

the guardian

Two questions Trump must answer if he wants to drain the tax swamp

Trump has promised a 'phenomenal' plan to reform America's labyrinthine tax system, but it's a feat no president has achieved since Reagan

Dominic Rushe

April 16, 2017

“Historic”, “massive”, “phenomenal”. Donald Trump has pulled out all his increasingly tired superlatives to describe his plans for reforming the byzantine and bonkers US tax system. Well, good luck with that.

As he ponders his next move at Mar-a-Largo this Easter weekend, Trump will do well to remember that tax reform has a way of leaving a president with egg on his face. It's not without reason that no commander-in-chief has achieved it since Ronald Reagan, in 1986.

Reagan, wildly popular, didn't pass tax reform until his second term and it took 10 tense months to pull it off. Trump, who is wildly unpopular and has yet to even appoint most of the people who would do the heavy lifting on tax reform, wants it done by summer. Say what you like about Trump, he doesn't lack ambition.

When he accepted the Democratic presidential nomination in 1976, Jimmy Carter (the anti-Trump) called the US tax code “a disgrace to the human race”.

“All my life I have heard promises about tax reform,” he said, “but it never quite happens. With your help, we are finally going to make it happen. And you can depend on it.”

Forty years on, the federal tax code covers close to 75,000 pages, 187 times longer than it was a century ago.

The main problem, according to Cato Institute senior fellow Michael Tanner, is that tax reform lies at the heart of Washington's quagmire. “The tax code isn't just part of the Washington swamp,” Tanner wrote recently. “It *is* the swamp.”

But to hear it from the Trump camp, tax is easy. After the failure to “repeal and replace” Obamacare, treasury secretary Steve Mnuchin recently told a group of financial journalists: “Healthcare is a very, very complicated issue. In a way, [tax reform is] a lot simpler. It really is.”

Few beyond the Trumposphere would agree. But don’t worry, dear reader. As Richard Rubin, the Wall Street Journal’s tax wonk, recently pointed out, while tax policy is labyrinthine, tax reform stories are actually simple. In fact, there are only four: “It’s hard”, “What does X mean for reform?”, “What does reform mean for X?”, “Check out weird tax thing”.

When it comes to taxes, though, we’re all in favor of simplification. Right? So let’s cut Rubin’s Rules down to two: “Why is it hard?” and “What does X mean for reform?” Those are the two questions that, in the weeks to come, will keep the president padding through the corridors of power, into the wee small hours.

Why is it hard?

Advertisement

The White House needs a big win after its humiliating defeat over healthcare reform. In principle, everyone agrees that the US needs tax reform. The Tax Foundation’s last survey of tax competitiveness ranked the US a dismal 31st out of the 35 Organisation for Economic Co-operation and Development (OECD) member countries it measures. (If you really want simple taxes, move to Estonia or New Zealand). While everyone in Congress would like to see that score improve, no one agrees how.

Trump’s plan is to cut taxes on middle-class Americans, reduce business taxes and simplify the tax code. Three tax bands will replace the current seven, with the threshold for paying tax rising and the top rate falling.

Tax cuts that add to the national debt – that are not “revenue neutral” – have to expire after 10 years. Tax reform is more ambitious and Trump must balance the books in order to get it passed. In order to do so he has proposed cutting loopholes for the super-rich and corporations – including, perhaps, the “carried interest” loophole used by billionaire hedge funders. A one-off 10% tax on repatriating the \$2.5tn corporations have sitting in cash sitting overseas would pay for some cuts, as would a controversial “border adjustment” tax on imported goods.

But even if Trump can get his pluses and minuses to balance out, the plan has to pass Congress. Democrats, hoping for a second major Trump fail, won’t give the president any votes, not least because an analysis of Trump’s plan by the nonpartisan Tax Policy Center concluded it would give rich people the biggest tax cuts, with about half of the benefits going to the top 1%.

Among Republicans too, tax reform is a knotty issue. The proposed border tax has reportedly managed the unusual feat of uniting Paul Ryan, the House speaker, and Stephen Bannon, Trump’s top strategist. The tax would raise \$1tn in revenue over 10 years, paying for other cuts and incentivizing US manufacturing (or so Trump argues) over overseas production. It also contains the word “border”, which should appeal to his isolationist base.

But treasury secretary Mnuchin and economic adviser Gary Cohn are against the tax, as are business leaders who argue it will effectively translate into a tax on consumers as retailers and others pass costs on to buyers. Even for Republicans, tax cuts for the rich paid for by price hikes at Walmart might prove a tough sell as the midterm elections approach.

Then there are the special interest groups and their pet politicians who will be fighting to keep their tax breaks while lobbying for new ones they'd like. Rewriting 75,000 pages of tax code will create a feeding frenzy of opportunity.

“Tax cuts are easy, tax reform is hard,” says Maya MacGuineas, president of the Committee for a Responsible Federal Budget, a bipartisan and nonprofit organization that studies the impact of fiscal policy.

Even with the national debt now marching its way to \$20tn (a credit card debt of more than \$61,000 for every US citizen) MacGuineas said she saw little sign that politicians were making the tough choices needed to pass true tax reform.

“We are in a period of giveaways and politicians are reluctant to talk about hard choices,” she said.

What does X mean for reform?

Where X equals the Affordable Care Act, the answer is everything. Politically, Trump's failure to make good on his promise to repeal and replace Barack Obama's signature healthcare policy makes passing any new and major legislation both more important and more difficult.

The rightwing Freedom Caucus played chicken with Trump's health plans and Trump was the first to blink. His threats of retaliation look about as convincing as those of an overweight school bully who finds his “victim” has a blackbelt in jiu-jitsu. The Freedom Caucus now knows it can hold out for the tax policies it likes and will likely derail any plan that appeases the moderates.

Financially, the failure to repeal Obamacare also gives Trump a tax headache. Trumpcare (aka the American Health Care Act) could have cost 24 million Americans their health insurance, according to the Congressional Budget Office, while handing \$144bn in tax cuts over the next decade to those with incomes of \$1m or more by axing new taxes created under Obamacare, according to the non-partisan Joint Committee on Taxation.

It would also have shaved \$337bn off the federal budget over the next decade.

If Trump's tax plans are to remain revenue neutral, and they will have to placate the Republican's deficit hawks, Trump will have to find other ways to make up that saving. He will also be under pressure to shoehorn those tax breaks back in to the tax reform package.

He has pledged to go back for a second run at healthcare but to do so while tackling tax reform would risk creating a tsunami of wonk that could drown an administration that so far has shown little patience for the details.

The net result of this swamp-a-thon? The grand plan will collapse and Republicans will eventually pass a 10-year tax cut for the rich, said Cato's Tanner.

"They are not going to just come out and say they want tax cuts for the rich," he said. "Tax reform sounds so much more noble."

But in the end?

"I don't think they really care about paying for those tax cuts."