

# Lost in the Tax Debate: Would Growth Benefit? How much GOP plan would help the rich matters less than if GDP boost comes true

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## FULL TEXT

Since rolling out their "unified framework" for a tax overhaul last month, the Trump administration and Republican congressional leaders have been on the defensive, trying to bat down accusations their plan is a boon to the wealthy. The rich "will not be gaining at all," President Donald Trump claimed before the plan was released. "Wealthy Americans are not getting a tax cut," Gary Cohn, Mr. Trump's top economic adviser, insisted soon afterward.

There are two problems with their claims. The first is that they are wrong: As currently envisioned, the plan would deliver huge benefits to the wealthy. The second is that, according to how they view the economy, that shouldn't matter. Mr. Trump's goal, as his officials never tire of saying, is to stimulate economic growth. If the plan succeeded on that front, that should mean far more for the middle class than any reapportionment of taxes.

Some 40 years ago, the economist Arthur Okun argued that most economic problems come down to a tradeoff between equality and efficiency. For example, higher tax rates on the most productive workers and on companies narrow the gap between rich and poor but also discourage work and investment, in his view.

Democrats have traditionally prioritized equality over efficiency; Republicans, the opposite.

Mr. Trump sought to break that mold by promising a tax cut that he said would both spur growth and benefit the middle class more than the rich. A few days after the framework was released, a prominent think tank said he failed. The Tax Policy Center concluded the top 1% of households would see after-tax incomes rise 8.7% in a decade's time while those of the middle 20% would see their incomes edge up just 0.5%.

There are several ways this critique of the GOP plan, which has yet to be finalized, is incomplete. For example, it assumed the top individual tax rate would drop to 35% from 39.6% even though Mr. Trump and Republicans have said it may not. And it left for later any assessment of the impact on overall economic output.

Yet raising economic output is what the plan's architects say is foremost in their mind. Kevin Hassett, chairman of Mr. Trump's Council of Economic Advisers, said in a speech last week that even Greece's socialist government and former President Barack Obama accept that cutting corporate rates and eliminating corporate breaks—a centerpiece of the plan—ought to have some positive impact on the broader economy.

"We are just responding to the global consensus that corporate tax rates are harmful generally and particularly for the U.S.," Mr. Hassett said.

The benefit of cuts in tax rates is long debated, with critics asking why cuts haven't spurred growth booms in the past, in the U.S. or abroad. One reason is that the impact is transitory. Suppose a rate cut makes the economy 3% larger than it otherwise would be. Over a decade that would raise annual economic growth by 0.3 percentage point before reverting to its old growth rate.

Moreover, it can be impossible to disentangle tax changes from other influences such as demographics, technology, the business cycle and monetary policy. The impact of fiscal stimulus is hard to detect for the same reason, yet economists still believe it exists.

Analysts at the Tax Policy Center doubt this plan would generate much growth because it would lead to deficits that push up interest rates and soak up savings that would otherwise finance private investment. But this may be less true when the world is awash with savings and Treasury bonds yield just 2.3%. Indeed, yields throughout developed countries are low even as government debt has on average climbed above 100% of GDP, according to the International Monetary Fund.

The Tax Foundation, a think tank that favors lower rates, believes a 20% corporate rate would eventually lift gross domestic product by 3.1% and wages by 2.6%.

Also subject to debate is how much the middle class is helped by lower corporate taxes. The Tax Policy Center assumed 80% of the benefits go to owners of capital and just 20% to workers.

But some economists think that understates how high corporate taxes depress investment and productivity, the ultimate source of wage growth. In a 2007 paper, economists Mihir Desai and Fritz Foley of Harvard University and James Hines Jr. of the University of Michigan compared countries and time periods and concluded 45% to 75% of the benefit of cuts in corporate tax rates go to workers .

The administration is likely overpromising by claiming its tax cut would permanently lift the growth rate to 3% from its recent 2% trend, given an aging workforce. Yet even a temporary boost translates to a higher standard of living for most households.

Moreover, the windfall for the wealthy could be trimmed without undermining the growth dividend. For example, if the GOP scrapped its idea of repealing the estate tax, it would free up money for the deficit or more generous treatment of investment with no loss to 99% of households.

Even so, the final plan would no doubt shower benefits on the wealthy, by virtue of the fact they own the companies whose taxes are being cut. That may not bother workers if they benefit in the process—which would be a more plausible defense than the plan's advocates have mustered thus far.

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