WebMemo

Published by The Heritage Foundation

No. 956
January 5, 2006

Make the Bush Tax Cuts Permanent

William W. Beach and Rea S. Hederman, Jr.

This Thursday marks the beginning of a renewed effort by the White House economic team to make the 2001 and 2003 tax cuts permanent. Bush Administration officials will carry this message to key states: their tax policy program has helped the U.S. economy to thrive, with steady job creation and strong economic growth. If the tax cuts of 2001 and 2003 are allowed to expire, millions of working families will see their economic prospects dim, their job opportunities diminish, and economic uncertainty rise.

The central provisions of these landmark tax bills are scheduled to expire over the next five years, which means that taxes will rise dramatically for most taxpayers. Between now and January 1, 2011 (five short years away),

- Tax rates will rise substantially in each tax bracket, some by 450 basis points;
- Low-income taxpayers will see the 10-percent tax bracket disappear, and they will have to pay taxes at the 15-percent rate;
- Married taxpayers will see the marriage penalty return;
- Taxpayers with children will lose 50 percent of their child tax credits;
- Taxes on dividends will increase beginning on January 1, 2009;
- Taxes on capital gains will increase, also beginning on January 1, 2009; and
- Federal death taxes will come back to life in 2011, after fading down to nothing in 2010.

What make this tax nightmare scenario particularly scary are the economic benefits that will never be realized if the 2001 and 2003 tax cuts disappear. Businesses are watching now to see if Congress will make permanent the first to expire of the major economic growth components of the 2001 and 2003 tax acts—lower taxes on dividends and capital gains. Failing to make permanent the low tax rates on investment would signal to businesses of all sizes that the other major elements of the Bush tax plan will also be allowed to expire. They would adjust their investment and hiring accordingly.

Economists in the Center for Data Analysis at The Heritage Foundation used a mainstream model of the U.S. economy to project the economic effects of making the tax cuts of 2001 and 2003 permanent. Their report estimates significant economic gains throughout the period from 2006 through 2014, particularly after 2008. For example, making certain that taxes on investment remain low will add about 285,000 jobs per year in fiscal years 2008 and 2009. In those two years alone, lower taxes on capital gains and dividends mean an additional $70 billion in economic output and an additional $110 billion in disposable income for households.

This paper, in its entirety, can be found at:
www.heritage.org/research/taxes/wm956.cfm

Produced by the Center for Data Analysis

Published by The Heritage Foundation
214 Massachusetts Avenue, NE
Washington, DC 20002–4999
(202) 546-4400 • heritage.org

Nothing written here is to be construed as necessarily reflecting the views of The Heritage Foundation or as an attempt to aid or hinder the passage of any bill before Congress.

The Heritage Foundation

If Congress makes the tax cuts permanent, the major economic benefits begin in 2011. For example,

- Total employment will rise by 1,087,000 jobs per year, on average;
- Annual GDP will be over $111 billion higher, after inflation;
- Personal savings will grow by $163 billion per year, on average, after inflation; and
- After-tax household income will grow by an annual average of $274 billion per year, after inflation.

However, these benefits become economic losses if Congress fails to make the 2001 and 2003 tax cuts permanent. What is the cost of failing to act? Over one million lost jobs each year between 2011 and 2014; over a hundred billion dollars less in economic output per year; slower wage and salary growth; slower savings growth; and so on. The need for Congress to make the 2001 and 2003 tax cuts permanent is clear.

The four attached charts focus on the employment gains from making the tax cuts permanent—or, alternatively, the forgone potential growth should Congress fail to act. Chart 1 presents the average annual growth in employment for each state between 2008 and 2014 if the tax cuts are made permanent. The year 2008 is important from a policy perspective because investors, workers, and business owners will know then whether or not significantly higher taxes are in their future as the low tax rate on capital gains and dividends is now set to expire on December 31, 2008. Chart 2 presents the average annual growth in disposable personal income in every state if the tax cuts are made permanent. Chart 3 focuses on the states that the Bush economic team will visit in the coming days and covers the four-year period, from 2011 through 2014, during which the biggest economic gains from permanency will be realized, while Chart 4 presents income growth over the same period—but only, that is, if Congress makes the tax cuts permanent.

Rea S. Hederman, Jr., is Senior Policy Analyst in, and William W. Beach is Director of, the Center for Data Analysis at The Heritage Foundation.

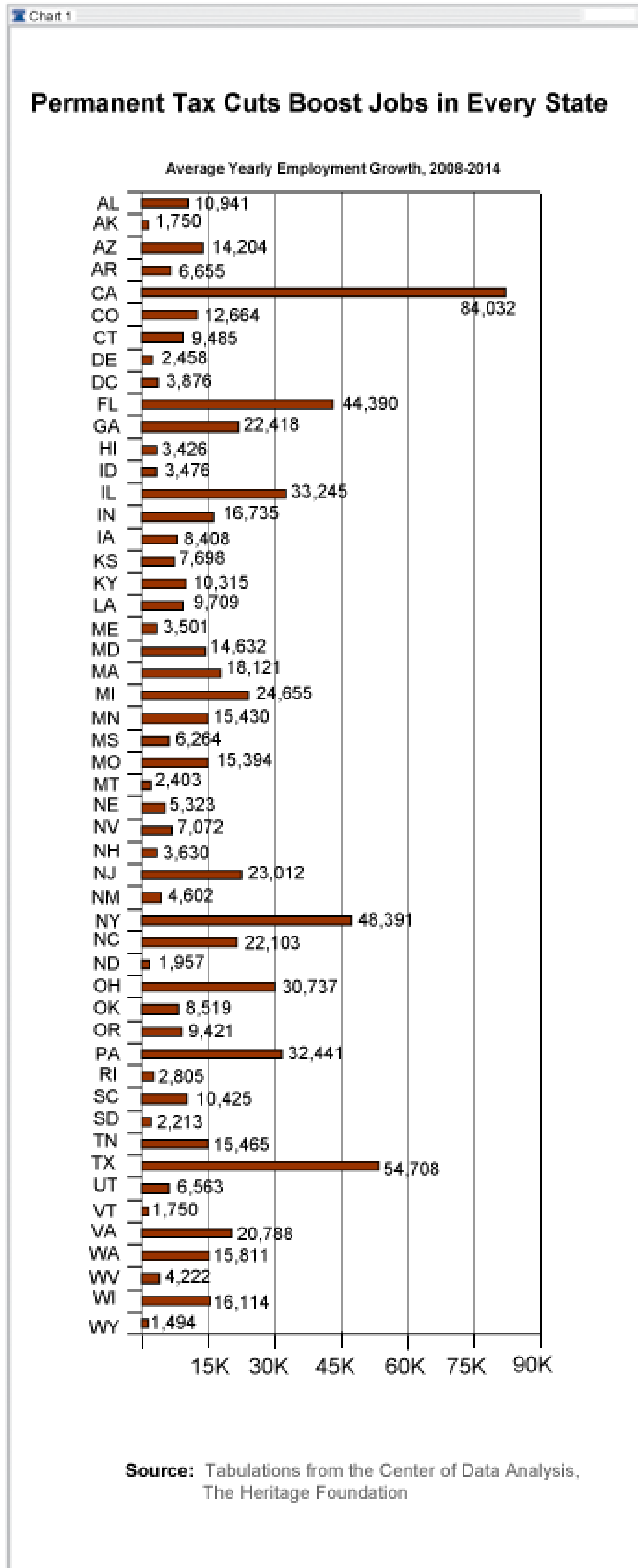
Chart 1
Permanent Tax Cuts Boost Jobs in Every State
Average Yearly Employment Growth, 2008-2014
AL 10,941
AK 1,750
AZ 14,204
AR 6,655
CA 84,032
CO 12,664
CT 9,485
DE 2,458
DC 3,876
FL 44,390
GA 22,418
HI 3,426
ID 3,476
IL 33,245
IN 16,735
IA 8,408
KS 7,698
KY 10,315
LA 9,709
ME 3,501
MD 14,632
MA 18,121
MI 24,655
MN 15,430
MS 6,264
MO 15,394
MT 2,403
NE 5,323
NV 7,072
NH 3,630
NJ 23,012
NM 4,602
NY 48,391
NC 22,103
ND 1,957
OH 30,737
OK 8,519
OR 9,421
PA 32,441
RI 2,805
SC 10,425
SD 2,213
TN 15,465
TX 54,708
UT 6,563
VT 1,750
VA 20,788
WA 15,811
WV 4,222
WI 16,114
WY 1,494
15K 30K 45K 60K 75K 90K
Source: Tabulations from the Center of Data Analysis, The Heritage Foundation

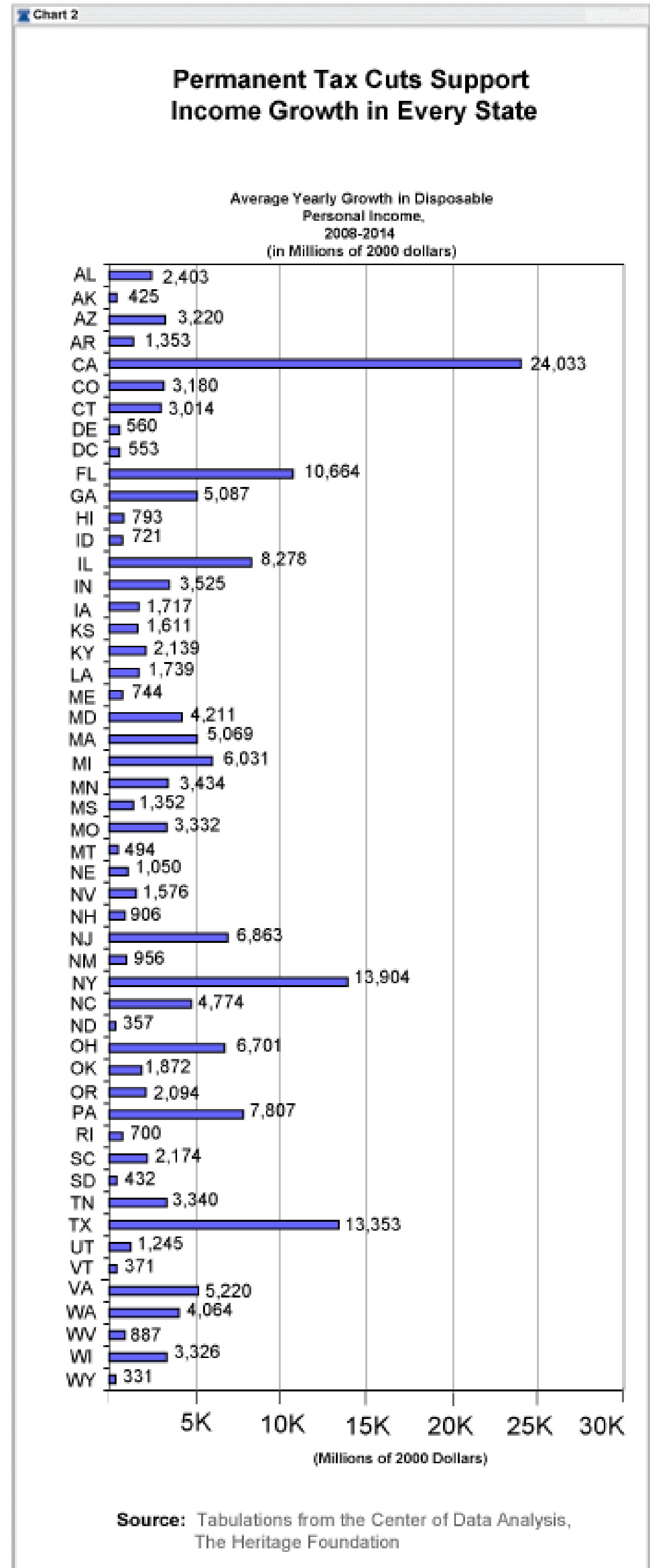
Chart 2
Permanent Tax Cuts Support Income Growth in Every State
Average Yearly Growth in Disposable Personal Income, 2008-2014 (in Millions of 2000 dollars)
AL 2,403
AK 425
AZ 3,220
AR 1,353
CA 24,033
CO 3,180
CT 3,014
DE 560
DC 553
FL 10,664
GA 5,087
HI 793
ID 721
IL 8,278
IN 3,525
IA 1,717
KS 1,611
KY 2,139
LA 1,739
ME 744
MD 4,211
MA 5,069
MI 6,031
MN 3,434
MS 1,352
MO 3,332
MT 494
NE 1,050
NV 1,576
NH 906
NJ 6,863
NM 956
NY 13,904
NC 4,774
ND 357
OH 6,701
OK 1,872
OR 2,094
PA 7,807
RI 700
SC 2,174
SD 432
TN 3,340
TX 13,353
UT 1,245
VT 371
VA 5,220
WA 4,064
WV 887
WI 3,326
WY 331
5K 10K 15K 20K 25K 30K
(Millions of 2000 Dollars)
Source: Tabulations from the Center of Data Analysis, The Heritage Foundation

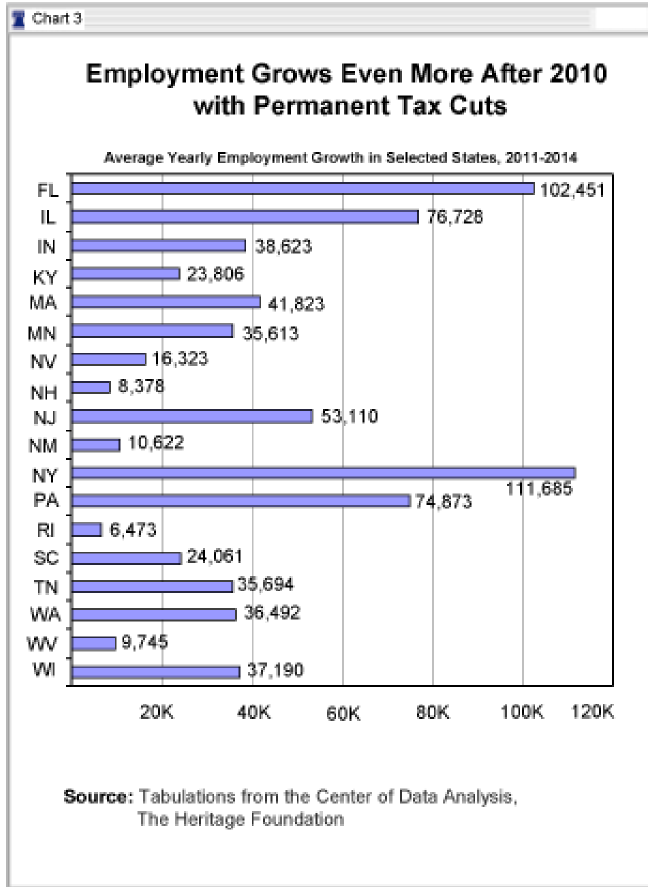
Chart 3
Employment Grows Even More After 2010 with Permanent Tax Cuts
Average Yearly Employment Growth in Selected States, 2011-2014
FL 102,451
IL 76,728
IN 38,623
KY 23,806
MA 41,823
MN 35,613
NV 16,323
NH 8,378
NJ 53,110
NM 10,622
NY 111,685
PA 74,873
RI 6,473
SC 24,061
TN 35,694
WA 36,492
WV 9,745
WI 37,190
20K 40K 60K 80K 100K 120K
Source: Tabulations from the Center of Data Analysis, The Heritage Foundation

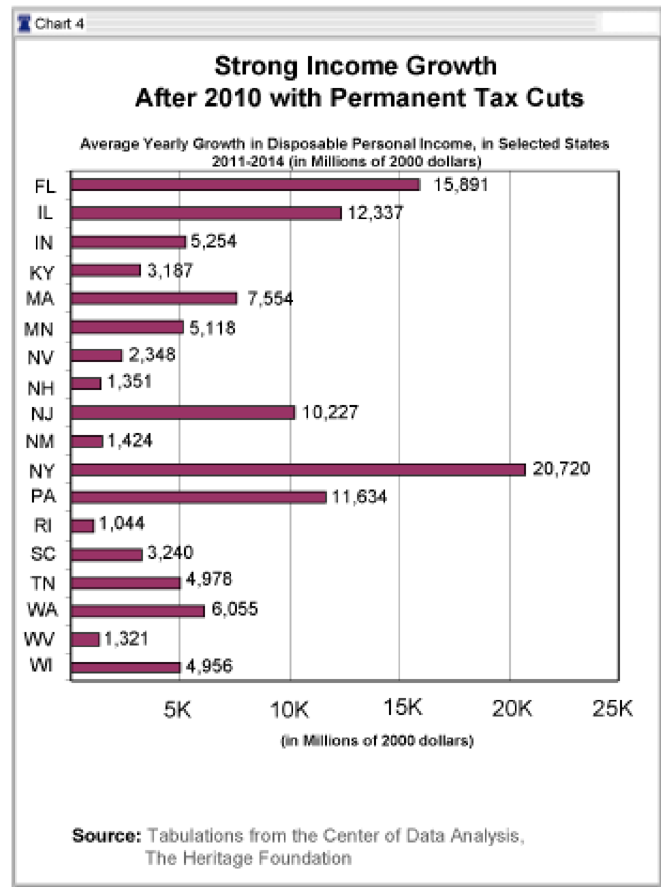
Chart 4
Strong Income Growth After 2010 with Permanent Tax Cuts
Average Yearly Growth in Disposable Personal Income, in Selected States 2011-2014 (in Millions of 2000 dollars)
FL 15,891
IL 12,337
IN 5,254
KY 3,187
MA 7,554
MN 5,118
NV 2,348
NH 1,351
NJ 10,227
NM 1,424
NY 20,720
PA 11,634
RI 1,044
SC 3,240
TN 4,978
WA 6,055
WV 1,321
WI 4,956
5K 10K 15K 20K 25K
(in Millions of 2000 dollars)
Source: Tabulations from the Center of Data Analysis, The Heritage Foundation