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September 26, 2010

The Reagan Tax Cuts and Revenues

Wall Street Journal op-ed, **Tax Cuts and Revenue: What We Learned in the 1980s**, by **Richard W. Rahn** (Cato Institute):

> *Supply-siders never argued that all tax cuts pay for themselves. But the evidence is clear that lower rates on high earners do produce more revenue over time.*
>
> There will be no gain in long-term tax revenue from increasing tax rates on those making more than $200,000 per year, despite claims by President Obama's Office of Management and Budget, and the Congressional Joint Committee on Taxation, which studied the administration's tax proposals. The current debate over the expiring Bush tax cuts is a replay of the debate about the Reagan tax-rate reductions of three decades ago. We know the outcome of that debate. Lower tax rates, particularly on labor and capital, lead to higher levels of employment and economic growth.
>
> Those of us who argued in the late 1970s and early 1980s for lower tax rates were often characterized as "radical supply-siders" and criticized for claiming that all tax-rate reductions lead to higher tax revenues. This was untrue; none of the principal advocates of Reagan's 1981 tax cuts made this claim.
>
> The Reagan tax cuts reduced rates for all income classes, even though it was well understood that cutting the lower rates would result in substantial revenue losses. Low tax rates (below 20%) do not cause much of a disincentive for working, saving or investing, and hence there is little supply-side effect. We did argue, however, that reducing the high marginal rates (up to 70% on high-income earners) would cause little, if any, revenue loss, because of the large, positive supply-side effects. Were we right?
>
> Since most of the Reagan tax cuts applied to lower- and middle-income earners, there was

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> close to a dollar lost in tax revenue for each "dollar" of tax cut for these groups. Still, CBO figures show that total tax revenue only fell from 19.2% of gross domestic product (GDP) in 1982, before most of Reagan's tax-rate reductions were put in place, to 18.4% of GDP in 1989, the year he left office. This happened because the U.S. economy grew by more than one-third in real terms (34.3%), much faster than the 24.3% rate expected even by economists within the Reagan administration. Thus, by the time President Reagan left office, the economy was generating more tax revenue at a maximum 28% rate than many on the left forecast it to generate at a maximum 70% rate.

Bruce Bartlett notes that the op-ed ignore the **eleven major tax increases** signed into law by President Reagan in 1982-88:

Tax Increases	Billions
Tax Equity and Fiscal Responsibility Act of 1982	57.3
Highway Revenue Act of 1982	4.9
Social Security Amendments of 1983	24.6
Railroad Retirement Revenue Act of 1983	1.2
Deficit Reduction Act of 1984	25.4
Consolidated Omnibus Budget Reconciliation Act of 1985	2.9
Omnibus Budget Reconciliation Act of 1985	2.4
Superfund Amendments and Reauthorization Act of 1986	0.6
Continuing Resolution for 1987	2.8
Omnibus Budget Reconciliation Act of 1987	8.6
Continuing Resolution for 1988	2.0
Total Cumulative Tax Increases	**132.7**

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