ASSESSING THE BUSH ADMINISTRATION'S TAX AGENDA: A COMMENTARY ON GALE AND ORSZAG'S *AN ECONOMIC ASSESSMENT OF TAX POLICY IN THE BUSH ADMINISTRATION, 2001–2004*

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Abstract: In response to Doctors William G. Gale and Peter R. Orszag's Article, this Commentary argues that because the economic and social consequences of making permanent the 2001 and 2003 tax cuts would be disastrous, they would need to be paid for through some form of tax increase or spending decrease. This Commentary argues that reductions in tax expenditures are equivalent to reductions in direct spending and thus should be considered together with them for deficit reduction purposes. This Commentary next notes that the Alternative Minimum Tax has become, for no clear congressional purpose, a tax on the middle class. Finally, this Commentary argues that the negative impact of the 2001 and 2003 tax cuts on future generations is morally unacceptable.

INTRODUCTION

Doctors William G. Gale and Peter R. Orszag, in *An Economic Assessment of Tax Policy in the Bush Administration, 2001–2004*, present a powerful and convincing critique of the disastrous economic and, I would add, social consequences that could flow from making permanent the tax cuts enacted in 2001 and 2003.[1] This Commentary focuses on three aspects of their Article, in particular. First, this Commentary addresses the impact of the tax cuts on the budget and notes the possibility of reducing tax expenditures to help pay for the cuts.[2] Second, this Commentary addresses the increasing impact of the alternative minimum tax (the "AMT") on middle-class taxpayers.[3] Fi-

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[1] *See generally* William G. Gale & Peter R. Orszag, *An Economic Assessment of Tax Policy in the Bush Administration, 2001–2004*, 45 B.C. L. REV. 1157 (2004).

[2] *See infra* Part I.

[3] *See infra* Part II.

nally, this Commentary notes the impact of the cuts on future generations of taxpayers.[4]

I. Budget Impact and Tax Expenditures

First, as the Doctors Gale and Orszag note, the tax cuts will put enormous pressure on U.S. policy options. They assert that the individual income and estate tax cuts, if made permanent, must be financed in some way.[5] Possible methods include massive reductions in direct spending programs such as Social Security and Medicaid, reductions in discretionary spending, and huge increases in other taxes such as payroll or corporate income taxes.[6]

Section III of Doctors Gale and Orszag's Article provides examples that demonstrate the magnitude of the changes that might be necessary to fund the proposed permanent tax cuts in 2014 alone:

- A 48% reduction in Social Security benefits;
- Elimination of the federal component of Medicaid;
- An 80% reduction in domestic discretionary spending;
- A 37% increase in payroll taxes; or
- A 124% increase in corporate income taxes.[7]

The authors, of course, do not present these examples as policy prescriptions. But I would add an item to their list, and it is that item to which I initially address my comments. If it were desirable to fund the permanent tax cuts, those same budgetary effects could be replicated by reducing tax expenditures to cover all of the cost of the tax cuts provided through income tax rate reductions and repeal of the estate tax. Tax expenditures seem an especially inviting target given the explosion in the cost of tax expenditures during the Clinton and Bush administrations, with the enthusiastic participation of Congress.

Some data may be helpful. In the fiscal year 1994, there were 119 total tax expenditure programs in the Staff of the Joint Committee on Taxation (the "JCT") list.[8] The total cost was about $2.430 trillion for

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[4] *See infra* Part III.

[5] Gale & Orszag, *supra* note 1, at 1166–68.

[6] Borrowing to finance the cost of making the cuts permanent still would increase the budget deficit further and simply would defer the above actions, to be taken by future generations.

[7] Gale & Orszag, *supra* note 1, at 1170–71.

[8] Computations derived from Staff of the Joint Comm. on Taxation, Estimates of Federal Tax Expenditures for Fiscal Years 1994–1998, at 11–18 (1993), *available at* http://www.house.gov/jct/s-6-93.pdf.

the fiscal years 1994 through 1998, for a five-year average of about $480 billion per year.[9] But, in the most recent JCT tax expenditure list, there were 147 tax expenditure programs (a nearly 20% increase) with a total cost of over $4.944 trillion in the period fiscal years 2004 through 2008 for an average of almost $1 trillion per year, double the revenue cost for fiscal years 1994 through 1998.[10] Doctors Gale and Orszag estimate the cost of making the tax cuts permanent will equal $400 billion in 2014.[11] Thus, it would take a 40% cut in total annual tax expenditures at current cost levels to fund this amount. The tax expenditure accounts also reveal that funding the tax cuts through reductions in tax expenditures could have significantly different social and economic costs than the examples provided by the authors.

Of course, not every tax expenditure can or should be repealed. But, the political debate on, for example, an across-the-board 40% reduction in tax expenditures would seem hardly more contentious than a 48% reduction in Social Security benefits. I can see no compelling reason for eliminating tax expenditures from the budget calculus and for focusing solely on some combination of reductions in direct expenditures and increases in other taxes.[12]

I recognize that in some political circles, repealing or cutting back tax expenditures is not a cut in federal spending; such actions are simply tax increases. Those with this view would oppose such an approach because they would believe it undercuts the objective of tax reduction. This argument, explicitly or implicitly, rejects tax expenditure analysis. That position can be taken. But if it is, intellectual coherence requires that those putting forth the argument openly acknowledge that any reduction in direct spending also is a tax increase.

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[9] I understand the problems of adding revenue costs to produce a total, that is, elimination of one program may cause an increase in the use of a related tax expenditure program. But it is likely that the figure underestimates rather than overestimates the total cost. This issue is discussed in STANLEY S. SURREY & PAUL R. MCDANIEL, TAX EXPENDITURES 51–53 (1985).

[10] Computations derived from STAFF OF THE JOINT COMM. ON TAXATION, ESTIMATES OF FEDERAL TAX EXPENDITURES FOR FISCAL YEARS 2004–2008, at 20–29 (2003), *available at* http://www.house.gov/jct/s-8-03.pdf.

[11] Gale & Orszag, *supra* note 1, at 1170.

[12] The Organization for Economic Cooperation and Development also urged a reduction in tax expenditures as a method to address the U.S. budget deficit. *See* ORG. FOR ECON. CO-OPERATION & DEV., 2004/7 OECD ECON. SURVS. UNITED STATES 83 (May 2004). Again, Doctors Gale and Orszag are not advocating any of the potential approaches they describe to fund permanent tax cuts; in fact, their policy prescription is not to make the 2001 and 2003 tax cuts permanent so that such drastic cuts or tax increases are unnecessary. *See* Gale & Orszag, *supra* note 1, at 1231. They might have the same view with respect to cutting tax expenditures.

This conclusion follows on the fact that direct government payments can be viewed as negative taxes. As a result, any reduction in a direct spending program will cause a reduction in the beneficiary's negative tax rates and may even turn them positive. This is a tax increase!

I thus am prepared to accept either of the following two positions: (1) reductions in tax expenditures are spending cuts just as reductions in direct spending are spending cuts, or (2) reductions in tax expenditures are the equivalent of tax increases and reductions in direct spending programs are also tax increases.

II. The Alternative Minimum Tax

Second, I want to address the impact of the expanding scope of the AMT on the proposed permanent tax cuts. Here I find Table 2 of Doctors Gale and Orszag's Article both revealing and, initially, puzzling.[13] As Table 2 demonstrates, in adjusted gross income ("AGI") classes from zero to $50,000, there is not much AMT impact on the tax cuts. And in the $500,000 to $1,000,000 and over $1 million AGI classes, the AMT likewise claws back only a relatively small amount of the tax cuts (16% and 6.2%, respectively). But, in the AGI classes $50,000 to $500,000, the AMT substantially and, in some cases, dramatically cuts back the impact of the tax cuts. To put the matter differently, for some reason, the AMT is allowed to impact these income groups far more heavily than the groups above and below them.

Why should this be? As Professor Martin McMahon, Jr.'s Article demonstrates, the AMT base has changed dramatically in recent years.[14] Whereas it once was intended to cut back on above-the-line (AGI) exclusions and deductions, successive legislation has reduced or eliminated the impact of the AMT on these items dramatically. Instead, the AMT now falls primarily on exemptions and deductions from AGI, such as state and local income taxes, miscellaneous itemized personal deductions, the medical expense deduction, and the personal exemptions. This statutory structure provides the answer to the above question. Those with AGI below $50,000 are unlikely to be itemizers, so they generally will not be thrown into the AMT. For the super rich, the denial of such items is inconsequential and, in any event, the top AMT rate is only 28% compared to a 35% top individual rate. It is not the purpose of this Commentary to explore why

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[13] *See* Gale & Orszag, *supra* note 1, at app. tbl.2.

[14] Martin J. McMahon, Jr., *The Matthew Effect and Federal Taxation*, 45 B.C. L. Rev. 993, 1044–45 (2004).

Congress would want to have the impact of the AMT fall on the income groups that it does, although no tax or social policy reason readily presents itself.

III. Impact on Future Generations

Finally, Doctors Gale and Orszag's Article points out vividly the devastating impact that making the tax cuts permanent will have on current, younger, and future generations by creating enormous budget deficits. Their data raise for me the question whether there is any ethical argument that can be made to support a shift of responsibility from the currently rich to future less well-off citizens and residents. There are circumstances that can provide ethical support for such a shift. For example, it may well be possible in some cases that current deficits are justified because future generations will be better able to pay for the cost of the expenditures producing the deficits. This belief could be based in confidence on technological advances that will benefit primarily future generations, productivity gains producing higher real incomes, or other advances in areas such as healthcare and dealing with poverty. But I cannot see how anyone can believe that any of these factors can be used to justify the massive federal deficits that would be produced if the 2001 and 2003 tax cuts are made permanent.

I once was present in court at the conclusion of a trial when the defendant's attorney inquired whether the judge would like to receive trial briefs. The judge replied, "I don't need trial briefs." And turning to the defendant he pronounced his judgment: "What you did was just wrong!" That episode accurately captures my view of the judgment future generations will cast on us if these tax cuts are made permanent.

Conclusion

Doctors Gale and Orszag's Article provides an excellent analysis of the economic and social problems that will confront the United States if the Bush Administration's tax cuts are made permanent. The principal contribution of this Commentary is to recommend that tax expenditures be included in any analysis of federal programs to be cut if fiscal discipline is to be restored. It also points out the incoherence of the distribution of the AMT burden and the lack of justification for shifting the burdens of current deficits to future generations.