No Tea Parties for Tax Cuts

Even with the 2010 deficit pegged at $843 billion, nobody seems outraged at adding $200 billion by extending Bush’s tax cuts.

By John Maggs

As Congress continues to struggle with a proposal to commit nearly $100 billion a year to overhauling the health care system, it is likely that a far larger commitment will breeze through next year with little dissent.

The tax cuts that President Bush championed in 2001 and 2003 expire at the end of 2010. If Congress lets that happen, taxes on individuals and businesses would rise by an average of $320 billion a year over 10 years. This amount represents an increase of approximately 10 percent in tax revenue. During the 2008 presidential campaign, Barack Obama declared the Bush tax cuts irresponsible, but he is on record favoring the extension of most of them, and Democratic and Republican leaders are likely to support this. Even if Obama succeeds in his promise to block continued tax cuts for high-income earners, Congress is all but certain to approve more than $200 billion a year in tax cuts for middle- and low-income taxpayers, according to congressional aides and tax policy experts.

And despite Democratic promises to offset tax cuts with spending reductions or other tax increases, these sources expect the extension to add more than $200 billion a year to the budget deficit, which is conservatively forecast to be $843 billion in 2010, according to the Congressional Budget Office. House and Senate leaders have deadlocked over a proposal to require offsets, but even if the measure passes, it would exempt action on the expiring Bush tax cuts.

Len Burman, a tax policy expert who teaches at Syracuse University, spent the past decade lamenting the Bush administration’s decision to cut taxes while supporting an ever-growing government. Now he ruefully notes that Obama, who ran for president promising not to raise taxes on 95 percent of Americans, is continuing the

Cost of Extending Bush Tax Cuts

President Obama supports extending the 2001 and 2003 tax cuts, an expensive proposition. Even assuming that some cuts for upper-income earners, businesses, and investors don’t get extended, the price tag is expected to be well over $200 billion a year, based on an average of the Treasury Department’s 10-year revenue estimates.

Provisions of Bush tax cuts (annual cost, in billions)

<table>
<thead>
<tr>
<th>Provision</th>
<th>Cost (billions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Individual marginal income-tax rates</td>
<td>$138.4</td>
</tr>
<tr>
<td>Tax rates on capital gains</td>
<td>$9.4</td>
</tr>
<tr>
<td>Standard deduction for married taxpayers</td>
<td>$5.9</td>
</tr>
<tr>
<td>Personal-exemption phaseout</td>
<td>$3.9</td>
</tr>
<tr>
<td>Other*</td>
<td>$5.5</td>
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<tr>
<td>Total</td>
<td>$264.6</td>
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</tbody>
</table>

*Includes expensing for small business, EITC marriage penalty relief and simplification, and tax incentives for higher education.

SOURCE: Treasury Department’s Green Book
practice. Burman wonders what it will take for Obama and congressional leaders to recognize that taxes for the middle class have to rise to reduce mounting deficits. But, he said, “there is no sign that is going to happen” before the Bush tax cuts get extended.

Congress must act next year because of a procedural decision by Bush in 2001 and 2003 to sidestep the Senate rule that effectively requires the votes of at least 60 of the 100 senators to pass legislation. By using the budget process, Bush’s allies needed merely a simple majority; the trade-off, though, was that the taxes would last until 2011.

At the time, Republicans believed that the Bush cuts would be renewed because no president or congressional leader would want to be blamed for letting taxes go up. They were mostly right. When he was running for president, Obama favored extending most of the Bush tax cuts — those that affected middle- and lower-income people. He said he would allow the tax cuts to expire for individuals earning more than $200,000, and for families earning more than $250,000.

This group is a surprisingly small share of taxpayers—3 million households, or about 1.9 percent of the total number of income-tax returns, according to the nonpartisan Tax Policy Center. (The recession has helped to depress that figure.) Obama’s promise to raise taxes only on this group led the center to estimate that to close its projected $9 trillion budget gap over the next decade, top federal income-tax rates would have to rise to the politically improbable level of 60 percent.

Obama favors individual income-tax cuts after 2010 of $200 billion to $220 billion a year, assuming that he lets upper-income taxes rise. (See chart, opposite.) This amount doesn’t include about $80 billion a year in other popular business tax cuts, such as allowing small businesses to write off new investments as expenses, which Obama is likely to favor.

Since proposing a budget in February, Obama and his advisers have acted as though the Bush tax cuts should be treated as current law after next year, even though they won’t be unless Congress acts. When he proposed a new “pay-as-you-go” law to require Congress to offset further tax cuts or new spending with spending cuts or tax increases, Obama included a provision that would exempt the Bush tax cuts. The idea, said Tom Kahn, staff director of the House Budget Committee, was that the price of extending the Bush cuts would be tough new budget rules for the House and Senate. “Because of the important role statutory pay-go can play in restoring fiscal responsibility, House Democrats are committed to the enactment of statutory pay-go as a condition for extending the 2001 and 2003 tax cuts,” he said.

To some budget analysts, that sounds a little like burning the village to save it. Robertson Williams, a budget scholar at the Urban Institute, said that this strategy would make sense only if Democrats, on principle, refuse to go along with Obama’s extension of the Bush cuts for middle- and low-income earners. “There is no chance of that,” said Williams, who predicted that it would surely lead to an election rout. “There is really no interest in either party for that.”

Meanwhile, after the House passed the pay-go legislation, it stalled in the Senate, and the prospects for enactment are slim, Williams said. Internal House rules that would require offsets for the Bush cuts can be waived with a simple majority, which is what happened when other Obama priorities have come to a vote, Williams noted.

Republicans, according to Burman, aren’t likely to object to Obama’s efforts to extend tax cuts for middle- and lower-income families, even if they fight Obama’s decision to let rates rise for the upper 2 percent, a group that will contain many small-business owners.

Also, Obama has already committed the $60 million a year in high-income tax increases several times over—for health care and for offsetting the costs of a carbon tax, if Congress ever agrees to one, as well as for other initiatives.

When it came time to find offsets for other tax cuts in recent years, Congress and Bush agreed to short-term fixes—“patches,” as they are called. Similarly, Obama is expected to back a short-term fix that would keep constant the number of people who pay a higher tax rate under the so-called alternative minimum tax. A one-year AMT patch would cost $70 billion in 2011, as opposed to a permanent fix that would carry a 10-year price tag of nearly $600 billion.

Likewise, congressional tax writers are talking about a short-term compromise for the estate tax, which drops to zero in 2010 but snaps back to 50 percent in 2011 for estates larger than $1 million.

All of this patching has led to speculation that Obama might resort to a one- or two-year patch for the income-tax code, but Williams says that this probably won’t be necessary. “There is so much support for [extending these cuts] even if there is no serious attempt to pay for it.”

Burman wonders whether the populace will ever get exercised about what he sees as unsustainable tax cuts, compared with the way that conservatives have stoked outrage about higher spending. “The effect is the same. You’ve got to pay for it eventually.” Burman’s disappointment with the political budgeting process has persuaded him that the time has come to talk about “catastrophic budget failure,” where out-of-control deficits become a serious drag on the economy. He is working on an economic model showing how such a budget impasse can lead to disastrously high interest rates and a vicious spiral of slow growth and crushing debt.