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Herman Cain's 999 Plan: Will It Work? Experts Speak Out

Analysis

By Maggie Astor | October 13, 2011 12:00 PM EDT

Herman Cain has been making waves with his catchy "9-9-9" tax plan -- but is it good economic policy? The International Business Times spoke with experts at several economic think tanks to find out.

Herman Cain has made waves with his "9-9-9" tax plan. What are the tax plan's strengths and weaknesses for U.S. tax filers?

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A Simple but Controversial Plan

The basic structure of the plan is simple. It would involve three separate taxes: a 9 percent personal income tax, a 9 percent corporate tax and a 9 percent national sales tax. Eventually, if Cain had his way, he would replace all of that with a single "consumption tax," which would tax purchases rather than income. The national sales tax included in the 9-9-9 plan is meant as a step in that direction.

The 9-9-9 plan stole the show at the Republican presidential candidates' debate at Dartmouth College on Tuesday, but it has been widely panned both by Democrats and by Cain's Republican opponents.

Democrats call the plan unfair for reducing taxes on the wealthy while increasing them for many low-income Americans. Republicans have made a litany of criticisms: Future presidents could increase three tax streams rather than one. It oversimplifies the complex problem of improving the tax code. Or, more pragmatically, it could never pass Congress anyway, so what's the point?

Side I: Good Economic Policy

Support for the 9-9-9 plan focuses less on how it will affect the distribution of wealth, and more on how it will affect the economy as a whole. On a macroeconomic scale, Cain argues, the plan has tremendous potential to strengthen the economy and create jobs, because it would lower taxes on businesses, giving them an incentive to start hiring.

Daniel Mitchell, a senior fellow with the Cato Institute, a libertarian think tank, said the principles of Cain's plan were solid. "As a matter of economic policy, it's a very good idea: lower marginal tax rates, less double taxation on savings and investments, and elimination of corrupt and inefficient loopholes," he told IBTimes. "Those are all things that public finance economists have long recognized are important."

The 9-9-9 plan has drawbacks "relative to an ideal tax system," but "relative to our current system, you'd have to say on balance it's much better," Will McBride, an economist for The Tax Foundation, a nonpartisan tax research group based in Washington, said. "It reduces taxes on saving and investment, and that's where economic growth comes from, basically. That is its primary benefit, and then, of course, it simplifies the tax code tremendously."

Supporters of the plan have addressed some of the main criticisms of it, such as the fear -- raised most recently by Michele Bachmann at Tuesday's debate -- that future presidents would inevitably raise the 9 percent rate, creating, for example, a 15-15-15 plan.

"It's certainly a risk, but that's the history of taxation," McBride said. "Sure, there's always going to be that pressure with any tax, but we have to compare to the current system, and it's a big improvement over the current system. It's a big reduction in the top tax rate and a flat tax on personal and corporate income. Those are very good things for long-term growth. Even if we eventually push the rate up to 15 percent, that's a drastic decrease from the current system," in which the corporate tax -- though not personal income tax -- is 35 percent.

And, in response to Mitt Romney's jab at Tuesday's debate that the 9-9-9 plan oversimplified the complex task of fixing the economy, Mitchell said, "I think the plan is strong because of its simplicity." There is more to fixing the economy than tax reform, of course, but "one of the reasons I think Cain is attracting so much support is because he's willing to come up with a bold plan," he said.

Kevin Hassett, the director of economic policy studies at the American Enterprise Institute, a conservative think tank, agreed. "This is a far more sophisticated plan than one might have expected, given that he is not a person that has been inside politics his whole life," Hassett told USA Today. "The Cain plan is really solid. The only criticism one could make is it's too bold or something like that."

Side II: Bad Economic Policy

Critics of the 9-9-9 plan say that its negative microeconomic effects -- that is, the potential burden on low-income Americans -- would outweigh any benefits for the economy as a whole.

On paper, as Cain said at a debate in September, the plan treats everyone the same. But in practice, it taxes low-income Americans at a higher rate than their affluent counterparts, because how much a person would pay under the national sales tax, and how much they would save from the eliminated taxes on savings and investments, depends on how much of their income they spend, save and invest. In other words, the taxes take a disproportionate share of a low-income Americans' disposable income.

Consider two people: one who earns $30,000 a year and spends all of it by necessity, and one who earns $500,000, spends $100,000 of it and saves or invests the remainder. Under Cain's plan, the first person would pay an 18 percent tax on that $30,000: 9 percent in income tax and 9 percent in sales tax. But the second person would only pay about 11 percent in taxes on their $500,000 income: 9 percent in income tax and 1.8 percent in sales tax, since only 20 percent of their income would be subject to the sales tax, and savings and investments wouldn't be taxed at all.

"Businesses will tax all wages, because wages don't seem to be deductible," Roberton Williams, a senior fellow at the nonpartisan Urban Institute, told IBTimes. "People, when they receive those wages, will pay another 9 percent tax on it, and then when they spend it, they'll pay another 9 percent."

That is a 27 percent effective tax on wages -- but a zero percent tax on income from investments and capital gains.

"The obvious winners are the big guys who get a lot of their income from capital gains, and capital gains would not be taxed at all," Williams said. But the majority of Americans who make their living from wages, not capital gains, would be hammered under the 9-9-9 plan.

"It is hard to fathom a hedge fund manager paying a higher effective tax rate than a secretary under Mr. Cain's plan," Andrew Fieldhouse, a budget policy analyst at the Economic Policy Institute, wrote recently. "Financiers would be able to receive all of their compensation as tax-free investment income, and ... the windfall from eliminating investment income taxes would accrue to the top 1 percent of earners, who will pay over 70 percent of all capital gains and dividends taxes in 2011."

The 9-9-9 plan "only makes sense if you believe that the problem with the current tax code is that low- and middle-income households have it way too good, and they should give more of their income to those poor Americans making more than half a million dollars a year," Fieldhouse wrote.

Williams dismissed the idea that, as President Ronald Reagan famously argued, the economic benefits of cutting taxes for the wealthy would "trickle down" to middle-class and working-class Americans. "Only if you have very, very, very large macroeconomic gains would you get the trickle-down [effect], and in our history of that, there's not much trickle down," he said.

In a separate critique, Mitchell, the Cato Institute fellow -- who did praise many of the principles of the 9-9-9 plan -- expressed concern about some of the particulars, especially the idea of having three separate tax streams.

"Politicians have done a really bad job with one source of revenue, the personal income tax. Imagine giving them three sources of revenue," he told IBTimes. "That, to me, would be very dangerous, because we see from the experience in Europe that politicians wouldn't keep it 9-9-9. It would go to 19-19-19, or 29-29-29."

What do you think? Would Herman Cain's 9-9-9 tax plan be a good economic policy?