tax relief under the Bush plan: over \$40,000 apiece. The average tax benefit for those in the absolute middle of the income distribution is less than \$500, and poor working people, especially those single-mom waitresses with kids, get nothing. If this is equal treatment, it's the equal treatment of George Orwell's *Animal Farm*, in which everyone is equal, but some are more equal than others.

GOP Claim: High earners deserve the bulk of tax relief because they pay the bulk of taxes.

New Democrat Response: Every working American deserves equal tax relief.

- This GOP claim ignores the simple fact that the lower- and-middle class tax payers who get relatively little in income tax relief are bearing a crushing burden in payroll taxes. Unlike the wealthy, they pay payroll taxes on every dollar they earn. The argument for tax relief proportionate to income tax payments is a direct attack on the principle of progressive taxation, which holds that tax rates should vary according to the ability to pay. Moreover, the top tax bracket has declined significantly since the 1980s, from 60 percent to 39 percent. There is no evidence that progressivity has made it harder for Americans to accumulate wealth and rise into the upper class. Under current tax rates, the United States during the 1990s created the largest upper class, and the first mass upper-middle class, in human history.
- New Democrats are happy and proud about the number of Americans who realized the American dream and rose into the upper class during the Clinton-Gore Administration. But thanks to progressive tax rates, the country was able to combine this private wealth accumulation with the public resources needed to help lift millions of former welfare recipients into productive workers, and lift millions of low-income workers into the middle class, while turning budget deficits into surpluses, and to begin dealing with the debts piled up during the 1980s and the IOUs we face in the near future when the baby boom generation begins to retire. This is no time to break this virtuous cycle, which is truly a win-win proposition for the country and for future generations.
- The key question in designing tax relief should not be some dubious moral judgment about who *deserves* tax relief (there being no particular evidence that the wealthy are better people than those struggling to stay in, or rise into, the middle class). *Equal tax relief means people at the top and the bottom of the income scale should get equal dollar reductions in taxes.* If we truly value work, every American who works should get the same tax relief regardless of income. The Bush plan clearly flunks that test of equity on a grand scale.

GOP Claim: We need the Bush tax plan to stimulate the economy and avoid a recession.

New Democrat Response: The economy is still fundamentally strong, and the Bush tax plan is not designed to strengthen it.

- It's not at all clear the economy is going into a recession -- no thanks to the scare tactics of the Bush Administration -- but it is clear the Bush tax plan is ill-designed as a counter-cyclical tool; could conflict with the Federal Reserve Board's efforts to boost the economy through interest rates; and is dangerous for the long-term growth of the economy.
- Most economists believe the current slowdown is a short-term reaction to the hyper-growth the economy was experiencing in 1998 and 1999 (real economic growth peaked at a stunning and unsustainable 8.3 percent in the fourth quarter of 1999), and to the series of interest rate increases the Fed put into place to cool off that hyper-growth. As Chairman Greenspan made clear in his Senate testimony, the long-term fundamentals of the economy remain strong. For example, productivity growth -- the key to low-inflation, full-employment economic growth -- went up a robust 3.2 percent in the fourth quarter of 2000, during the same period when President-elect Bush and Vice President-elect Cheney began fanning recession fears. Indeed, the decision of Republicans to "scare up a tax cut" by using fears of a recession as a justification for its fiscal priorities contributed to the one real recession threat: declining consumer and investor confidence.
- But even if we are heading into a recession, a tax cut -- and especially a tax cut targeted to high earners rather than middle-class consumers -- is a notoriously clumsy mechanism for stimulating the economy. Chairman Greenspan, in his testimony that was "spun" by Republicans as an endorsement of the Bush tax plan, specifically repudiated the idea that a tax cut could head off a recession -- as did the Administration's own Treasury Secretary, Paul O'Neill, in his Senate confirmation hearing.
- The best way to head off a recession is to let the Fed ease interest rates and restore consumer and investor confidence in the long-term strength of the economy. And the best way to maintain that long-term strength is to retain, not abandon, the formula that created the strong economy of the 1990s: fiscal discipline (including progressive tax rates and spending restraint), open markets, support for technology and innovation, and investments in the skills of the American people.

GOP Claim: If we don't use up the surplus by cutting taxes, Congress will just spend it.

New Democrat Response: Congress should control spending and use the surplus wisely, not tie its hands through regressive tax cuts.

- It's odd to see Republicans who control both Houses of Congress argue that they must cut taxes to keep themselves from irresponsible spending. The way to avoid irresponsible spending is to refuse to irresponsibly spend.
- Besides, the spending which could be avoided through a large, permanent tax cut includes reducing the national debt, modernizing Medicare and Social Security while keeping them solvent, preparing Americans through better education and skills to succeed in the Information Age, keeping America's defenses strong, fighting crime, protecting the environment, and completing welfare reform. Which, specifically, of these priorities is irresponsible, and must thus be avoided by making sure the resources to meet them are instead distributed primarily to high earners? Republicans should answer this question, or stop making this claim. In fact, this "starve the government" theory was abundantly tested in the 1980s, producing a cycle of deficits and debt, and the recession that struck during the earlier Bush Administration. Why go back?