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Overheated Rhetoric on Tax Reform

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Even in a town where overheated rhetoric comes as naturally as breathing, the reaction to the Senate version of the Republican tax bill has been somewhat . . . unhinged.

“Armageddon,” House Minority Leader Nancy Pelosi warned, calling it “the worst bill in the history of Congress,” as it apparently surpasses the Alien-Sedition Acts, the Fugitive Slave Act, the Indian Removal Act, Prohibition, and the Gulf of Tonken Resolution, among others. Liberal journalist Kurt Eichenwald agreed that “America died tonight,” urging, “Millenials: move away if you can. USA is over. We killed it.” And disgruntled former Republican strategist Bruce Bartlett decried the bill for “raping” middle America.

Maybe not.

Start with the debt. It is wonderful that Democrats, who previously considered the national debt somewhere below lawn mold on their list of priorities, have now been reborn as deficit hawks. And there is reason to be concerned that the tax bill will add to the debt. But to keep things in perspective: Under current law, the federal government is expected to collect $43 trillion in taxes over the next ten years, while spending $53 trillion. That will increase the national debt to $30 trillion by 2028. If this tax bill passes, the federal government will collect $42 trillion in taxes over the next ten years, while spending $53 trillion. That will increase the national debt to $31 trillion by 2028.

Worse? Absolutely, like a drunk asking for one more drink. But it would be nice if everyone got this worked up about the first $30 trillion.

In fact, even after this tax cut, the federal government will be collecting 17.6 percent of GDP in taxes, more than the post-war average of 17.4 percent. The problem is that we will be spending 22.2 percent of GDP, considerably more than the 20.3 percent that we’ve averaged since World War II. We don’t tax too little — we spend too much.

So, yes, as many Democrats fear, we will have to reduce future spending and reform entitlements. But we would have to do that even without this tax cut. The danger is that Republicans, having done the fun stuff like tax cuts, will now shirk the hard work of cutting spending.

Opponents of the tax bill also portray it as a giveaway to the rich. But even after passing this bill, the United States will have a far more progressive federal tax structure than most of the

European countries so admired by social democrats. (European countries have much higher total taxes, but they rely heavily on a regressive value-added tax for much of that revenue.) Currently, Americans earning $1 million or more pay 29 percent of federal income taxes. Those earning less than $50,000 pay about 1 percent of federal income taxes. As a result of this tax bill, those millionaires will now pay 31 percent of federal taxes, while those earning less than $50,000 will still pay less than 1 percent. True, those making between $500,000 and $1 million will see their share of federal income taxes decline, but the bill is far more progressive than portrayed.

That isn't to say there are no reasons to be less than thrilled with the bill. Concerns over increasing the debt are real, given Republican reluctance to cut spending. Yes, this bill will boost economic growth, but counting on the "growth fairy" to bail us out is a perilous strategy.

Moreover, much of the "reform" portion of tax reform has been abandoned. Tax reformers have long championed the idea of trading the elimination of loopholes and deductions, which distort economic activity and make tax-filing needlessly complicated, for lower rates. After all, the purpose of the tax code should be to raise revenue, not to micromanage society. The tax bill does some of this, but some of the biggest — and least justifiable — tax breaks remain, including the mortgage-interest deduction, the exclusion for employer-provided health insurance, and the deduction for charitable contributions. These are tax breaks that primarily benefit wealthier taxpayers.

Worse, as is inevitable with bills that rely on last-minute vote-trading, the bill is also stuffed with new special-interest provisions, including tax breaks for the alcoholic-beverage industry, cruise ships that dock in Alaska, car dealerships, and citrus farmers, among others. Ultimately, we should recall that taxes, even if a necessary evil, reduce people's choices and autonomy.

On the other hand, corporate-tax reform is something that even President Obama supported. Reducing the corporate rate will go a long way toward both making U.S. businesses more competitive and reducing the incentives for corporate inversions. (The U.S. will still have a higher statutory rate than Ireland, Switzerland, and the United Kingdom, among others.) More important, the bill would move us from a unitary to a territorial tax system like those in virtually every other country in the world. This will encourage businesses to invest their money here rather than keep it parked abroad.

And the reduction in individual tax rates, together with the doubling of the standard deduction and an increased child tax credit, will put more money back in people's pockets.

There will undoubtedly be winners and losers under this bill, as there would be with any tax reform. If you don't itemize, you will generally be much better off, while there are more mixed outcomes for itemizers. Only 6 percent of tax returns reporting under $25,000 in income had itemized deductions in 2013. On the other hand, 93.5 percent of tax returns with over $200,000 in income had itemized deductions.

For example, there has been much wailing and gnashing of teeth over the trimming of the deduction for state and local taxes. But according to the Tax Foundation, only 10 percent of tax filers with incomes less than $50,000 claimed the SALT deduction in 2014, compared with about 81 percent of tax filers earning more than $100,000.

Ultimately, we should recall that taxes, even if a necessary evil, reduce people's choices and autonomy. Every dollar that the federal government takes from people to spend the way it wants is one less dollar that individuals have to spend the way that they want. As Frédéric Bastiat put it in his parable of the broken window: If the shopkeeper with the broken window hadn't had to pay to replace it, "he would, perhaps, have replaced his old shoes or added another book to his library." Or to put it in today's context, he might have purchased health care, saved for his retirement, or donated to charity. He might have started a business or hired workers. Or he might have spent it entirely on frivolities. Whatever he might have done, he is now deprived of that choice.

Giving some of that money back falls a little short of Armageddon.

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