Tax Cuts Make Sense – Do The Math *(SB News-Press)*

(December 15, 2010) The extension of the Bush tax cuts through 2012 – though not permanent, and packaged with a compromised $190 billion of more unemployment spending through next December – is a modest first step to inject some positive expectations into the private sector. Here's the basic math.

Personal income taxes are reduced for ALL Americans for two more years. Someone making $70,000 will pay around $5,400 less in taxes over the next two years. Employee payroll taxes will drop 2% next year, adding another $120 to that monthly paycheck. What we still really need is payroll taxes sliced for the employer's portion. That would provide more funds that businesses could invest in the company, and to hire more workers.

Firms can write off 100% of capital investments next year, so that $350,000 of new manufacturing equipment will save $120,000 in taxes. That alone could cover the down payment and make the net cost only $230,000. The firm could also hire more workers and expand.

Other business tax breaks that expired at the end of 2009 are back in 2011. And while there was no estate tax just for 2010, the new top rate in 2011 will be 35% (not the old 55%), and the exemption will be $5 million (up from $1 million). I advocate elimination of the estate tax permanently because these are already after-tax values and should not be double-taxed.

But the $860 billion in tax savings over two years exposes different philosophies behind the deal. I, and many others, see it simply that the American private sector gets to keep $860 billion of its own hard-earned cash. Matt Continetti described this philosophical gap in the September 27th *Weekly Standard*: "In the liberal imagination, our earnings are the government's by default, and the president and Congress determine through the tax code how much to give back to the people."

Others ridicule the tax cuts as "unfair," "helping the rich," and "adding to the deficit." Let's take these in order. First, the cuts are actually VERY fair because they are across-the-board and keep funds in the hands of the entire range of households and businesses throughout the economy. Second, lower taxes help *everyone.* How can politicians arbitrarily impose their own bias that $250,000 of earnings defines someone as rich? Why not $200,000? Or $500,000? How about $328,466? The profit incentive and enterprise opportunities to create and build wealth are what drive American capitalism. More after-tax income in the private sector increases the supply of capital and lowers the cost of borrowing and investing, for households and businesses to purchase assets, expand, modernize, and create jobs. Third, tax cuts only add to the deficit if the government spending money it no longer has. A larger deficit is not the fault of the tax savings.

This math exposes the huge difference in how households and businesses understand "revenue," compared with the federal government's view. Household revenues are earnings people are paid for work. When wages and salaries are reduced, households typically reduce spending. Business revenues come from selling goods and services to buyers in the market. When sales are down, companies trim budgets to save operating costs. But government's revenues are taxes, fees, tariffs, and other costs imposed by legislation and regulatory compliance. When the economy is down or flat, tax revenues decrease, but government either maintains or even increases spending. The new Congress needs to commit to spending less and let the tax cuts help the economy.

There's a lot of misinformation about the Bush tax cuts so let me set the record straight. The dot.com bubble peaked in March 2000, Bill Clinton's last year in the White House. The ensuing economic downturn was already ten months along before Bush took office in January 2001. When 9/11 happened eight months later, there was every reason to believe the U.S. economy would experience a significant recession. In the immediate aftermath, New York City alone lost almost half a million jobs and $3 billion in wages during the fourth quarter of 2001. The stock market fell and unemployment moved higher. The military responses to protect America from further attacks significantly increased defense spending and deficits, and the Bush tax cuts were a strong response to the potential for a prolonged economic downturn. During his two terms, the U.S. economy grew from $10 trillion to $14.44 trillion. That's a 4.6% average annual rate (compounded quarterly) – a total 44% over 8 years. Once the tax cuts took effect in 2003, the economy had 52 consecutive months of job creation through 2007, as unemployment remained under five percent.

The Bush tax cuts also get blamed for huge deficits, but total federal spending as a percentage of GDP actually dropped to 18% in Bush's first year, and stayed between 18% and 20% for his entire 8 years (today it has ballooned to 25%) – while funding two major military operations. And while the 2004 budget deficit was 4% of GDP, the pro-growth tax cuts fueled economic expansion and lowered that to just 1% of GDP in 2007 (today it's over 9%).

Two years of tax cuts are only the beginning of what's needed to jump-start the economy and create millions of jobs. Yes the Dow Jones is up 19% in the second half of this year – gaining 1,800 points. But it's only up 30% total over the last two years. Unemployment was over 10%, eased a bit to 9.4%, but last month went back up to 9.8%. The U.S. economy needs to add 300,000 new jobs each month through December 2013 just to get back to pre-recession levels. GDP has been flailing this year – from a 3.2% pace in IQ, down to only 1.7% in IIQ, and then 2.5% in IIIQ. Government must rein in runaway spending, earmarks, and pork projects that do nothing to spur economic growth. And funding another $1 trillion (probably more) for Obamacare would be two giant steps back after extending the Bush tax cuts gives us one step forward. More funds in the private sector and less under the control of government is math that always makes sense.