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### 1NC—Taxmageddon CP

#### The United States federal government should make current tax policy permanent by eliminating tax hikes scheduled to go into effect on January 1, 2013.

#### Here’s our solvency advocate: the counterplan prevents Taxmageddon—it’s key to the economy.

Foster 12 — J. D. Foster, Norman B. Ture Senior Fellow in the Economics of Fiscal Policy in the Thomas A. Roe Institute for Economic Policy Studies at The Heritage Foundation, former Associate Director for Economic Policy at the White House's Office of Management and Budget, holds a Ph.D. in Economics from Georgetown University, 2012 (“The 2012 Tax Policy Two-Step: Taxmageddon, Then Tax Reform,” Heritage Foundation Issue Brief #3599, May 9th, Available Online at http://www.heritage.org/research/reports/2012/05/2012-tax-policy-two-step-taxmageddon-then-tax-reform, Accessed 07-19-2012)

On January 1, 2013, among other unfortunate tax consequences:

Income tax rates shoot up,

The child credit is cut in half,

The marriage penalty roars back,

The capital gains tax rate goes up,

The dividend tax rate soars,

The payroll tax rate jumps two percentage points,

The death tax is restored to its punitive past,

The Alternative Minimum Tax relief expires, and

A uniquely pernicious additional payroll tax hike from Obamacare takes effect.

Collectively, this would by far be the largest tax hike in history. The effects on families and businesses would be devastating; the effects on the economy no less so.

Congress should make current tax policy permanent and eliminate, once and for all, this cavalcade of tax hikes. At the same time, Congress should repeal Obamacare and in the process eliminate its own panoply of harmful tax hikes. In the event it does neither, Congress should delay these tax hikes for as long as possible—whether one year, two years, or longer.

Nor should Congress wait until after the election to act. Taxpayers deserve more respect from their elected officials than being left in doubt about facing a massive tax hike. The economy also needs better tax certainty. And on this issue, voters in November should be able to cast their votes based not on what Members say they will do but on what they did before the election.

Also, without question Congress should not kick the Taxmageddon can down the road into early 2013, much as it did with the payroll tax hike prevention enacted late last year. Just as taxpayers do not need a massive tax hike, they do not need the oppressive uncertainty of delaying Taxmageddon for a few months into 2013 only to face it again in the spring.

#### And—uncertainty about Taxmaggedon is already tanking the economy—failure to act now ensures another recession.

Dubay 12 — Curtis S. Dubay, Senior Analyst in Tax Policy in the Thomas A. Roe Institute for Economic Policy Studies at The Heritage Foundation, former Senior Associate at PricewaterhouseCoopers and Senior Economist for the Tax Foundation, holds an M.A. in Economics from the University of Connecticut, 2012 (“Taxmageddon Is Slowing the Economy Now,” *The Foundry*—The Heritage Foundation’s blog, June 20th, Available Online at http://blog.heritage.org/2012/06/20/taxmageddon-is-slowing-the-economy-now/print/, Accessed 07-19-2012)

The uncertainty caused by Taxmageddon—the one-year $494 billion tax increase [2] that looms on January 1, 2013—is strong enough to slow the economy months before it actually strikes. In fact, it is already doing so.

Highly knowledgeable and highly influential market observers have been warning Congress of this for weeks. Their goal is to get Congress to do its summer job [3] and stop Taxmageddon.

The first warning came from Mohammed El-Erian, CEO of Pimco, the world’s largest bond fund. Writing in The Washington Post [4], he bluntly told Congress that the longer they wait to stop Taxmageddon, the more likely it is that markets will start to slow.

Then Jamie Dimon, CEO of JP Morgan Chase, echoed El-Erian almost verbatim during his recent testimony to the Senate Banking Committee [5]. He said Congress should not wait until year’s end, because markets will react well before December 31 if they see Congress failing to stop Taxmageddon.

Congress didn’t heed El-Erian’s or Dimon’s warnings, and now it looks like it waited too long.

Eminent economist Irwin Kellner writes [6] that the recent spate of bad economic data—everything from low consumer sales to weak consumer sentiment—is a tell-tale sign that the economy is slowing. And he pins the blame on the uncertainty caused by Taxmageddon.

The uncertainty is slowing the economy because businesses, investors, and entrepreneurs can’t plan for the near future. They can’t because they don’t know what their taxes are going to be in just a few months. If they don’t know what their taxes will be, there is no way for them to determine if their potential job-creating investments would be profitable. Without being able to make that vital calculation, there is no way they can move forward on projects that would speed growth and create much needed jobs. So they’re sitting back, waiting for Congress to provide some certainty.

Congress needs to provide that certainty and stop Taxmageddon as soon as possible. Or risk that its own inaction will cause a return to recession.

## \*\*\* Impacts

### Manufacturing Impact

#### The manufacturing industry is recovering now but uncertainty about Taxmaggedon is stunting growth—the counterplan is the only way to sustain the industry and overall economic growth.

Coleman and Moutray 12 — Dorothy Coleman, Vice President for Tax and Domestic Economic Policy at the National Association of Manufacturers, and Chad Moutray, Chief Economist at the National Association of Manufacturers, 2012 (“Don’t push our economy off a cliff,” *The Washington Post*, July 15th, Available Online at http://www.washingtonpost.com/business/capitalbusiness/dont-push-our-economy-off-a-fiscal-cliff/2012/07/13/gJQAb18tmW\_story.html, Accessed 07-19-2012)

Everyone is talking about manufacturing and its comeback. Politicians, economists and the media continue to focus on the sector’s “renaissance,” primarily because manufacturing has been a major contributor to our economic growth since our nation’s steep economic downturn.

Manufacturers have added 13 percent of the net new jobs gained since the end of 2009, and we have made larger-than-normal contributions to gross domestic product. But there is a black cloud looming with much uncertainty ahead.

It is no secret that our nation is racing toward a fiscal cliff on Jan. 1, with Americans facing tax increases and spending cuts totaling more than $600 billion. Few expect President Obama and Congress to address this issue before Election Day, leaving a daunting list of fiscal and economic issues to resolve during the “lame duck” session. This leaves manufacturers facing uncertainty and makes it difficult to plan for the future. In a recent survey, 64 percent of manufacturers said the tax and regulatory environment is their top concern.

Absent legislation, marginal tax rates for American taxpayers will go up in 2013 to levels not seen since 2001. A host of other tax relief provisions are also set to expire, including tax rates on capital gains and dividends. In addition, some $22 billion in new taxes in the health care law are slated for 2013, including a 3.8 percent surcharge on top incomes.

If these tax increases kick in, the nation risks a recession in the first half of 2013, according to the Congressional Budget Office. The United States already has the highest corporate tax rate in the world, and if the tax relief expires, the two-thirds of manufacturers that operate as “pass-through” entities and pay taxes at the individual rate would face even higher tax bills. With the addition of the new 3.8 percent surcharge, many manufacturers will face marginal tax rates of more than 40 percent.

Pending across-the-board cuts in defense spending will also place a drag on the national and local economies. A new National Association of Manufacturers study found that defense spending cuts will negatively impact manufacturers across the country, including defense contractors and their supply chains. By 2014, the economy would lose more than 1 million private sector jobs, including 130,000 in manufacturing. In addition, GDP would be nearly 1 percentage point lower.

The effects of defense cuts are particularly acute here. Virginia and Maryland are among the top 10 states impacted. Virginia — second only to California — would lose an estimated 114,900 workers in 2014, while Maryland would lose just more than 40,000. Given the planning cycle for defense contractors and their suppliers, the defense industry is already experiencing job losses.

As growth slows elsewhere, the United States should be primed to capitalize on new opportunities around the world. If we effectively deal with our fiscal situation and adopt pro-growth policies that allow us to more effectively compete in the global marketplace, manufacturers across the United States should flourish, creating new jobs and expanding their operations.

By failing to do so, however, policymakers are holding back a move to more durable economic growth and job creation. That is why we need action sooner, rather than later.

### General Economy Impact

#### Failure to end Taxmageddon will tank the economy—best study proves.

Dubay 12 — Curtis S. Dubay, Senior Analyst in Tax Policy in the Thomas A. Roe Institute for Economic Policy Studies at The Heritage Foundation, former Senior Associate at PricewaterhouseCoopers and Senior Economist for the Tax Foundation, holds an M.A. in Economics from the University of Connecticut, 2012 (“Ernst and Young: Obama’s Tax Increase Would Kill 710,000 Jobs,” *The Foundry*—The Heritage Foundation’s blog, July 18th, Available Online at http://blog.heritage.org/2012/07/18/ernst-and-young-obamas-tax-increase-would-kill-710000-jobs/, Accessed 07-19-2012)

A new study conducted by Ernst and Young proves conclusively that the President’s tax increase would be devastating to the economy and jobs.

The study finds that, if Congress misguidedly adopted President Obama’s plan to raise taxes on job creators by allowing the Bush-era tax policies to expire for incomes over $200,000 ($250,000 for married filers), the economy and jobs would suffer terribly:

Output in the long run would fall by 1.3 percent, or $200 billion, in today’s economy;

Employment in the long run would fall by 0.5 percent or, roughly 710,000 fewer jobs, in today’s economy;

Capital stock and investment in the long run would fall by 1.4 percent and 2.4 percent, respectively; and

Real after-tax wages would fall by 1.8 percent.

There are almost 13 million Americans out of work today. President Obama’s tax increase would needlessly add almost three-quarters of a million people to that already much too large number. Even those with jobs wouldn’t escape the pain of President Obama’s tax increase, as they would see their wages suffer.

The report validates Heritage’s argument that President Obama’s tax increase plan would badly hurt job creation because it would fall heaviest on the most successful businesses that employ workers and pay their taxes through the individual income tax (known as flow-through businesses). The study reports:

The concern over higher individual tax rates has also been a focus because of the prominent role played by flow-through businesses—S corporations, partnerships, limited liability companies, and sole proprietorships—in the US economy and that a large fraction of flow-through income is subject to the top two individual income tax rates. These businesses employ 54% of the private sector work force and pay 44% of federal business income taxes. The number of workers employed by large flow-through businesses is also significant: more than 20 million workers are employed by flow-through businesses with more than 100 employees. (Emphasis added.)

President Obama is fond of saying his tax increase wouldn’t impact 97 percent of small businesses. But those 97 percent of small businesses aren’t job creators. They range from people in their basements selling items on e-Bay to lawyers who practice out of their homes.

The businesses that would pay this tax increase are the businesses that hire millions of workers. Higher taxes on these vital job creators could force them to cut back on their existing workforce and would certainly cause them to slow hiring of new workers.

President Obama couches his argument for tax hikes on the rich in terms of fairness. But it would be anything but fair that millions of unemployed Americans desperate to go back to work would find it harder to land a job to provide for their families because of President Obama’s misguided class warfare.

There can be no doubt any more that President Obama’s Taxmageddon tax increase would devastate jobs. The Ernst and Young study should be the final nail in the coffin for his plan in Congress. It is time for Congress to do what’s right and stop all of Taxmageddon today.

#### Taxmaggedon will decimate the economy.

El-Erian 12 — Mohamed A. El-Erian, Chief Executive and Co-chief Investment Officer of the investment management firm Pimco, 2012 (“The fiscal cliff cometh,” *The Washington Post*, May 3rd, Available Online at http://www.washingtonpost.com/opinions/congress-shouldnt-delay-in-addressing-the-fiscal-cliff/2012/05/03/gIQAx3F0zT\_story.html, Accessed 07-19-2012)

Economists are rightly starting to warn that the United States faces a worrisome “fiscal cliff” at year’s end. The blunt spending cuts mandated by the 2011 compromise on the debt ceiling — and the failure of the “supercommittee” that followed — along with across-the-board tax increases would derail the U.S. recovery and undermine the well-being of the global economy. We should be avoiding the edge of this cliff — and politicians should not believe that they have until the end of this year to act.

In the next few months, possibly within weeks, markets here and abroad will be looking for signals that our politicians understand the severity of the situation and are able and willing to act appropriately. If clear signals are not forthcoming, markets could react early to the looming trouble, compounding the uncertainties that weigh on the U.S. economy.

It is well known that both Democrats and Republicans in Congress have failed in the past few years to address our nation’s difficult fiscal issues. The most visible example is the repeated absence of a comprehensive annual budget. Less obvious but equally important is the large and meaningful collection of budgetary reforms that have been delayed, obfuscated and derailed. In the process, all sorts of spending cuts and tax increases got kicked further down the road. Now, a meaningful and consequential set is coming together in a rather disorderly fashion.

The sequestration mandated by the Budget Control Act of 2011 and the reversal of the Bush-era and payroll tax cuts would essentially mean withdrawing from the economy some 4 percent of the national income in one blunt go — and this doesn’t factor in possible knock-on effects. The importance of this issue cannot be overstated. A fiscal contraction of this magnitude and composition would stop dead in its tracks the economy’s nascent healing and job creation. Consumption and investment would be harmed. Foreigners would become more cautious about buying our ever-increasing debt issuance. And with our internal growth momentum weakened, the headwinds from the European debt crisis could prove overwhelming.

#### Prefer our evidence—the IMF’s Chief Economist agrees.

CNBC 12 — CNBC, 2012 (“‘Fiscal Cliff’ Could Trigger US Recession: IMF Economist,” Byline Justin Menza, July 16th, Available Online at http://www.cnbc.com/id/48196003, Accessed 07-19-2012)

Going over the fiscal cliff could cause a U.S. recession next year, Olivier Blanchard, the International Monetary Fund's chief economist, told CNBC’s “Squawk on the Street.”

“If the fiscal were to happen, it would be a major macroeconomic event,” Blanchard said. The fiscal cliff is when a host of tax cuts expire and automatic spending cuts kick in at the end of the year.

Blanchard said the IMF’s 2 percent U.S. economic growth forecast is based on fiscal consolidation of about 1.5 percent of gross domestic product next year, but the fiscal cliff would represent a 4 percent consolidation. “It would probably kill growth in the U.S. next year and probably kill growth in advanced economies,” Blanchard said.

He added, “I think that if the U.S. fell off the fiscal cliff, I’m quite sure we’d see negative growth in the U.S. next year.”

### Job Creation Impact

#### The counterplan is key to job creation.

Dubay 12 — Curtis S. Dubay, Senior Analyst in Tax Policy in the Thomas A. Roe Institute for Economic Policy Studies at The Heritage Foundation, former Senior Associate at PricewaterhouseCoopers and Senior Economist for the Tax Foundation, holds an M.A. in Economics from the University of Connecticut, 2012 (“Obama’s Taxmageddon Tax Increase Would Hurt Job Creation,” Heritage Foundation Issue Brief #3658, July 9th, Available Online at http://www.heritage.org/research/reports/2012/07/obama-s-taxmageddon-tax-increase-would-hurt-job-creation, Accessed 07-19-2012)

Stop All of Taxmageddon

President Obama often states that his plan would raise taxes only on “the rich” to force them to pay their “fair share.” But less job creation as a result of President Obama’s tax increase would make it harder for unemployed Americans at all income levels to find new jobs, and those seeking new opportunities to fully realize their potential would find it harder to find more rewarding positions. Most Americans would find those diminished opportunities anything but fair.

Congress should stop all of Taxmageddon as soon as possible. That means extending the Bush tax cuts for all taxpayers. Stopping a tax increase that would devastate job creation should be a rare occasion for bipartisan agreement and would be a useful way for Washington to prove to voters that it is focused on job creation at a time when almost 12.7 million Americans remain out of work.

#### Taxmageddon will decimate job creation—best study proves.

Dubay 12 — Curtis S. Dubay, Senior Analyst in Tax Policy in the Thomas A. Roe Institute for Economic Policy Studies at The Heritage Foundation, former Senior Associate at PricewaterhouseCoopers and Senior Economist for the Tax Foundation, holds an M.A. in Economics from the University of Connecticut, 2012 (“Obama’s Taxmageddon Tax Increase Would Hurt Job Creation,” Heritage Foundation Issue Brief #3658, July 9th, Available Online at http://www.heritage.org/research/reports/2012/07/obama-s-taxmageddon-tax-increase-would-hurt-job-creation, Accessed 07-19-2012)

Hitting Almost All Income Earned by Job Creators

President Obama’s plan to repeal the Bush tax cuts for incomes over $200,000 ($250,000 for joint filers) would, along with other tax increases, raise the top two marginal tax rates from 35 percent and 33 percent to 39.6 percent and 36 percent, respectively. The debate about whether to adopt the President’s tax increase centers heavily on how these higher tax rates would affect important job-creating businesses that pay their taxes through the individual income tax, known as flow-through businesses.

There is considerable debate about whether flow-through businesses that pay the higher rates are job creators.[3] A report from President Obama’s own Treasury Department provides data that settle the point conclusively.[4] The report parcels out the flow-through business income earned by traditional businesses that employ workers from the income earned by individuals earning business income from side jobs. Such broken-out data did not exist previously.

The distinction the Treasury report makes is important because the individuals that do side jobs report what they earn from their endeavors as business income. They also make up the vast majority of filers with flow-through business income. However, they rarely hire workers.

A few examples of individuals earning side income but not acting in the manner of a traditional business include issue experts writing articles for publications, academics conducting studies or giving lectures, computer technicians repairing computers and other electronic devices, hobbyists selling the products they make, and people selling items on e-Bay.

According to the Treasury study, out of 34.8 million tax returns that claimed flow-through business income, 4.3 million employed workers in 2007 (the most recent year for which data are available). The more than 30 million returns with business income (88 percent of the total returns with business income) that did not qualify as employer-businesses are those individuals earning business income from side jobs.

It is those 4.3 million employer-businesses that matter most when it comes to determining the impact that President Obama’s tax increase would have on job creation. The Treasury report shows that 1.2 million, or 28 percent, of them earned more than $200,000—the income threshold over which President Obama’s tax increase would apply. More important as it pertains to job creation, those 28 percent of businesses earned almost all—91 percent—of the income earned by flow-through employer-businesses.

Obama Tax Increase Would Hit Largest Job Creators

The businesses that earn almost all of the income are the most successful flow-through employer-businesses. That also means they are the businesses that create the most jobs.

Successful businesses are the businesses with the most demand for the goods and services they make and provide. This high demand generates the high incomes that typify successful businesses. To meet that high demand, these businesses need more workers.

By pinpointing his tax increase on incomes over $200,000, President Obama has maximized the detrimental impact that his tax increase would have on job creation. A higher tax bill would deprive the most successful flow-through employer-businesses of resources they would otherwise plow back into their business. These investments would allow them to compete for more business and create more jobs in the process.

Higher marginal tax rates would also reduce the incentive for these important job creators to expand and take on risk with their remaining resources, because the higher rates would reduce the return that the owners of the businesses could expect to earn from their investment. This would further deter job creation.

### Uncertainty Impact

#### The counterplan provides certainty—that’s key to growth.

Huizenga and Genetski 12 — Bill Huizenga, Congressman representing Michigan’s Second Congressional District, and Robert Genetski, economist at classicalprinciples.com, 2012 (“‘No, Mr. President, the private sector is not 'doing fine',” *Detroit News*, July 19th, Available Online at http://www.detroitnews.com/article/20120719/OPINION01/207190338/1008/OPINION01/Commentary-No-Mr-President-private-sector-not-doing-fine-, Accessed 07-19-2012)

The private sector is not doing fine. America's families are not doing fine.

According to a June study by the U.S. Federal Reserve, the average family's net worth dropped by nearly 40 percent between 2007 and 2010. In 2010, median family income fell by 7.7 percent alone. There is no reason to think this trend has reversed itself in the last 18 months. In fact, the evidence may prove just the opposite.

President Barack Obama's agenda based on increased regulation, reckless spending and higher taxes has increased economic uncertainty and created an environment in which businesses are afraid to invest and hire new employees.

Obama repeatedly refers to "revenues" not "taxes," just as he refused to allow Obamacare to be called a tax. That is, until the Supreme Court called his bluff. Taxes are not the same as revenues. The reason is very simple. If you tax Americans at 0 percent, you get no revenue. And, if you tax Americans at 100 percent, you will also get no revenue. Why work if your money will simply be redistributed by Washington? The key is to find the sweet spot, where the government is forced to cut its spending and the people are not overburdened, especially in a recession.

Last month, the Commerce Department confirmed that GDP grew by an anemic 1.9 percent in the first quarter of 2012. The latest monthly jobs report confirmed that private sector growth has stagnated and that job creation is unable to keep up with population growth. Under Obama's failed economic model Americans have been forced to suffer through 41 consecutive months of unemployment above 8 percent, causing millions of Americans to give up looking for work altogether. On top of that, now Obama wants to raise taxes on already struggling small businesses.

With job creators unable to expand and hire, families need all the help they can get. "Taxmaggedon," as it's been labeled, may just prove to be the real 2012 doomsday story.

Stopping this onslaught will take not only legislative will, but a change in occupancy at the White House.

Some pundits assume Obama and Congress will reach a compromise on tax policy. However, given Obama's announcement this week (one that reverses his previous position) to raise taxes on small business owners, there is no reason to believe taxes will be going anywhere but up should Obama be re-elected.

With no third term to face and no repercussions to exercising his veto power, Obama could effectively block any bipartisan tax reform Congress offers that he doesn't approve of.

That is why we support Speaker John Boehner and Majority Leader Eric Cantor's efforts to extend all the current tax rates, and by doing so ensure that no American faces a tax increase during these difficult economic times.

It makes no economic sense to raise taxes on small businesses as millions of Americans struggle to find work. By preempting these scheduled tax hikes, we can add certainty for our job creators and prevent further reductions in family incomes.

#### Uncertainty alone is sufficient to trigger the impact—tax rates themselves aren’t as important.

Stockman 12 — Farah Stockman, columnist for the *Boston Globe*, recipient of the Scripps Howard Foundation national journalism award, graduated Magna Cum Laude from Harvard College, 2012 (“Uncertainty on taxes has a high cost for US economy,” *Boston Globe*, July 17th, Available Online at http://articles.boston.com/2012-07-17/opinion/32695490\_1\_tax-rates-tax-policy-tax-analysts/2, Accessed 07-19-2012)

But one thing that does seem to matter, perhaps more than the tax rate itself, is the frequency with which the tax rates change. In the 1930s — during the Great Depression — tax rules shifted constantly, as the government reacted to the crisis. Since investors could never predict what taxes would be, they delayed new investments rather than make big decisions with too many unknowns. That prolonged the Depression.

Today’s investors are in the same boat. The crash of 2008 prompted a host of new policies, literally overnight. An unpredictable presidential election raises more questions about what tax policy will be.

And even after November, uncertainty looms as both sides vow to fight on to undo whatever the other side has already done. It is no wonder that companies would rather wait for the dust to settle, instead of investing big now.

So this leads to another idea that has been gaining currency lately: That our ailing economy is not due to Democratic or Republican policies, but rather to the epic failure to agree on any policy at all; that the biggest obstacle to an economic recovery is the interminable struggle over how to bring a recovery about.

Last year, three economists — Scott Baker and Nicholas Bloom of Stanford and Steven Davis of University of Chicago — set out to quantify the feeling of uncertainty, and measure its impact on the economy. Using a combination of inputs, such as mention of the word “uncertainty” in news reports and how widely economic forecasts vary, they created an “uncertainty index.” Their findings? Economic policy uncertainty hit a historic high last year.

In an interview last week in Cambridge, Baker showed me his latest “uncertainty chart,” which reached its jagged apex last August during the debt ceiling debate.

He said the psychological weight of uncertainty over taxes might have an ever bigger impact than the taxes themselves. Take the health care bill. “The effect on many businesses might be small, but the hysteria over it makes a large impact,” he said.

Another reason for so much uncertainty these days is the new fad in Congress for passing temporary tax cuts that expire in a matter of years. In 2000, there were 22 such laws, worth about $90 billion. Last year, there were nearly 100, worth more than $4 trillion.

The temporary measures are popular because they are easier to pass, and they look deceptively affordable because budget estimates assume they will not be extended. But they carry an invisible pricetag: far greater uncertainty. Baker and his colleagues estimated that as many as 2.5 million jobs would be created within 18 months if uncertainty dropped back down to what it was in 2006.

Who knows when our leaders will see fit to bring back some kind of clarity? Right now they have left us on the precipice of the economic unknown. But we have been here before, and we’ll be here again. That is just the nature of politics.

“Most economists say, ‘We need more stability. If we could just leave the tax code alone for awhile, governments could plan; businesses could plan,’ ” Thorndike told me. “But they have been saying that for 50 years. That’s just not how American democracy works.”

Politicians always tinker with the tax code. They just can’t help themselves.

#### The counterplan reassures consumers and investors.

Dubay 12 — Curtis S. Dubay, Senior Analyst in Tax Policy in the Thomas A. Roe Institute for Economic Policy Studies at The Heritage Foundation, former Senior Associate at PricewaterhouseCoopers and Senior Economist for the Tax Foundation, holds an M.A. in Economics from the University of Connecticut, 2012 (“Taxmageddon: Massive Tax Increase Coming in 2013,” Heritage Foundation Issue Brief #3558, April 4th, Available Online at http://www.heritage.org/research/reports/2012/04/taxmageddon-massive-tax-increase-coming-in-2013, Accessed 07-19-2012)

If President Obama and Congress fail to act this year, an enormous, unprecedented tax increase will fall on American taxpayers starting on January 1, 2013. The Washington Post called the looming tax increase “Taxmageddon,”[1] and Federal Reserve chairman Ben Bernanke called it a “massive fiscal cliff.”[2]

This impending tax increase is mostly the result of the expiration of many long-standing policies that all expire at the end of 2012. President Obama and Congress should start working together now to prevent this massive tax increase rather than waiting until the end of the year. That would assure families, businesses, and investors that their taxes will not rise sharply as the economy is still staggering to its feet and show the voters that Washington really can get important things done—even in an election year.

## \*\*\* Solvency

### Now Key

#### Enacting the counterplan now is key—every delay undermines confidence in the economy.

Dubay 12 — Curtis S. Dubay, Senior Analyst in Tax Policy in the Thomas A. Roe Institute for Economic Policy Studies at The Heritage Foundation, former Senior Associate at PricewaterhouseCoopers and Senior Economist for the Tax Foundation, holds an M.A. in Economics from the University of Connecticut, 2012 (“Taxmageddon: Massive Tax Increase Coming in 2013,” Heritage Foundation Issue Brief #3558, April 4th, Available Online at http://www.heritage.org/research/reports/2012/04/taxmageddon-massive-tax-increase-coming-in-2013, Accessed 07-19-2012)

Act Soon

Congress and President Obama have developed a penchant for waiting until the very last minute to act on pressing tax legislation. In 2010, they waited until late December to extend the expiring Bush tax cuts for two years. At the end of 2011, they waited again until late December to extend the expiring payroll tax holiday. They should break themselves of this bad habit.

Instead, Obama and Congress should remove the uncertainty clouding jobs and family finances by removing the threat of Taxmageddon now. Businesses, families, and investors need to know as soon as possible that this massive tax increase will not hit them as they awaken on New Year’s Day 2013.

#### Even perception of inaction to prevent Taxmageddon will tank the economy.

El-Erian 12 — Mohamed A. El-Erian, Chief Executive and Co-chief Investment Officer of the investment management firm Pimco, 2012 (“The fiscal cliff cometh,” *The Washington Post*, May 3rd, Available Online at http://www.washingtonpost.com/opinions/congress-shouldnt-delay-in-addressing-the-fiscal-cliff/2012/05/03/gIQAx3F0zT\_story.html, Accessed 07-19-2012)

The worries do not stop here. Never mind that it has been less than a year since the last political circus over the debt ceiling caused an economic slowdown, fueled concerns about a double-dip recession and contributed to Standard & Poor’s downgrading the United States’ sacred triple-A credit rating. Just as few in Washington presumed last year that things would reach that point, few think the fiscal cliff will materialize. After all, the deadline was always meant to act as a catalyst for serious revenue and expenditure reforms — including revamping the federal tax code, streamlining entitlements and realigning incentives to favor production and investment rather than consumption and operational avoidance of U.S. tax jurisdictions. But complacency has continued to reign, leaving the country exposed to unnecessary economic trauma and renewed political dysfunction.

Markets are discounters of the future, and prolonged political inaction is likely to encourage companies to postpone building plants and purchasing equipment and to discourage them from hiring.

All this speaks to the importance of acting now to avoid getting too close to the cliff’s edge. The good news is that quite a bit of technical work has been done in Washington on proper fiscal reform, along with background scenario analyses. Also, I suspect that, in their hearts, most politicians from both sides of the aisle recognize that progress necessitates a series of confidence-building compromises that are in the nation’s interest.

But I fear that, once again, we are more likely to witness dithering and bickering in Washington, accompanied by political posturing packaged in competing election-driven narratives. If these concerns materialize, and I sure hope they don’t, the economy will slow during the summer, rating agencies will again get nervous and the political environment will become even more polarized.

It is unfortunately once again time to fasten your economic seat belts.

### A2: Stimulus Key

#### The counterplan is comparatively superior to stimulus.

Lambro 12 — Donald Lambro, Chief Political Correspondent for *The Washington Times*, 2012 (“‘Pushing Us Off the Fiscal Cliff,” *TownHall.com*, July 11th, Available Online at http://townhall.com/columnists/donaldlambro/2012/07/11/obama\_plays\_class\_warfare\_while\_the\_economy\_gets\_worse/page/full/, Accessed 07-19-2012)

This time, Obama has decided to play a game of chicken with Congress at the end of the year when all of the Bush tax cuts are due to expire. This is the so-called "fiscal cliff" that economists say could push the sluggish economy into another recession if all the tax rates rise to their previous levels at the end of December.

And it's not far from that now, with the Obama economy barely growing last year by a pathetic 1.7 percent and a weak 1.9 percent in the first three months of this year. Slowing economic job growth means slower job growth, and we're seeing it now with three straight months of puny job-creation numbers and a rising 8.2 percent jobless rate.

But instead of addressing this bleak economic reality, Obama decided to play the old class warfare game again. He announced that he would support a one-year extension of Bush's low- and middle-income tax cuts, but not for any higher tax brackets. And the White House warned that if Congress sends him a bill that extends the tax cuts for all income levels, he will veto it.

Obama's threat to let all of the tax cuts rise if he does not get his way left Democrats on Capitol Hill scratching their heads. With less than four months to go before the election, why raise the specter of an across-the-board income tax hike for everyone?

No one in Congress thinks it will act on the expiring tax cuts before Election Day, but Obama was playing a card that only heightens the uncertainty about the economy's future. It is this uncertainty about fiscal policy that has held the economy back, suffocating needed capital investment and expansion.

At the same time, Obama's latest threat is one of the biggest flip-flops in a presidency noted for them. Since he assumed office in 2009, he has made killing the top Bush tax cuts an obsession of his presidency, and he went toe-to-toe with Republicans in 2010 over the issue.

In the end, when the invisible "summer recovery" never materialized and Republicans took control of the House and six seats in the Senate -- and even Democrats said "this is no time to raise taxes" in a weak economy -- Obama caved. He agreed to extend the Bush tax cuts for two more years, acknowledging that higher taxes would hurt the fragile economy.

Now, with the economy once again slumping and flirting with recession, Obama is calling on raising taxes on small businesses, investors, retirees who live off capital gains and dividends, and millions of other Americans who do not consider themselves rich.

But many economists, and some Democrats on Capitol Hill, say an extension of all the Bush tax cuts is called for in a still-anemic economy, at least until a full-scale rate reform can be enacted. Raising taxes now on anyone is out of the question.

Here's what would happen if Obama were to let the tax cuts expire at the end of this year:

The 10 percent income tax rate for low-income earners would return to 15 percent; the 25 percent rate would jump to 28 percent; the 28 percent would rise to 36 percent; and the top 35 percent would soar to nearly 40 percent.

That's only the beginning. The marriage penalty against two-earner couples would rise sharply. Families would see the $1,000 per child tax credit shrink to $500, and the 15 percent tax on dividends and capital gains would increase to 20 percent or more.

Letting these tax cuts expire at the end of December would be a massive body blow to an economy that has never really recovered and is still in terrible shape.

The Federal Reserve has sharply lowered its economic growth forecasts for the rest of this year to a new low of 2 percent, and says unemployment is going to stay in the 8 percent-plus range this year and next.

And yet here is the president telling the nation Monday that the best medicine for a weakening economy is to raise taxes on job creators and capital investment that is the mother's milk of a prosperous economy.

Obama has been campaigning in swing states voicing his own frustration about why his spending stimulus policy hasn't worked.

"(B)ut boy, things are still tough out there. Change hasn't happened fast enough. ... I get frustrated, too," he said in Ohio last week.

The problem isn't Bush's tax policies. If there is any life left in the economy, it is to some degree helped by lower tax rates on a still-struggling nation, trying to get back on its feet.

Obama, whose knowledge of what makes the economy work wouldn't fill a thimble, still thinks that more spending is the cure-all and that tax cuts "drove us into the ditch" and caused all of our present problems.

He should read the report by Harvard economists Alberto Alesina and Silvia Ardagna, who studied stimulus policies in 21 countries undergoing economic problems. Their conclusion: "Fiscal stimuli based upon tax cuts are more likely to increase growth than those based on spending increases."

#### Tax certainty is the best stimulus—comparatively better than the plan.

Taylor 8 — John B. Taylor, Mary and Robert Raymond Professor of Economics at Stanford University, 2008 (“Why Permanent Tax Cuts Are the Best Stimulus,” *Wall Street Journal*, November 25th, Available Online at http://online.wsj.com/article/SB122757149157954723.html, Accessed 07-19-2012)

These results may seem surprising, but they are not. They correspond very closely to what basic economic theory tells us. According to the permanent-income theory of Milton Friedman, or the life-cycle theory of Franco Modigliani, temporary increases in income will not lead to significant increases in consumption. However, if increases are longer-term, as in the case of permanent tax cut, then consumption is increased, and by a significant amount.

After years of study and debate, theories based on the permanent-income model led many economists to conclude that discretionary fiscal policy actions, such as temporary rebates, are not a good policy tool. Rather, fiscal policy should focus on the "automatic stabilizers" (the tendency for tax revenues to decline in a recession and transfer payments such as unemployment compensation to increase in a recession), which are built into the tax-and-transfer system, and on more permanent fiscal changes that will positively affect the long-term growth of the economy.

Why did that consensus seem to break down during the public debates about the fiscal stimulus early this year? One reason may have been the apparent success of the rebate payments in 2001. However, those rebate payments were the first installment of more permanent, multiyear tax cuts passed that same year. Hence, they were not temporary.

What are the implications for a second stimulus early next year? The mantra often heard during debates about the first stimulus was that it should be temporary, targeted and timely. Clearly, that mantra must be replaced. In testimony before the Senate Budget Committee on Nov. 19, I recommended alternative principles: permanent, pervasive and predictable.

- Permanent. The most obvious lesson learned from the first stimulus is that temporary is not a principle to follow if you want to get the economy moving again. Rather than one- or two-year packages, we should be looking for permanent fiscal changes that turn the economy around in a lasting way.

- Pervasive. One argument in favor of "targeting" the first stimulus package was that, by focusing on people who might consume more, the impact would be larger. But the stimulus was ineffective with such targeting. Moreover, targeting implied that increased tax rates, as currently scheduled, will not be a drag on the economy as long as increased payments to the targeted groups are larger than the higher taxes paid by others. But increasing tax rates on businesses or on investments in the current weak economy would increase unemployment and further weaken the economy. Better to seek an across-the-board approach where both employers and employees benefit.

- Predictable. While timeliness is an admirable attribute, it is only one property of good fiscal policy. More important is that policy should be clear and understandable – that is, predictable -- so that individuals and firms know what to expect.

Many complain that government interventions in the current crisis have been too erratic. Economic policy -- from monetary policy to regulatory policy, international policy and fiscal policy -- works best if it is as predictable as possible.

Many good fiscal packages are consistent with these principles. But what can Congress and the incoming Obama administration do to give the economy a real boost on Jan. 20? Here are a few fairly bipartisan measures worth considering:

First, make a commitment, passed into law, to keep all income-tax rates were they are now, effectively making current tax rates permanent. This would be a significant stimulus to the economy, because tax-rate increases are now expected on a majority of small business income, capital gains income, and dividend income.

Second, enact a worker's tax credit equal to 6.2% of wages up to $8,000 as Mr. Obama proposed during the campaign -- but make it permanent rather than a one-time check.

Third, recognize explicitly that the "automatic stabilizers" are likely to be as large as 2.5% of GDP this fiscal year, that they will help stabilize the economy, and that they should be viewed as part of the overall fiscal package even if they do not require legislation.

Fourth, construct a government spending plan that meets long-term objectives, puts the economy on a path to budget balance, and is expedited to the degree possible without causing waste and inefficiency.

Some who promoted the first stimulus package have reacted to its failure by saying that we must now switch to large increases in government spending to stimulate demand. But government spending does not address the causes of the weak economy, which has been pulled down by a housing slump, a financial crisis and a bout of high energy prices, and where expectations of future income and employment growth are low.

The theory that a short-run government spending stimulus will jump-start the economy is based on old-fashioned, largely static Keynesian theories. These approaches do not adequately account for the complex dynamics of a modern international economy, or for expectations of the future that are now built into decisions in virtually every market.

#### Studies prove—tax certainty outweighs stimulus.

Alesina 10 — Alberto Alesina, Professor of Political Economy at Harvard University, 2010 (“‘Tax Cuts vs. 'Stimulus': The Evidence Is In,” *Wall Street Journal*, September 15th, Available Online at http://online.wsj.com/article/SB10001424052748704271804575405311447498820.html, Accessed 07-19-2012)

Politicians argue for increased stimulus spending, as opposed to spending cuts, on the grounds that it would speed up economic recovery. This argument might have it exactly backward. Indeed, history shows that cutting spending in order to reduce deficits may be the key to promoting economic recovery.

In Europe today, the risk of a renewed recession comes not from the spending cuts that some governments have enacted, but from a sovereign debt overhang and multiple bank failures. July's stress tests were not reassuring because they didn't test the exposure of European banks to sovereign debt; had they done so, many banks would have failed. Those banks remain a threat to the European economy.

In the U.S., meanwhile, recent stimulus packages have proven that the "multiplier"—the effect on GDP per one dollar of increased government spending—is small. Stimulus spending also means that tax increases are coming in the future; such increases will further threaten economic growth.

Economic history shows that even large adjustments in fiscal policy, if based on well-targeted spending cuts, have often led to expansions, not recessions. Fiscal adjustments based on higher taxes, on the other hand, have generally been recessionary.

My colleague Silvia Ardagna and I recently co-authored a paper examining this pattern, as have many studies over the past 20 years. Our paper looks at the 107 large fiscal adjustments—defined as a cyclically adjusted deficit reduction of at least 1.5% in one year—that took place in 21 Organization for Economic Cooperation and Development (OECD) countries between 1970 and 2007.

According to our model, a country experienced an expansionary fiscal adjustment when its rate of GDP growth in the year of the adjustment and the next year was in the top 25% of the OECD. A recessionary period, then, was when a country's growth rate was in the bottom 75% of the OECD.

Our results were striking: Over nearly 40 years, expansionary adjustments were based mostly on spending cuts, while recessionary adjustments were based mostly on tax increases. And these results would have been even stronger had our definition of an expansionary period been more lenient (extending, for example, to the top 50% of the OECD). In addition, adjustments based on spending cuts were accompanied by longer-lasting reductions in ratios of debt to GDP.

In the same paper we also examined years of large fiscal expansions, defined as increases in the cyclically adjusted deficit by at least 1.5% of GDP. Over 91 such cases, we found that tax cuts were much more expansionary than spending increases.

How can spending cuts be expansionary? First, they signal that tax increases will not occur in the future, or that if they do they will be smaller. A credible plan to reduce government outlays significantly changes expectations of future tax liabilities. This, in turn, shifts people's behavior. Consumers and especially investors are more willing to spend if they expect that spending and taxes will remain limited over a sustained period of time.

On the other hand, fiscal adjustments based on tax increases reduce consumers' disposable income and reduce incentives for productivity.

American firms today are profitable and have large unspent resources. But their uncertainty over regulation and taxes discourages them from risk-taking, investment and consumption. In Europe, governments would strengthen the banking sector if they cut spending and reduced their default risk. This, in turn, would ease the flow of credit into the private sector.

The composition of fiscal adjustments is therefore critical. Based on what we know, the U.S. and Europe are currently at greater risk from increased stimulus spending than from gradual but credible spending cuts.

Europe seems to have learned the lessons of the past decades: In fact, all the countries currently adjusting their fiscal policy are focusing on spending cuts, not tax hikes. Yet fiscal policy in the U.S. will sooner or later imply higher taxes if spending is not soon reduced.

The evidence from the last 40 years suggests that spending increases meant to stimulate the economy and tax increases meant to reduce deficits are unlikely to achieve their goals. The opposite combination might.