



Statement of Senator Chuck Grassley
Finance Committee Hearing on Administration's Budget: Revenue Proposals
February 2, 2010

Today, we focus on the revenue side of the budget. It is almost entirely in this committee's jurisdiction. It cannot be denied that the budget illustrates the fiscal peril the country faces. The President and Congress face a very tough set of tasks to start us on the path to fiscal discipline. Ignoring that path only makes the ultimate reckoning more difficult.

Mr. Secretary, this hearing provides us with the opportunity to take a look at the current fiscal policy path. We need to ask three questions. Where are we? How did we get here? And, finally, where we are going? The President is right that he did inherit large deficits and debt. I have one chart that shows the inherited deficit. And here's a chart that shows the inherited debt.

Republicans recognize that fact. To have an intellectually honest discussion, members on both sides need to own up to the fact that the deficits and debt were bequeathed on a bipartisan basis. The Congressional Democratic leadership wrote the budgets and passed the spending bills for two years prior to President Obama's inauguration. An outgoing Republican President signed those bills. Let's get the facts straight. A Democratic Congress and Republican President left the deficits and debt.

Over the past year, with the levers of power all concentrated in the hands of those on the other side, we've seen the fiscal path worsen. Deficits are up. Debt is up.

That, Mr. Secretary, is where we are. How did we get there? How did the bipartisan fiscal problems arise?

Both sides disagree. Many on the other side look at the last two decades of fiscal history and reduce it to two points:

1. All of the "good" fiscal history of the 1990s is attributable to the 1993 tax increase bill; and
2. All of the "bad" fiscal history of this decade is attributable to the bipartisan tax relief plans of 2001 and 2003.

Last year, during the budget debate, I showed this revisionist fiscal history doesn't stand up to scrutiny. The data was drawn from the Clinton Administration's Office of Management and Budget ("OMB") and the Congressional Budget Office ("CBO"). What we do know is that a growing U.S. economy is the best tonic to fiscal ailments.

Fiscal history in the past two decades shows that revenues grow strongly when the economy recovers. That history shows that, with bipartisan tax relief in effect, revenues grew faster than after partisan tax increases.

The two sides disagree on this relationship. It's like the saying about the tail wagging the dog. From our view, the healthy economy is the dog and revenue is the tail.

Too often, the other side views tax increases as a necessary imperative to a healthy economy. Fiscal history shows it to be precisely the opposite.

The division between the two sides in their views of how we got here informs the two sides' views of where we go from here. The President, in his State of the Union address the other night, at one point, indicated that we need to look forward. I couldn't agree more.

In this town, too often the tendency is to grow spending and raise taxes. Seldom do folks look at restraining the growth in spending and the resulting pressure to raise taxes.

Unfortunately, looking at the path ahead, the President's budget proves that point. Appropriations are up 25% over the last two years.

How many families have had the luxury of growing their budgets by 25% over the last two years? How many businesses, large and small, have had that luxury? The answer is American families and businesses have done just the opposite over the last couple of years.

The President talked about a freeze in that spending. And look at the pushback he received from his own Congressional Leadership.

Look at the budget and you find a big fiscal hole. Democrats and Republicans know the hole is there. The President knows the hole is there. Everyone agrees the hole needs to be filled.

Those on the other side, consistent with their view of fiscal history, view the tax side of the ledger, as under-subscribed. The President's budget is consistent with that view. Let's take a look at a few examples of the tax increase bias.

Both sides agree small business is the key to a goal both sides agree on: job creation. Yet, the President's budget raises the marginal rate on small businesses by over 15%.

The Congressional Democratic Leadership would go further. The House health care reform bill would've gone further – raising the marginal rate about 33%. The Senate health care reform bill would've raised the marginal rate by 20%.

Once enacted, either of those bills would take the marginal rates well above the highest rates during the Clinton era.

More dramatic marginal rate increases would fall on investment. For instance, if the House health care reform bill were enacted, it would push the marginal rate on capital income up by almost 70%.

The response from some on the other side is that, because these heavy tax increases are aimed at taxpayers over certain income levels, they would cause no economic harm.

That position, though politically popular, ignores the fact that taxes affect behavior. Economic growth occurs from positive behavior of families, businesses and investors. It is often said that tax cuts aren't free. But, on the other side of the coin, from the viewpoint of those paying the higher taxes, tax increases certainly aren't free either. Some of the group targeted for the tax increase may absorb it, but others will react by changing behavior. Small businesses will be affected. Which means workers, suppliers, and others will be affected. Likewise, if investors shift their money into tax-favored activities, the supply and cost of capital for garden-variety business activities is adversely affected.

What's more, contrary to the rhetoric of many on the other side, it isn't just the top 5% of earners who are singled out for tax increases in the budget. The revenues from the cap and trade program will adversely affect many families below \$250,000 of income. And, the Democratic Congressional Leadership's health care bills both contain tax increases that adversely affect millions of these middle-class families.

Let's take another look at the fiscal hole in the fiscal path ahead. What I'd ask my friends to do is look not just at the tax side of the Federal ledger. Look at the spending side. Think about that every time a new politically-popular entitlement program is proposed. Every new entitlement, every expanded entitlement, every double-digit increase in new appropriations spending is popular with the group targeted for the benefit.

Those who oppose these initiatives are always on the defensive. Somebody has to pay for this spending. That somebody is usually the portion of Americans not targeted for the benefit. In a budget with rising deficits, it means those Americans not targeted for the benefits can expect a future tax increase.

Looking forward, we need to examine the tax policy initiatives in this budget in three phases. They are the short-term, mid-term, and long-term horizons.

In the short term, the President, Democrats and Republicans agree on the basic objective. That objective: jobs, jobs, jobs. Everyone agrees those jobs will come from expansion in the small business sector. What are small business folks saying? They're worried about the business environment. There are higher taxes in that environment.

There may be new mandates in that environment. There are new regulations in that environment. There is a tight credit market in that environment. Since this hearing is about tax

initiatives in the budget, let's focus on the tax environment. Some higher taxes are known, such as the marginal rate increases in the budget before us. Some are possible and to some degree not known. Will the taxes directed at small business in the House and Senate health care bills materialize in that legislation or some other legislation?

My advice to my friends on the other side, from the President on down, is this. Listen to what small business is telling you. Back off the marginal rate hikes. Don't bury recovering small businesses with new taxes and penalties. Be cognizant of the tax burden you are raising on capital. Remember, cash is the life blood of small business. Be sensitive to the credit markets that small businesses are still struggling with.

In the mid term, the first five years of the budget, take a look at how all the fiscal policy, especially the new spending, affects the current and future hidden tax burden.

In the long term, years six through ten of the budget, realize that spending on its current path is unsustainable. It is the explosion of spending, not taxes at or above historical averages, driving those frightening deficit numbers.