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To Cut And To Please
Contributions of Ronald Reagan's Tax Cut Policy on the 1980s

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Growth in Federal Outlays
(Billions of Dollars)

	Outlays			
Fiscal	Real (1987 Dollars)		Current Dollars	
Year	Amount	% Increase	Amount	% Increase
1980	$ 832.1	6.4	$ 590.9	17.4
1981	867.7	4.3	678.2	14.8
1982	891.1	2.7	745.8	10.0
1983	921.1	3.4	808.4	8.4
1984	933.5	1.4	851.8	5.4
1985	1001.3	7.3	946.4	11.1
1986	1017.3	1.6	990.3	4.6
1987	1003.9	(1.3)	1003.9	1.4
1988	1027.1	2.3	1064.1	6.0
1989	1057.9	3.0	1144.2	7.5

Source: Budget of the United States Government, FY 1993, Supplement 1992, Table 1.3, Part 5-18.

One of the standard allegations is that the very large budget deficits were caused by the Reagan tax cuts. As Representative Donald J. Pease (D., Ohio) put into (June 11, 1992): "Let us look at the big deficits we have and try to find out what caused them . . . Fundamentally, our $4-trillion deficit or debt is caused by loss of revenue. The $4-trillion debt is caused by the 1981 tax cut and misguided supply-side economics."

The initial Reagan game plan, as detailed in the February 18, 1981, White Paper referred to by Paul Craig Roberts, projected a shift in federal budget outcomes from deficit to surplus occurring in fiscal year 1984. Although federal revenues as a percentage of gross national product were projected to fall from 21.1 per cent in 1981 to 19.3 per cent in 1984, the dollar amount of budget receipts was expected to increase from $600.2 billion in the former year to $772.1 billion in the latter. In the same period, federal outlays were to rise from $654.7 billion to $771.6 billion, although falling in relation to GNP from 23.0 per cent to 19.3 per cent. In essence, this budget policy represented an effort to bring receipts and outlays in relation to GNP more nearly in line with the average postwar experience.

The 1981-82 recession that had been developing in the late 1970s and in 1980 undid the Reagan plan. The revenue projections in the White Paper assumed prompt enactment and implementation of the proposed individual rate reductions and changes in depreciation provisions that would have raised the level and rate of growth of GNP. Although these tax changes were expected to reduce tax revenues compared to the amounts that would have been obtained under prior law, revenues in 1981 were nevertheless expected, at the higher levels of income produced by the tax changes, to exceed those in 1980 and to continue to grow each year thereafter.

Federal Budget Outlays, Proposed and Actual

(Dollar Amounts in Billions)

Fiscal	Outlays	
Year	Proposed	Actual
1981	$655.2	$678.2
1982	695.3	745.8
1983	773.3	808.4
1984	862.5	851.8
1985	940.3	946.4
1986	973.7	990.3
1987	994.0	1003.9
1988	1024.3	1064.1
1989	1094.2	1144.2

Source: Budget Message of the President, Fiscal Years 1981–89; Budget of the United States, FY 1993, Part Five, Table 1.3, page 5-18. Proposed outlays for 1981 from the March 1981 FY 1982 Budget Revisions.

In fact, under the influence of the recession and the unexpectedly sharp deceleration of inflation, budget receipts fell far short of those projected in the White Paper. Receipts were virtually the same in fiscal 1983 as in fiscal 1981 and were about $110 billion below the White Paper estimate. From 19.6 per cent of GNP in 1981, receipts fell to 18.1 per cent of GNP in fiscal 1983.

With the recovery beginning in late 1982, budget receipts expanded rapidly, on the average by slightly over 8 per cent a year, through fiscal 1990. By that year, budget receipts were 18.9 per cent of GNP. Whether the several substantial tax increases from 1982 through 1989 — particularly the Tax Equity and Fiscal Responsibility Act (TEFRA) of 1982, the Deficit Reduction Act (DEFRA) of 1984, and the Tax Reform Act of 1986 (TRA86) — contributed to rather than retarded this growth in revenue is, at the least, debatable. Unless one believes, however, that tax increases necessarily lose revenue (a not entirely implausible proposition), there is no basis in fact for insisting that tax-policy developments were responsible for the budget deficits of the Reagan years.

A major element in the initial Reagan budget policy was a slowdown in the growth of federal outlays and a change in their composition. The White Paper contemplated total budget outlays rising from $654.7 billion in fiscal 1981 to $771.6 billion in fiscal 1984, an annual rate of increase of 5.6 per cent. Defense outlays were to increase from 24.1 per cent of the total to 32.4 per cent, and the so-called "safety net" programs were to increase from 36.6 to 40.6 per cent, while all other programs and interest were to fall from 38.3 to 27.0 per cent.

This part of the budget plan, too, was not realized. Although the growth in federal outlays, in both nominal and real terms, slowed materially from fiscal 1980 through fiscal 1989, total outlays substantially exceeded those proposed in every Reagan budget. As a result, even had the revenues projected in the White Paper been realized, the budget would have failed to come into balance in 1984, when actual outlays of $851.8 billion were $80 billion more than had been contemplated.

Federal spending growth slowed more in Reagan's second term under the constraints imposed by the Gramm-Rudman-Hollings deficit-reduction targets. Contrary to the widespread assertion that if failed of its purpose, G-R-H was amazingly effective in slowing the growth of federal outlays. From fiscal 1985 through fiscal 1989, total outlays, measured in constant 1987 dollars, increased at an average annual rate of only 1.4 per cent, just over one-third the annual rate of increase in fiscal years 1981-85. Even measured in current dollars, G-R-H slowed the growth of spending, from an annual rate of 8.69 per cent in fiscal years 1981-85 to 4.86 per cent over the next four years.

Had federal outlays in the ensuing fiscal years increased no more rapidly than the 4.86 per cent average rate of 1985-89, federal outlays in fiscal 1992 would have totaled $1,319.2 billion, $156.2 billion less than the amount projected in the February 1992 budget document. Even with the recession-depressed revenues projected in the budget for the current fiscal year, the 1992 deficit would be $243.5 billion, not the $399.7 billion forecast.

Despite the success of G-R-H until its emasculation by the Omnibus Budget Reconciliation Act of 1990, total federal outlays grew too rapidly to achieve anything like fiscally prudent budget results. Political memories are short, but surely neither Democrats nor Republicans have forgotten that the standard congressional response to the Reagan budget proposals was "DOA." The historical budget record documents the failure of Congress to curb its appetite for spending increases. With the single exception of fiscal 1984, actual outlays in each of the fiscal years 1981-89 exceeded the Reagan budget requests, by as much as $50 billion in fiscal 1989. Spending excesses, not excessive tax cuts, account for the sorry budget deficit record of the past decade.

Distribution of Aggregate Revenue Loss Relative to Prior Law

(Millions of Dollars; 1981 Income Levels)

Expanded income class	Prior law tax liability	1982 total reductions	1983 total reductions
Under $5,000	–157	–69	–109
$5,000–$10,000	6.381	–937	–1,479
$10,000–$15,000	16,317	–1,925	–3.287
$15,000–$20,000	22,987	–2,651	–4,675
$20,000–$30,000	58,558	–6,715	–12,349
$30,000–$50,000	85,708	–10,183	–18,923
$50,000–$100,000	51,631	–5,900	–11,002
$100,000–$200,000	24,125	–2,639	–4,437
Over $200,000	21,110	–3,588	–4,080
Total	286,659	–34,803	–60,341

Expanded income equals adjusted gross income plus excluded capital gains and various tax preference items, less investment interest to the extent of investment income.

Deliberate Deficits?

A related myth is that these deficits were deliberate, part of the Reagan Administration's effort to reduce social spending. As Senator Daniel Patrick Moynihan (D., N.Y.) put it (June 25, 1992): "Mr.

Stockman, in his book, The Triumph of Politics: Why the Reagan Revolution Failed, describes this policy, this conscious policy of creating deficits, which in the White House and in the Office of Management and Budget at the time there was a term for it, it was called starve the beast . . . the Federal Government was the beast. It had to be starved."

The view that President Reagan indeed any President, could have engineered the deficits of the last several years boggles the mind. Conceivably, this could occur if federal budget receipts and outlays were determined solely by the President, and if these fiats of the President were impervious to economic developments. David Stockman, Pat Moynihan, and everyone else who subscribes to this notion know it is patent nonsense.

The initial Reagan fiscal agenda, as we have seen, called for spending slowdowns aimed at eliminating the budget deficit in fiscal 1984 and at producing budget surpluses thereafter. This agenda relied on the economic and budget projections for which David Stockman, as Director of OMB, was chiefly responsible. Stockman himself made determined efforts to come up with feasible proposals for slowing the growth of total outlays, while effecting the compositional shifts that were a basic part of the Reagan strategy. When he discovered the obstacles to achieving adequate cuts in increases in spending, Stockman sought to moderate the revenue losses in ERTA. And when the recession depressed tax revenues below the levels in his original projections, Stockman urged a shift to tax increases to moderate the deficits. It is astonishing that he would subsequently avow what would necessarily have been his own duplicity if the budget policies for which he was so largely responsible had, in fact, aimed at creating budget deficits.

As we have also seen, following ERTA, every tax bill proposed or supported by the Administration was a revenue raiser. It is impossible to reconcile this record of tax increases with the inane notion that the Reagan Administration's objective was to enlarge budget deficits.

The key to the deficits is the role of the Congress in budget making. Most of the budgets that President Reagan sent to Congress after 1981 were either rejected out of hand or very materially altered. Former OMB Director Jim Miller often recounts Reagan's asking him why he bothered to send a budget to Congress since the Budget Committee's standard reaction was to disregard it and to fashion its own.

Indeed, it may have been Congress's embarrassment over its role as the engineer of budget deficits that led most of its members to support G-R-H. And it is certainly reasonable to believe that deficit projections dampened congressional ardor for spending increases greater than those that actually occurred. But none of this places responsibility for the budget deficits on the Reagan Administration.

The Incentive Angle

According to the myth-makers, in addition to starving social spending, the Reagan policies were intended to favor the rich at the expense of the poor. As Governor Clinton's Putting People First:

A National Economic Strategy for America (June 20, 1992) stated it: "For twelve years, the driving idea behind American economic policy has been cutting taxes on the richest individuals and corporations . . . ." The Governor has a fragile grasp of history, even that of the recent past.

For one thing, during the eight years of the Reagan Administration, only one tax bill, ERTA, reduced taxes for upper-income individuals and corporations. The central objective of the initial Reagan program, of which ERTA was a critically important part, was to reorient national economic policy. Instead of focusing on income re-distribution and aggregate demand management of the economy, the Reagan policy aimed at reducing the Federal Government's intrusion into the nation's economic life. It sought to provide a policy climate in which individuals' incentives to pursue their own economic progress would not be frustrated by government tax, spending, regulatory, and monetary policies. ERTA's role in this economic strategy was to reduce the disincentives of high and steeply progressive individual tax rates and the biases they exerted against working, saving, and investing, and to provide more realistic and more nearly neutral tax treatment of investment in plant, machinery, and other depreciable property.

ERTA's core elements were a 25 per cent cut in individual marginal tax rates, phased in over three years, and the replacement of the archaic Useful Life depreciation system with the Accelerated Cost Recovery System. Another extremely important element in the Act was the indexing of the individual rate brackets, personal exemptions, and standard deductions. The indexing provisions sought to limit the bracket creep that, during the inflation-ridden 1970s, had escalated the real tax burdens of all taxpayers, but most severely hurt low- and middle-income individuals, for whom the tax brackets were very narrow.

ERTA reduced taxes for virtually all individual taxpayers, but the percentage reductions in tax liabilities for the lower- and middle-income taxpayers exceeded those for the rich. To be sure, the dollar amounts of the tax reductions for the well-to-do were greater; even Bill Clinton and his allies should have enough arithmetical savvy to recognize that a cut of one-tenth of one per cent in a $1,000,000 tax liability is ten times as many dollars as a 100 per cent cut in a $100 tax liability. If they troubled themselves to hunt up the data, they'd find that, according to the estimates of the staff of the Joint Committee on Taxation, the overwhelming bulk — more than two-thirds — of ERTA's individual tax cuts went to people with so-called "expanded" incomes of less than $50,000. Moreover, the percentage reductions in tax liabilities were greatest for people with expanded incomes of less than $10,000. People in the over-$200,000 class enjoyed tax reductions of 20.9 per cent, while the income taxes of those in the $5,000 to $10,000 range were reduced by 27.1 per cent.

Before President Reagan's signature on ERTA was dry, an effort to reverse the thrust of the Reagan tax policy got under way. The effort was undertaken both in Congress and in the Administration itself.

The Administration found itself in the late summer of 1981 looking at what it thought was the need for a drastic shift in fiscal strategy. The Democratic leadership in the Congress, smarting under its blistering defeat at President Reagan's hands in the enactment of ERTA, launched their own counterattack in the late summer of 1981. Its principal effort was to roll back the business-incentive provisions in ERTA, an effort that met with little resistance from the White House. The result was the grossly mislabeled Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA). With this legislation, much of ERTA's tax savings and most of the positive incentive effects for business were eliminated.

The alleged centerpiece of the Reagan tax policy is the Tax Reform Act of 1986 (TRA86). The Act's attention grabbers were the dramatic revision in the individual-income-tax rate structure, eliminating all but two of the prior law's sixteen rate brackets, and the sharp cuts in the top rates of both the individual and corporate income taxes. Far more consequential and extensive, however, were the Act's so-called base broadeners. In this respect, TRA86 was the most thorough-going revision of the income tax since its inception — the culmination of the traditional, liberal tax reformers' "loophole" — closing efforts.

Some of these changes broadened the tax base, while others contracted it. The increases in the personal exemption and standard deduction had the effect of taking an estimated four million or more low-income individuals off the income-tax rolls altogether and of materially reducing the tax liabilities of millions of low- and middle-income individuals. Virtually all of the other base changes, on the other hand, increased the taxes of millions of other middle-income as well as most higher-income taxpayers.

According to estimates of the staff of the Joint Committee on Taxation, TRA86 would reduce individual income-tax liabilities by close to $122 billion over the five-year period 1987-91. Over the same period, it would raise corporate income-tax liabilities by $120.3 billion.

Estimated percentage changes in tax liabilities ignored entirely the huge increases (about $227 billion for the years 1987-91) in higher-income individuals' tax liabilities resulting from the hundreds of billions of dollars of base broadeners — effectively accentuating the double taxation of saving.

Welcome as were the changes in the statutory rate structure of the individual income tax and the cutback in the top statutory rate to 28 per cent, TRA86's base broadeners were an enormous price to pay. TRA86 can be perceived as conferring tax favors on the rich only if these base broadeners are ignored.

Additional tax increases, falling entirely on business and upper-middle and higher-income individuals were enacted in 1987 and 1988.

The cumulative effects of the tax legislation during the Reagan years has been a substantial increase in the share of federal income-tax liabilities paid by the wealthy. In 1981, the wealthiest — the top 1 per cent — paid 17.6 per cent of total federal individual income taxes; in 1988, their share had increased to 27.5 per cent.

Even a cursory review of the fiscal history of the Reagan years reveals that, with the sole exception of ERTA, all the tax changes enacted during that period were unmistakably anti-business and anti-rich individuals. If, contrary to fact, tax fairness were properly measured by the shares of total tax burdens borne by lower-, middle-, and higher-income individuals, one would have to say that the Reagan tax program was as fair as all get-out.

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