

The Upside of Playing Fiscal Chicken

Progressives can use the budget crisis to create a fairer tax system.

David Callahan | June 22, 2011 | web only

The budget hysteria that now grips Washington bodes ill for the economy by foreclosing new and badly needed stimulus. Yet the upside is that it also creates a historic opportunity to revamp federal spending in ways that foster greater national equity.

Big reforms are most likely to happen during periods of crisis. Conservatives have famously appreciated this truth with a “starve the beast” strategy that aims to first cut revenues and then use resulting budget crunches to downsize government. That playbook guides them today at both the federal and state level.

Progressives need their own strategy for exploiting the fiscal crisis. In truth, there is a whole lot to hate about federal budget priorities, but reform is tough in normal times. So while progressives should keep fighting any and all spending cuts until the economy rebounds, we also have a rare chance to push big changes in where federal dollars go and who gets what.

First on the list of progressive wish-list of cuts is defense spending. With Obama’s announcement Wednesday of a troop drawdown in Afghanistan, an era of war is nearing a close. The trick now is to leverage both this shift and the fiscal crisis to make truly deep defense cuts, including ones that have nothing to do with the recent wars.

There may well be enough votes in Congress to pull this off. The libertarian quest to downsize the Pentagon along with the rest of government - a position long espoused by the CATO Institute - has now crept firmly into the mainstream of the Republican Party. While Paul Ryan’s budget envisioned modest growth in defense spending, House Whip Eric Cantor said earlier this year about defense cuts that “Everything’s got to be on the table” and some prominent Republicans, like Sen. Tom Coburn, have campaigned loudly for defense cuts to help reduce the deficit.

Meanwhile, the budget squeeze provides cover to Democrats who are skittish about cutting defense. Barney Frank - who has long called for deep Pentagon cuts - has found new allies for his cause on the Hill by framing such cuts as a fiscal imperative. Last fall, he got 55 members of Congress, including Ron Paul, to sign a letter to the President’s fiscal commission saying that any deficit reduction plan must include steep cuts to defense.

Attacking corporate tax breaks should be the next top priority for progressive budget reformers. And here, too, once-impregnable political barriers are weakening fast in a climate of crisis.

The Joint Committee on Taxation estimates that corporations will receive about \$375 billion in tax breaks over the next five years. Many of these breaks have been untouchable because they go to industries with allies in both political parties. But the deficit debate has put corporate tax reform on the political agenda for the first time since the 1980s. Indeed, the President's fiscal commission called for eliminating all corporate tax breaks - 75 in total by its count - while slightly lowering the top corporate tax rate (which nobody pays anyway). A similar reform in 1986 boosted overall revenues from corporate taxes by a third.

Whacking tax perks for big business has more bipartisan support than you might think and it seems to be growing by the day. Many Republicans now understand that the only way to raise revenues without raising tax rates is to close loopholes, while libertarians have long despised "corporate welfare." Democrats, in turn, can show they are fiscally responsible and tough on business at the same time. (Lowering the top rate also allows them to claim they are helping U.S. companies become more internationally competitive.) No wonder the Obama White House is said to be working up a corporate tax reform plan.

Also high on the budget hit list should be the fat tax breaks for individuals, which cost hundreds of billions of dollars a year and mostly flow to wealthier households. Few politicians have dared to target this hidden welfare state - which includes deductions for home mortgage interest, retirement savings, and employer-based healthcare. That has changed, and budget plans on both the left and the right call for reining in these once-sacrosanct subsidies. The best plans would limit itemized deductions and restructure tax subsidies, like the mortgage interest deduction, to favor lower income households. This has been a dream of many progressives for years. But only now is it being seriously discussed.

There are other worthy targets: cutting agricultural subsidies, trimming foreign military aid, defunding the failed war on drugs, and more. It is folly to cut any spending during a downturn. But, sooner or later, deficit reduction must happen, and progressives need a strategy beyond just raising taxes. The good news is that equity-minded reformers have been waiting years - and in some cases decades - to slaughter any number of sacred cows. Now is the chance.