The Bush tax agenda courts a budget disaster

By Bruce L. Fisher

WASHINGTON — The Bush administration's current drive to cut the tax on capital gains is part of a larger economic policy agenda that, if enacted, will fundamentally change the nation's tax system while swelling the federal budget deficit — all at the expense of middle- and lower-income Americans.

The administration has persuaded the House and now awaits a Senate vote to cut the capital-gains tax, at a net cost of $21 billion over 10 years.

Bush also wants incentives for savings, such as expanded Individual Retirement Accounts, arguing, against a mountain of contrary evidence, that this will stimulate personal savings. Treasury Secretary Nicholas F. Brady has proposed costly corporate tax breaks, including a deduction for stock dividends that would cost $40 billion a year.

To deal with the budget-busting impact of these changes, the president's team is likely to seek enactment of a regressive national sales tax similar to the value-added taxes assessed in Europe.

Unfortunately, some key House and Senate members are receptive to these ideas. The Democratic congressional leadership had already endorsed expanding tax breaks for IRAs. And Senate Finance Committee Chairman Lloyd Bentsen has said "there'd be a good chance" for enacting a national sales tax if Bush gave the plan his full support.

These proposals will all swell the deficit. They will all contribute to a further shift of wealth from the middle class to the wealthy. None of them will increase savings or reduce the cost of capital.

These proposals are on the table because the 1986 Tax Reform Act has been an economic success but a political failure. Although tax sheltering is down and both savings and investment are up since the tax bill was enacted, the public has never been convinced that the Reagan administration and Congress did the right thing three years ago.

Public skepticism has left tax reform vulnerable to special-interest lobbyists who want pre-1986 tax breaks restored in the name of helping business capital formation.

Advocates of capital formation point with alarm to our high real-interest rates and our low national-savings rate. Capital costs in the United States are higher than in Japan and West Germany. But the primary cause is Washington's excessive borrowing — to cover the debt run up by the supply-side tax cuts of the early 1980s.

Moreover, Department of Commerce data show that the personal savings rate is now on an upswing, from a low of 2.3 percent of GNP in 1987 to 4.0 percent for the first two quarters of 1989.

This resurgence in personal savings has occurred despite the limitations on IRA tax deductions enacted in 1986, whereby they were restricted to families that make less than $50,000 or have no other private retirement plan. Congress took the heat on IRAs in the 1986 tax reform act because it saw that unrestricted IRAs were merely a tool used by high-income people to shift existing savings into tax-advantaged accounts.

Meanwhile, since the 1986 reforms eliminated many of the costliest tax breaks for business, corporate profitability has grown. Real capital spending has grown at an annual rate of 6.1 percent since 1986, compared to an anemic 2.1 percent over the previous five years.

The fact is that tax reform has worked and worked well but that the federal deficit continues to hang like a millstone around the economy's neck.

The Bush agenda would reprise the early Reagan administration program, which President Reagan himself abandoned in 1986, and fund it with a national sales tax, which will take a larger share of the disposable incomes of lower-income people than of higher-income people.

Studies by the Congressional Budget Office show that between 1977 and 1988, the richest 1 percent of Americans enjoyed a 74 percent jump in real after-tax incomes, while real incomes for low- and middle-income families stagnated or declined.

And the lesson of the early Reagan years is that if you give the rich more money, they don't save it — they spend it. Between 1983 and 1986, for example, U.S. sales of Jaguars went up 55 percent; Mercedes, 35 percent; Porsches, 40 percent; and BMWs, 63 percent, while sales of U.S.-made cars grew by only 21 percent.

The Bush agenda would swell the deficit and then raise taxes on working people, all in the name of helping business. The fact that business is doing just fine now goes unnoticed. The fact that the deficit impedes business capital formation is ignored. It's time for Congress to come to its senses and reject the whole Bush agenda on this issue and get to work on our largest national problem: the federal budget deficit.

Fisher is research director of Washington-based Citizens for Tax Justice. He wrote this for the Los Angeles Times.