Senate Democratic Policy Committee Hearing

"Will The Bush Economic Plan Create Jobs?"

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Mr. Chairman and Members of the Committee, thank you for allowing me to express the views of Empower America on the economic growth aspects of H.R. 2, the Jobs and Growth Tax Relief and Reconciliation Act of 2003 recently enacted into law. We at Empower America enthusiastically support the tax reforms contained in H.R. 2.

Alexis de Tocqueville famously observed that, "Men will not receive the truth from their enemies, and it is very seldom offered to them by their friends…" I am here today as a friendly adversary, to share with you the truth, as I see it.

The reason I care about the state of the Democratic Party is that for our democracy to be strong, both political parties must be strong and capable of competing for every vote in our national family. For many years, the Republican Party suffered from a lack of ideas. Before Ronald Reagan came along, we couldn't propose ideas to move America forward because we were obsessed with deficits.

I speak to you today as someone who has spent a lifetime in politics trying to encourage my colleagues and friends to support policies premised upon maximizing economic growth. Not as a means of promoting an ideology, or "theology", as former President Clinton described it, but to promote sound economic principles to provide the greatest good for the American economy and the American people. In fact, I first learned of supply-side economics not from Art Laffer or Robert Mundell, but from reading the speeches of John F. Kennedy circa 1962.

In an eloquent speech before the New York Economic Club President Kennedy provided the rationale for corporate and personal tax relief. He argued, "Next year's tax bill must reduce personal as well as corporate income taxes—for those in the lower brackets, who are certain to spend their additional take-home pay: And for those in the middle and upper-brackets, who can thereby be encouraged to undertake additional efforts and enabled to invest more capital. Third, the new tax bill should improve both the equity and the simplicity of our tax system."

These words could easily have been uttered by President George W. Bush while campaigning for the recently enacted tax cuts and those words ring as true today as they did back then. It is not just the rhetoric that is similar, but the proposals I believe are similar as well.

In 1962, President Kennedy proposed legislation to cut income tax rates by 25 percent and corporate tax rates by 10 percent "to increase incentives and the availability of investment capital." After the Kennedy tax cuts became law the economic growth rate expanded from 4.3 percent to 6.6 percent and the economy created over 1 million jobs the following four years. A 1966 article in the US News and World Report read, "Tax collections are beginning to astonish even those who pushed hardest for tax cuts in the first place."

Indeed, after the tax cuts took effect, income tax collections rose by more than 50 percent from 1963 to 1968. Economic growth picked up and the deficit fell. By 1965, economic growth had increased sufficiently that in spite of increased defense spending, the budget was essentially balanced. Except for one year (1968), the deficit was 1.5 percent of GDP or less throughout the decade, even as defense spending averaged 8.5 percent of GDP, which is more than twice the 4.4 percent we will spend on defense this year, including the president's emergency request for an additional $75 billion.

Today, President Bush has signed into law tax relief that will cut personal income tax rates across-the-board, slash capital gains and dividend tax rates, increase the so-called expensing provisions for small business, and expand provisions for accelerated depreciation and alleviating the marriage penalty.

Most criticism of the Bush tax cuts have focused on three general points:

1) the tax cuts are skewed toward "the rich";
2) the tax cuts will not "stimulate" aggregate demand; and
3) the tax cuts will explode the deficit.

It's important to remember that all taxpayers benefit under the just passed tax legislation. Those preoccupied with the "top one percent" of all wage earners would do well to remember that roughly two-thirds of the people in the top one percent are owners of flow-through entities, including small business owners and entrepreneurs who file not under the corporate code, but under the individual income tax code. These individuals currently pay 37.4 percent of all income taxes. Also, families earning more than $100,000 will end up paying 73 percent of all federal income taxes after the law goes into effect. And, under the Act, the lowest income group (under $30,000) will on average receive refundable credits in excess of $400 from other taxpayers.

Secondly, opponents argue that the tax cuts will not "stimulate" the economy and will not "put money in peoples' pockets." I would argue the economy does not need, nor has it ever needed government-induced economic "stimulus," nor in fact is it even possible for the government to "stimulate" economic growth in the short run without causing long-run damage to the economy.

The most important provisions of the tax legislation are those that reduce the disincentives for work, saving, investment and entrepreneurial risk taking. These provisions are: the across the board income tax rate reductions, capital gains and dividend tax rate reductions, the increased "expensing" provisions for small business and the expanded provisions for accelerated depreciation.

Despite the success of the Kennedy tax rate reductions in the 1960s, the Reagan tax rate reductions in the 1980s and dramatic effects of the capital gains tax rate reductions in 1997 some insist pro-growth policies will not work this time around.

Many of the people arguing that today's tax rate reductions will not help our economy return to a growth trajectory are the same people who argued the increase in capital gains taxes in 1986 would produce a windfall to the Treasury. For example, in 1986 the Congressional Budget Office (CBO) and the Joint Committee on Taxation (JCT) predicted that the increase in the maximum capital gains tax rate from 20 percent to 28 percent would not deter asset sales and would increase government revenues. In 1985 capital gains realizations were greater than $165 billion, and those realizations dropped precipitously after the enactment of the tax hikes in the capital gains tax rate, falling to $116 billion in 1992. The $26.8 billion collected in capital gains revenues for 1992 was about 13 percent greater than the $23.7 billion collected in 1985, but after adjusted for inflation, the collections represented a 13 percent decline.

Conversely, in 1997, those who said the tax rate reductions were solely for the wealthiest one percent also argued the Treasury and the economy would be worse off after the tax cuts. Wrong again. The capital gains tax rate reductions reduced the net cost of new investment by approximately 3 percent and were responsible for approximately 25 percent of the 1997 stock price increases, and revenues exploded. In 1996, the last year with the 28 percent rate, the government collected $62 billion in capital gains receipts. In 1999, the government took in an estimated $110 billion in receipts.

Finally, the opponents of the tax cuts ominously warn about the danger of "exploding deficits." I remember hearing many of these same people argue the same points about the Kemp-Roth/Reagan tax rate reductions in 1981.

In the 1960s John F. Kennedy observed, "Our true choice is not between tax reduction, on the one hand, and the avoidance of large federal deficits on the other. It is increasingly clear that no matter what party is in power, so long as our national security needs keep rising, an economy hampered by restrictive tax rates will never produce enough revenues to balance our budget just as it will never produce enough jobs or enough profits. Surely the lesson of the last decade is that budget deficits are not caused by wild-eyed spenders but by slow economic growth and periodic recessions, and any new recession would break all deficit records. It is a paradoxical truth that tax rates are too high today and tax revenues are too low and the soundest way to raise revenues in the long run is to cut rates now."

These words proved prophetic, for in the 1980s the same battle was fought yet again. And again, John F. Kennedy's words reminded us of the course we should take. Ronald Reagan heeded that call and passed the Kemp-Roth tax rate reductions.

The result:

During the Reagan years the Treasury Bill interest rate fell from 14% in 1981 to 7% by 1989, inflation fell from 13.5 percent to 4.1 percent, unemployment from 7.6 percent to 5.5 percent, GDP expanded by an average of 3.2 percent, and federal tax revenues exploded from $517 billion to $1.031 trillion. During the Reagan years the national debt went from 27 percent of GDP to 42 percent of GDP, largely do to a tripling of government spending and as for "exploding deficits", that opponents often quote, when Reagan walked into the White House in 1981 the federal deficit was 2.7 percent of GDP, when he left in 1989 it was 2.9 percent of GDP.

Ironically, when President Kennedy proposed his tax plan it was the Republican Party and conservative members of Congress who accused him of being "fiscally irresponsible." And, then, as with President Bush's tax plan today, the opponents of tax relief argued it would explode the deficit and cause undo burden on the national debt.

To opponents, President Kennedy replied, "Our practical problem is not between a tax-cut deficit and a budgetary surplus. It is between two kinds of deficits; a chronic deficit of inertia, as the unwanted result of inadequate revenues and a restricted economy, or a temporary deficit of transition, resulting from a tax cut designed to boost the economy, increase tax revenue and achieve—and I believe this can be done—a future budget surplus." The same argument holds true today.

Thank you.