

# OpinionJournal

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from THE WALL STREET JOURNAL *Editorial Page*

October 30, 2007

OUTSIDE THE BOX

## Inconvenient Tax Truths

*Charlie Rangel and other liberal leaders want to raise tax rates even if it means lower tax revenues.*

BY PETE DU PONT

Nobel Peace laureate Al Gore believes global warming is "an inconvenient truth." Here are some economic truths that America's liberal leadership finds too inconvenient to support.

Tax rate reductions increase tax revenues. This truth has been proved at both state and federal levels, including by President Bush's 2003 tax cuts on income, capital gains and dividends. Those reductions have raised federal tax receipts by \$785 billion, the largest four-year revenue increase in U.S. history. In fiscal 2007, which ended last month, the government took in 6.7% more tax revenues than in 2006.

These increases in tax revenue have substantially reduced the federal budget deficits. In 2004 the deficit was \$413 billion, or 3.5% of gross domestic product. It narrowed to \$318 billion in 2005, \$248 billion in 2006 and \$163 billion in 2007. That last figure is just 1.2% of GDP, which is half of the average of the past 50 years.

Lower tax rates have been so successful in spurring growth that the percentage of federal income taxes paid by the very wealthy has increased.

According to the Treasury Department, the top 1% of income tax filers paid just 19% of income taxes in 1980 (when the top tax rate was 70%), and 36% in 2003, the year the Bush tax cuts took effect (when the top rate became 35%). The top 5% of income taxpayers went from 37% of taxes paid to 56%, and the top 10% from 49% to 68% of taxes paid. And the amount of taxes paid by those earning more than \$1 million a year rose to \$236 billion in 2005 from \$132 billion in 2003, a 78% increase.

Finally, another inconvenient truth is that there have been 49 consecutive months of job growth as a result of the economic expansion induced by President Bush's 2003 tax rate reductions.

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One would think that this positive economic performance would inspire Congress to

continue the successful policies that caused it. But the liberal establishment takes a negative view of tax rate reductions and embraces the opposite approach: ensure expiration of the Bush tax cuts in 2011 and in the meantime enact substantial tax increases.

Rep. Charles Rangel of New York, chairman of the tax-writing House Ways and Means Committee, last week introduced an estimated \$3.5 trillion tax increase that would raise the capital gains tax rate from 15% to 19.6% and places a surtax of as much as 4.6% on people making more than \$150,000 a year. Mr. Rangel applies it not to current taxable income but to adjusted gross income, thus phasing down itemized deductions such as charitable contributions, home mortgage deductions, and state and local tax deductions. Together with the end of the Bush tax cuts, Mr. Rangel's plan would increase the top income tax rate to 44% from 35% for individuals, small-business owners and farmers, who make up about three-fourths of taxpayers in the highest bracket.

While raising taxes on individuals, the Rangel bill would reduce corporate tax rates to 30.5% from 35% and eliminate the alternative minimum tax. That would be "paid for" by increasing taxes on hedge funds and buyout firms by about \$48 billion.

Federal tax revenues have been rising between 6.7% and 14.5% in each of the past three years, but the proposed tax increases, by slowing rather than stimulating the economy, would ensure that these percentages decline. Hillary Clinton defines the liberal tax policy as "we are going to take things away from you on behalf of the common good," but in the unlikely event that the tax bill passes Congress next year, President Bush's veto pen will surely take away from the liberal leadership things that will do harm to the common good.

On the other hand, the 2008 elections could lead to a very different outcome, for the Rangel bill shows in which direction tax policy will proceed

if there is a Democratic president and Congress in 2009.



A much more interesting approach was introduced in the House three weeks ago by Rep. Paul Ryan, a Wisconsin Republican: elimination of the Alternative Minimum Tax, extension of the 15% capital gains and dividend rates that expire in 2010, and giving taxpayers a choice between filing under the current tax system or a new option with just two income tax brackets, 10% for joint filers with incomes less than \$100,000 and 25% for those with higher incomes. It includes a \$25,000 standard deduction plus a \$3,500-a-person exemption, which comes to \$39,000 for a family of four. The new option would be a flat-tax choice, with no other exemptions or loopholes, and the AMT would be gone.

Every taxpayer would be able to make a choice between the current tax system with the AMT burden, tax rates from

10% to 35%, and many complex deduction options, or the Taxpayer Choice Act. Mr. Ryan estimates that the federal government's revenues--excluding AMT revenues, the elimination of which would cost the government only about 2.4% of revenues over 10 years--would be about the same as under the current system, and the top 5% and 1% of taxpayers would pay slightly higher taxes than they do today.

Such a system would stimulate the economy, increase economic growth and job opportunities, and simplify a very complex and frustrating current tax system. But for the liberal establishment a flat tax with lower rates would be a very inconvenient truth. Much better in their view are the substantial Rangel tax increases.

*Mr. du Pont, a former governor of Delaware, is chairman of the Dallas-based National Center for Policy Analysis. His column appears once a month.*