

Comments on Altshuler and Bosworth's paper on Fiscal Consolidation in America: the Policy Options



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Difficulty of recovery and its implication on budget management

Table 2. Illustrative Rebalancing

Percent of potential GDP

| Demand Component | Mid-2010 | Alternative Recovery Paths | |
|------------------|--------------------------|----------------------------|--------------------|
| | Shortfall from Potential | Pre-Crisis Economy | Economic Rebalance |
| Consumption | -4.0 | 4.0 | 1.0 |
| Investment | -4.0 | 4.0 | 2.0 |
| Net Exports | 2.0 | -2.0 | 3.0 |
| Government | 0.0 | 0.0 | 0.0 |
| Total GDP | -6.0 | 6.0 | 6.0 |

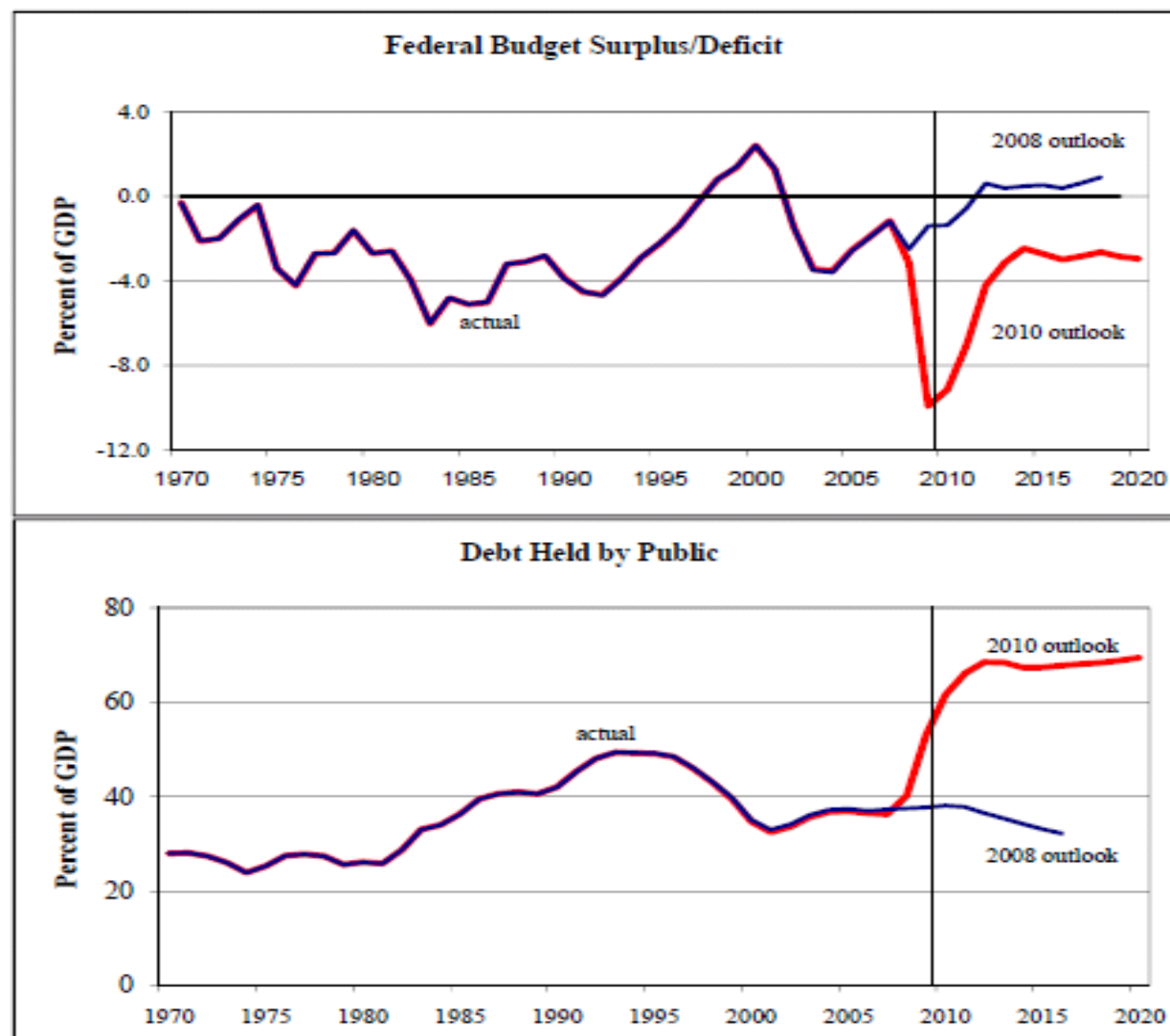
Source: Authors' calculations as described in text.

- Going back to the consumption-driven pre-crisis days is difficult.
- Rebalancing the economy by expanding exports is also difficult.
- So, either structural reform of expenditure or revenue, or both are necessary.

CBO's Budget Projection

- Congressional Budget Office (CBO) numbers provide an overly optimistic picture and understate the magnitude of the budget problems.
- CBO Current-law: assumes Bush-tax expiration, termination of AMT (alternative minimum tax) indexation, increases of discretionary expenditure limited to adjustment for price inflation
- Current-Policy baseline: assumes the continuation of the Bush-tax cuts, inflation adjustment of the AMT, increases in discretionary spending in line with the growth of the GDP

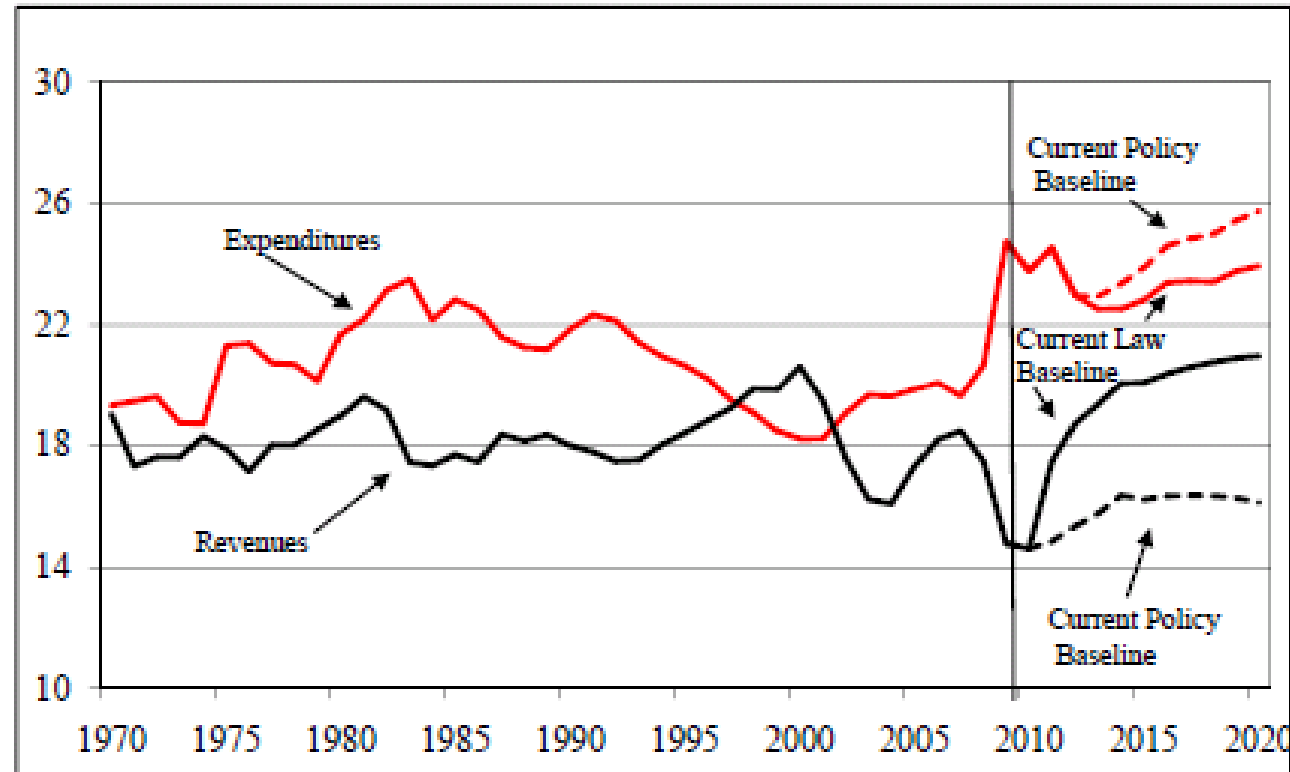
Figure 4. The Federal Budget Balance and the Public Debt, 1960-2019.
Percent of GDP



Source: Congressional Budget Office, Budget and Economic Update, August, 2010 and August 2008.
Baseline Projections

Current-policy projection tells that less-than 3% deficits in 2015 and after is infeasible.

Figure 5. Federal Revenue and Expenditures, 1970-2020
Percent of GDP



Source: Congressional Budget Office. 2010c.

Expansion of health-care costs in the federal budget

- “Medicare and Medicaid are subject to the same demographic factors that will increase Social Security benefits in future years; but **additional pressures result from a historic trend of increases in costs per enrollee in excess of the average growth in per capita incomes.** In past decades, this excess cost growth has averaged about two percent per year.” page 21.

Health-care cost control in the U.S.

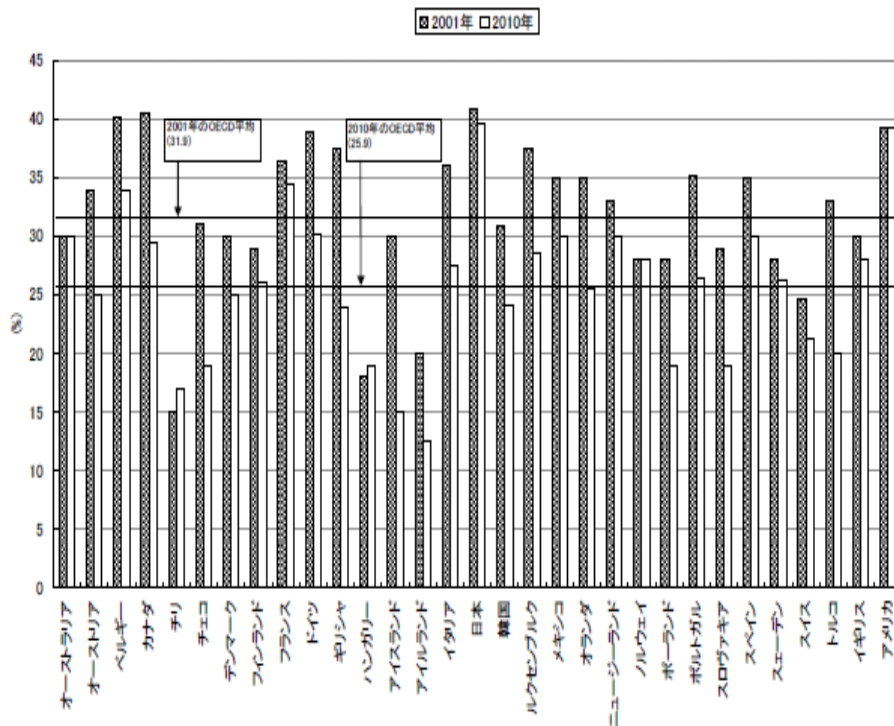
- How is the federal budget used for financing the health-care costs in the U.S.? Is it merely for ex-post balancing the health-care budget or is there any other ex-ante (say, contractual) fiscal measure to meet the balance?
- How will the Obama's health care affect the budget? His address at the congress said not a dime will be added to the fiscal deficit. Is this true?
- Why the Obama's plan was so much disliked the Republicans?

Revenue-side reform

- “ALW’s exercise clearly shows that simply increasing rates is not a realistic approach to reducing the deficit. Further, raising revenue solely from high-income individuals is not the answer to the revenue problem going forward.” page 33.
- “A more credible perspective would be that a broadening of the corporate tax base should be used to “pay down” the current law’s high marginal corporate income tax rates. That in turn means that corporate tax reform is unlikely to be a significant net revenue raiser.” page 33

A note on the corporate income tax in Japan

図表1 OECD諸国の法人税率（国税と地方税）



- The statutory corporate tax rate of Japan is slightly higher than the U.S.
- Japan moved into a territorial system; exempted income repatriated from foreign subsidiaries.

(出所) 田近 (2010b)、原資料は OECD Tax Database

A package proposal for tax reform

- *Broaden the individual and corporate income tax bases:* reducing the value of itemized deductions to 15 percent
- *Add a VAT to the current system:* 5 percent VAT could raise revenues equal to 2.2 percent of GDP; providing per-capita refundable credits to all individuals; overall 1.6 percent of GDP.
- *Raise gas taxes:* An increase in gas taxes of 50 cents could raise revenues equal to 0.4 percent of GDP.

Base broadening

Table 7. Largest Income Tax Expenditures, 2011-2015
(dollar amounts in billions)

| Provision | 2011-15 |
|---|---------|
| Exclusion of employer contributions for health insurance | 1,054 |
| Mortgage interest deduction | 638 |
| Exclusion of employer and employee contributions to employer-provided pensions and retirement plans | 608 |
| State and local tax deduction (property, income, etc.) | 451 |
| Capital gains step-up at death | 283 |
| Preferred rates on capital gains | 271 |
| Charitable contribution deduction | 257 |
| Exclusion of net imputed rental income | 224 |
| Capital gains exclusion on home sales | 216 |
| Exclusion of interest on municipal bonds | 180 |
| Accelerated depreciation | 147 |
| Exclusion of interest on life insurance savings | 132 |

Source: Office of Management and Budget, Analytical Perspectives, February 2010.

- Broadening tax base is important. But tax expenditures that result from various deductions look so deep rooted into vested interests.
- Isn't mortgage interest deduction "necessary" for recovery?

Prospect of introducing the VAT in the U.S.?

- With the VAT already in place in Japan and with almost 200% of public debt, it still is very difficult in Japan to persuade the public about the necessity/ importance of increasing its rate (presently 4% for the central, and 1% for the local governments) .
- How can the American people who have no prior knowledge of the VAT and state governments with sales tax be persuaded?