

CITY A.M.

The progressives are cheating in the argument against Donald Trump's tax cuts

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Has anyone noticed how “tax cuts for the rich” has become a moniker for all and every income tax cut?

When the Conservatives dropped the top rate of income tax from 50p to 45p, that was predictably lambasted as a tax cut for the rich. George Osborne's promise to raise the starting threshold for the 40p rate? Tax cut for the rich.

Even proposing to raise the personal allowance further was described by progressive economists in the 2015 election as a tax cut for the better off.

So I've been getting *deja vu* here in the US listening to the debate about Donald Trump's self-proclaimed “giant, beautiful, massive... tax cut”. The President wants to double the “standard deduction” for the income tax (the equivalent to personal allowance), and compress the number of income tax rates from seven to three, while lowering them.

This will be financed in part by eliminating a whole bunch of other income tax exemptions and allowances. And his opponents are already presenting this package as “a giveaway to the wealthy”.

As with all misleading statements, there is a grain of truth here. In pure cash terms, richer households look as if they would benefit from the income tax package more than poorer ones.

But that is a fig leaf for a whole bunch of chicanery which misleads on the broader arguments for tax cuts like this – and which you should be aware of next time the debate arises in Britain.

First, economists believe that efforts to lower marginal income tax rates and eliminate deductions can raise the level of GDP. Tax reform can improve incentives to work and produce, simplify filing returns, and lead to less tax-induced distortion of the economy.

But this improved efficiency won't show up on any assessment that looks solely at the static impact of tax changes on an individual's finances. As such, it is misleading to look at who is left “better” or “worse” off through the prism of individual circumstances, because doing so ignores these growth effects.

In the US, analysis like this also ignores the effect of Trump's corporate income tax cut, which more and more academic analyses suggest will raise productivity and wages in time.

Second, analysis from the US Treasury Department shows that the bottom 50 per cent of households, on average, do not pay net income taxes. Meanwhile, the top 20 per cent of

households pay 95 per cent of federal income tax receipts, with the top 0.1 per cent of taxpayers alone paying 24 per cent.

It is highly unsurprising that, if marginal tax rates are cut, the people who will benefit directly are those who actually pay the tax.

Opponents to rate cuts on these grounds are criticising tax changes on the basis that they do not help people who are already completely exempt from them. This is bizarre. It effectively implies that they are against all tax cuts, of any sort.

Third, left-leaning policy analysts often get slippery when describing whether a proposed tax change is “progressive” or “regressive”.

Usually, a policy is described as progressive if it increases the relative disposable income of poorer households by a larger proportion than richer ones. But when things like the personal allowance are raised, analysts move the goalposts by looking at the absolute cash changes instead.

This, of course, makes it look as though people on upper incomes benefit more, rather than the tax cuts being proportionately more beneficial to those on middle incomes.

There are two lessons here for Republicans and Conservatives.

Most obviously, tax reform is hard. Unless it is complemented by other tax changes elsewhere that make everyone financially better off in cash terms, it leads to strident opposition from the losers. But cutting taxes for all will raise deficits, merely delaying subsequent future tax rises, unless government spending can be sustainably cut.

Perhaps more importantly, Republicans and Conservatives should leave the class struggle to the other parties when they make the case for tax cuts.

Progressive analysts have effectively shown that they do not believe income taxes should ever be cut. Given that poorer households tend to pay no to little income tax, the focus on messaging for income tax changes should be about how they would support durable economic growth for the nation as a whole.

In Trump’s case, selling income tax cuts as middle class relief when the middle class pay so little in income tax in the first place is a fool’s errand. Instead, his government should focus on why eliminating deductions and lowering rates will improve incentives and grow the economy.

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