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PLATTE CHAT

To Fix Deficit, Tax Man Must Knock on Many Doors

As appeared in the April 12, 2010 edition of the Wall Street Journal

John D. McKinnon

Most Americans believe taxes are heading higher. The big questions are by how much, when, and on whom?

Unless Washington summons the nerve to drastically cut spending, taxes are likely to rise a lot, soon and probably hit many ordinary Americans, but especially the well-to-do.

A January study by the nonpartisan Tax Policy Center provides the worst-case scenario. It found that to reduce the federal budget deficit to a sustainable 3% of gross domestic product, the government would have to find an average of about half a trillion dollars each year in new revenue (or spending cuts). That's roughly how much the federal government spends now on the giant Medicare program.

To cover that amount through tax increases on the top two brackets—roughly, families with more than \$209,000 in taxable income—top rates would have to go

people. To make the process easier, the Platte Institute has assembled a list of links which allow you to submit a letter to the editor to nearly all Nebraska newspapers. Simply [CLICK HERE](#) for a listing of the newspapers and follow the appropriate link to submit your letter.

Contact Us

If you would like to contact someone at the Platte Institute, you are always welcome to give us a call, drop us an email or stop by the office. Our telephone number is 402.452.3737. We are located at 10050 Regency Circle – Suite 120 – in Omaha. Below is a list of staff email address:

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from the current 33% and 35% to 72.4% and 76.8%, the study found.

Citing those findings, Sen. Orrin Hatch (R., Utah) says such steep rate increases can't provide the answer.

"They would cripple economic growth," says Mr. Hatch, who's in line to become the top Republican on the Senate Finance Committee next year. Mr. Hatch, like other Republican lawmakers, insists spending reductions are the only way to address deficits.

But if Congress and the White House ultimately decide to go with a mix of spending cuts and tax increases—as seems more likely for now—lawmakers probably would seek to spread the tax pain around.

One idea gaining currency is broadening the tax base by limiting individuals' deductions and closing what the Obama administration terms corporate tax loopholes.

Another plan getting attention is adding new taxes on consumption, such as a value-added tax, widely used in other countries. The VAT could be paired with an overhaul of the U.S. corporate tax, to focus it only on income generated inside the U.S., and make it more like other countries.

Each idea faces political challenges. The real-estate industry, for example, would fiercely resist limiting the huge mortgage-interest deduction—an idea that the Obama administration already has floated with its proposal to limit the value of top earners' itemized deductions to 28%, from 33% and 35%.

Corporations, meanwhile, worry that taking away their tax breaks will make them less competitive with overseas rivals, and encourage more cross-border takeovers of American companies. Big retailers vehemently oppose a broad consumption tax, because it would limit spending.

Still, the possible elements of an eventual budget deal

are on the table. At this point, rate increases, especially on higher-income earners, appear likely, and further limits on some types of deductions are very possible, as evidenced by the health-care legislation's modest curbs on tax breaks for employer-sponsored health plans.

And even some conservative economists concede that consumption taxes, such as on energy, are among the least harmful sorts of taxes under consideration.

So when will taxes go up? It's already started. The just-passed health-care bill contained a couple of increases in Medicare payroll taxes for higher-income earners. Deloitte experts say those provisions would cost about \$2,250 for a family with income of \$500,000.

Congress might raise taxes on the well-heeled still further this year. President Barack Obama has proposed allowing the Bush-era tax cuts to expire for families making more than \$250,000, a change that would return their top rates to 39.6% and 36% lift their capital-gains rate and trim some deductions.

Given the still-precarious economy, the coming election and the looming need for a broader look at spending and taxes, it's possible Congress will decide to simply extend some or all the Bush tax cuts for a year or two. And prospects are growing that Congress will punt on the tough decisions until after November.

But sometime soon after the election, lawmakers will try for a broad bipartisan deal on taxes and spending, perhaps aided by a recently formed fiscal commission.

At least some Democrats remain optimistic, despite Republicans' resistance to new taxes and their own members' reluctance to cut entitlements.

When Rep. Richard Neal (D., Mass.) joined the House in 1989, deficits were so deep that "many said we could not fix that issue, that it was a hopeless cause," he says. "But [President George H.W.] Bush once and Clinton twice, with spending and revenues, addressed the issue

four-square."

Mr. Neal, the chairman of a key House Ways and Means subcommittee, held a hearing recently that explored many of the tax options, such as base-broadening and consumption taxes.

Mr. Obama might want to postpone the day of budget reckoning until after the 2012 election. Some economists worry that the U.S. won't have that much time, however, and that the financial markets suddenly might lose confidence in U.S. ability to repay its debt.

As for who will wind up paying higher taxes, it's a safe bet that the well-to-do will bear the lion's share, particularly if Mr. Obama has his way.

The president "is not proposing to cut the deficit at the expense of middle-class families," says White House spokeswoman Amy Brundage.

Republicans complain that already, almost half of American households pay no income tax, a trend that Rep. Pat Tiberi (R., Ohio) worries will continue. Still, even some Democrats appear to be questioning Mr. Obama's pledge to protect all families making less than \$250,000.

The "notion that somehow this is going to be accomplished merely by taxing 1% of the population or 2% of the population or 5% of the population is...a fantasy," Rep. Earl Blumenauer (D., Ore.), said at the recent hearing.

Like a number of Democrats, Mr. Blumenauer said he's "intrigued" with the consumption-tax idea. Tax experts say consumption taxes are regressive, because lower-income people tend to spend more of their income. But a consumption tax could be designed with offsetting breaks for lower-income Americans, to shield them from its impacts.

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