THE TAXONOMIST

Down is Up (or so some say)

By Robert S. McIntyre

New budget projections from the Congressional Budget Office suggest that this year's deficit will be $75 billion or so smaller than last year's record level. Similar figures will be reported by the Bush administration just after this column goes to press. The right is already claiming victory.

"Our policies continue to boost the economy and tax revenues," says Rep. Jim Nussle (R-Iowa), chairman of the House Budget Committee. "These numbers prove what we've said all along," chimed in House Speaker Denny Hastert (R-Illinois). Indeed, claims GOP anti-tax zealot Stephen Moore in the *Wall Street Journal*, "The numbers are an eye-popping vindication of the Laffer curve."

Now wait a minute. Far from "an eye-popping vindication" of right-wing theories, the recent budget news is merely an eye-glazing vindication of the laws of arithmetic. Consider:

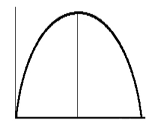
When Bill Clinton left office, he had turned the huge non-Social-Security deficit he inherited from the first President Bush—equal to 4.6 percent of the economy—into a small surplus. He did that by boosting revenues by a fifth and cutting spending by a seventh. But George W. Bush quickly took us back to the bad old days. By the end of last year, non-Social-Security revenues had plummeted from 15.1 percent of the economy to a 62-year low of only 11.3 percent. Coupled with increased spending (largely on Iraq), that produced a deficit of 4.9 percent of the economy.

To be sure, taxes are doing better this year. Corporations are paying more, mostly due to a tax hike (the big corporate tax cuts that depressed revenues in fiscal 2002 through 2004 expired). Personal income taxes are up, in part because there weren't any significant new tax cuts this year. Even so, this year's non-Social-Security revenues are likely to about a fifth below what Bush inherited from Clinton, and the deficit outside of Social Security will probably be close to $500 billion, or 4 percent of the economy.

Here are the rankings of non-Social-Security tax receipts as a share of the economy since 1943. Fiscal 2003 and 2004 are tied for the lowest. Fiscal 2002 ranks third lowest. This year will probably rank fifth lowest—hardly anything to clap about.

In a nutshell, Clinton cut spending, raised taxes and with the help of a booming economy, balanced the budget. Bush cut taxes and increased spending—and deficits skyrocketed. It's a familiar pattern that even the most ardent believer in voodoo economics ought to be able to see. Unless, of course, facts just don't matter.

Which brings us back to Steve Moore's citing of "the Laffer curve." A simple parabola sketched out on a cocktail napkin back in 1974 by the felicitously named Arthur Laffer (then a University of Chicago business professor), this theory holds that there is a magical, ideal tax rate that produces the most revenues for the government. Tax less than that rate, and you'll get less revenue. Tax more and you'll also get less. Rather like Goldilocks, you might say.



In practice, Laffer and his disciples applied his theory only to the top income tax rate. Although Laffer's number-free graph didn't specify the ideal rate, during the Reagan administration it was assumed to be 50 percent, which is what President Reagan's 1981 tax cut bill prescribed. Reagan was so enamored of Laffer's idea that he famously promised to pay for his defense build-up with the revenues generated by his tax cuts.

That, of course, didn't work out. Yet despite that failure, not to mention the fact that revenue-maximization seems like an odd goal for those who claim to be anti-big-government, the Laffer curve has remained in the background as one of several bedrock, albeit incoherent tenets of what has passed for "conservative" economics over the past three decades. There is one codicil: whatever the current top tax rate, it's always too high.

To be sure, GOP leaders haven't trumpeted Lafferism during the Bush administration until very recently. On the contrary, Bush started off telling us we needed to cut taxes because the government simply had too much money. When that fantasy was quickly disproved, Bush cited the need to stimulate the weak economy (even though his tax cuts were backloaded into the future). Once the economy recovered, the tax cuts were defended as a way to force huge reductions in allegedly wasteful (and unspecified) government programs. Now, as spending has risen anyway, Republicans have come full circle, back to the ridiculous Reaganesque claim that their tax cuts are helping raise the money to pay for Bush's profligate spending.

You shouldn't believe any of these excuses, but certainly no rational person can believe all of them. Ultimately, it seems, the reason that Republican politicians and their allies favor tax cuts is because, well, they favor tax cuts. If that means bankrupting our country, so be it.

ROBERT S. MCINTYRE *is director of Citizens for Tax Justice.*