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Taxes and the Deficit Reduction Plans

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Abstract

Plans to rein in the U.S. budget deficit remain in the spotlight as the Bipartisan Policy Center's Debt Reduction Task Force released its plan to solve the debt crisis. TPC expert William Gale offers analysis of the recommendations and includes recommendations of his own.

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Introduction

The deficit reduction plan offered this week by the Bipartisan Policy Center is a serious and attractive plan. On the tax side, where I will focus, it shares key features with, but is more nuanced than, the draft proposal released last week by Alan Simpson and Erskine Bowles, the co-chairs of President Obama's fiscal commission. Both commissions would broaden the tax base and reduce tax rates. That's the right direction for reform, for all of the reasons described here.

Both of the proposals have been criticized for cutting taxes on the wealthy, but that depends on the baseline used (see reports from the Tax Policy Center here and here). The BPC proposal specifies changes in tax expenditures—cutting the mortgage interest deduction and charitable contributions deductions into 15 percent credits—whereas the Simpson-Bowles proposal would just wipe them all out. Because the co-chairs wipe out more tax expenditures, they can afford to reduce rates by somewhat more than the BPC proposal. The biggest difference between the two proposals is that the BPC also includes a value-added tax. It isn't called a VAT, it is called a "Debt Reduction Sales Tax," but it is actually a VAT. That's good news. It would give U.S. more options for dealing with the fiscal problem and could help solve the fiscal problem, as described here.

Tax increases are going to have to be part of the solution to the fiscal problem. It is encouraging to see two bold plans come out in such a short period. While it is a long way from the release of a non-binding commission report to enacted legislation, one can hope that the release of the two reports will let people talk in terms of one plan versus another, rather than implicitly comparing the plans to the status quo.

Other Publications by the Authors

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