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Ardavan Mobasheri: Tax proposals borrow from the future to spend now

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THE GOP-CONTROLLED House of Representatives voted on its version of tax "cuts" last week, and the Senate will have its chance shortly after the Thanksgiving holidays.

Once the House and the Senate have talked through their differences and special interests have had their opportunity to speak out, what is likely to come out of Congress will be different than any of the proposals we have seen to date. One thing, however, that will be a certainty is that any final bill placed on President Donald Trump's desk will essentially be a tax cut that increases the deficit to the tune of $1.5 trillion over 10 years.

And the impact on economic growth in the long-run? Questionable, at best. What drives an economy to expand beyond the short term are labor force growth (i.e., population growth), and labor productivity (i.e., how much smarter the workers are working). The proposals to date do not address either of these factors in a material way. Hence, other than the possibility of a short-term impact on consumption and spending, they are not likely to result in sustainable acceleration in the economy. We may see 3 percent-plus growth here and there, but not on an ongoing basis.

The history of tax cuts, particularly since the 1980s, tells us that marginal reductions in income taxes result in short-term increases in personal consumption and spending on the part of individuals for a very brief period — usually not more than a year — and a reversion back to the old growth rates shortly thereafter.

Meaningful reductions in corporate tax rates can result in significant increases in investment over time and even higher wages at times. But that is not what is being proposed.

The proposed reduction in the statutory rate — from 35 percent to 20 percent — simply brings the rate down to near what is actually being paid now by corporations after allowable deductions. Lowering the statutory rate while simultaneously eliminating many deductions is akin to taking from one hand and giving it to the other and expecting more activity as a result.

Many people on the right, including the president, repeatedly argue that our taxes are one of the highest in the world as a reason for cuts.

However, if looked at in terms of how high those taxes are relative to what they produce, we have some of the lowest taxes in the world. According to the Organization for Economic Cooperation and Development, combined tax collection of all kinds represented roughly 26 percent of the U.S. gross domestic product in 2015, which placed the United States 32nd lowest out of the 35 countries analyzed.

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What is somewhat surprising, though not necessarily remarkable, is how the debate between Democrats and Republicans over the proposals is dominated by who the primary beneficiaries are or aren't today. The voices of reason who argue over who benefits or doesn't in the longer run are hard to hear these days. The voices of whether the middle class is getting a cut or not, or of whether the rich will pay more or not, are loud and clear. However, the voices questioning who will pay for the cuts are not.

Is the U.S. tax system in need of reform? Absolutely. The last meaningful reform occurred in 1986, and the world economy has changed significantly since then. However, it needs to be genuine reform, not a haphazard plan of cuts that increase the deficit while masquerading as reform.

Borrowing from our grandchildren — and asking our children to pay the interest on that borrowing while we spend and consume the money today — is not the answer.

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