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Why The Tax Deal Is A Good Deal

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The tax deal is a big positive breakthrough. It could have been better, but it was better than I ever expected. We shouldn't expect too much boost from it, however, because taxes weren't lowered. We just avoided the calamity of a large tax increase at a very bad time. We dodged a bullet.

The Payroll Tax Cut

The deal suffers somewhat from a confusion of goals. Presumably, the number one priority was supposed to be jobs, jobs, jobs. The two percent reduction in the payroll tax for employees will likely help a little with new job creation—but very little. How much more targeted it would have been for job creation if the reduction were on the employer portion of the payroll tax. That would have directly reduced the cost of hiring. This seems like a no brainer, but one side was apparently interested in the appearance of helping people—albeit people already employed—than the reality of helping them with a tax reduction that ostensibly goes to employers.

Let me repeat: reducing the tax on employer hiring would have created more hiring than reducing the tax on those already working. If the false cosmetics had to be honored, they could have at least cut both the employer and employee section. The way they did it will give a small amount of new purchasing power to the employed, but with virtually no positive job impact and with a likely proportionate increase in the budget deficit.

Extension of Unemployment Benefits

My thinking on this issue has undergone some change recently. Heretofore, I've accepted the academic argument that more generous unemployment benefits increased the level of unemployment and slowed the rate of decline in unemployment, although I have assumed the degree of harm to be fairly modest. I've also believed that those conclusions are more relevant to actual policymaking when the unemployment problem is less severe than it is today. With available and accessible jobs so few and the number of unemployed so large, my view has been

during this recession that such tough love is a tad too tough. To reduce employment by reducing or limiting unemployment benefits might speed the process along, but at a great cost in human suffering.

I haven't moved too far away from that view, but I recently talked to executives in the construction business who gave me a perspective that shouldn't have been new to me, but was. They said that, in practice, many lower-level, lower-wage workers collect unemployment benefits and also work a day or two a week "off the books," and that this combined income compared favorably with wages-only income. Consequently, many workers—not just a few, but many—are content with their unemployed status.

I assume that the same problem exists in various degrees outside the construction industry, but I don't know how prevalent it is. I've wondered from time to time whether unemployment benefits shouldn't be phased down to smaller amounts over time to gradually make them less competitive with employment.

Expensing

More generous expensing provisions, or even 100 percent expensing permanently, strikes me as a good idea. Temporary expensing will likely spur investment temporarily, but investment will likely drop off at that point. Full expensing is better than cash for clunkers since the latter took cash (taxes) from some of us to give to others—color that unfair as well as neutral in its impact—while expensing is more likely to pay for itself through more rapid growth. Still, why not make it permanent?

The Death Tax

Okay, 35 percent over a higher exemption is better than 55 percent over a lower exemption, but any amount above zero sticks in my craw. What is fair about taxing the assets bought with income that has already been taxed six ways to Sunday?

Fairness is my big complaint; however, the disincentives to economic growth would be sufficient grounds for opposition without the fairness issue. Why keep working hard in those latter years if it's going to the government? Why make heirs have to sell businesses to pay the taxes or even homes for that matter.

What gets me is the tax I think is the least fair is apparently the tax most loved by those who don't vote my way. They probably have good tax and estate attorneys.

Taxes on Income, Capital Gains, and Dividends

Extending what we already have and which has been baked into the cake a long time won't provide much new stimulus to the economy. However, avoiding the massive tax increase that would have come from their expiration dodges a big bullet. Hopefully, we will all feel the exhilaration that comes with being shot at and missed and will give our animal spirits free rein again. If 2011 is much better than we had been expecting—and I suspect it will be—it might be harder to take the cuts back in the next round.