State workers hoping to receive annual pay raises in the coming years will have to wait for the State of Illinois to creep back from the edge of an unprecedented fiscal cliff. That’s the message desperate lawmakers and other officials are sending to Gov. Pat Quinn (D) and 44 public-sector unions as they embark on contract negotiations.

“As we fight to keep facilities open and we fight to fund the pension systems, the state is at the point where any and all additional financial pressures have to be looked at very seriously,” said state Rep. John Bradley (D-Marion). “There is not a magic pot of money that can be found to pay for all the things we want.”

Bradley and other lawmakers were in Chicago recently to consider House Joint Resolution 45, put forth by powerful House Speaker Michael Madigan (D-Chicago) with bipartisan support. It would cap cost-of-living increases for state workers. It also says the size of the state’s workforce is 52% of legislators read Budget & Tax News.

Michigan Acts to Free Workers from Abusive Unions

By Jack Spencer

Bills making Michigan the 24th right-to-work state in the nation passed the state House and Senate on December 11 and were signed later that day by Gov. Rick Snyder (R).

Workers in right-to-work states have the freedom to choose if they want to be members of a union and are not forced to pay union dues or agency fees as a condition of employment.

‘Union Influence Has Fallen’

Michigan is the home of the United Auto Workers union, long a powerful ally of the Democratic Party. The passage of right-to-work legislation in Michigan is a sign of the decline of labor union power, said David Denholm, president of the Public Service Research Foundation, which studies the influence of labor unions on government.

“The very idea that the Michigan legislature could
Michigan Acts to Free Workers from Abusive Unions

Continued from page 1

The legislative action came on the heels of a morning news conference on December 6 that was held by Gov. Rick Snyder, Republican legislative leaders, and union members who support right-to-work. At that news conference, Snyder, Senate Majority Leader Randy Richardville (R-Monroe), and House Speaker Jase Bolger (R-Marshall) expressed support for right-to-work.

In the late afternoon, the bills began moving. House Bill 4054 was passed. Later, Senate Bill 116 and House Bill 4003 were passed by the Senate after lengthy debate. The bills moved to the other chambers for approval and final passage happened on December 11.

Snyder didn’t hesitate about what he would do when a final bill hit his desk, saying when the bill “arrives on my desk, I plan on signing it.” And that’s what he did.

HB 4003 applies to public-sector unions, with the exception of police and firefighters. SB 116 applies to private-sector unions.

Republicans Dominate Vote
In the House, the vote was 58–52, with six Republicans voting “no.” All of the Democrats voted “no.”

In the Senate, the right-to-work legislation passed on a 22–16 vote. Four Republican senators voted “no” along with all of the Democrats.

The Capitol building was jammed with union protesters on December 6. Ultimately the outside doors were locked for security reasons so no more protesters could get in. Those already inside were allowed to stay. Some filled the galleries in the House and Senate chambers and could be heard reacting to the debates.

Lawmakers who voted for right-to-work bills said the protesters didn’t influence them.

“We found [the union protesters] extremely underwhelming. We were expecting a lot more. We were surprised that so few turned out. We knew a lot of those people were bused in. This wasn’t a grassroots effort.”

JEFF FARRINGTON, STATE REPRESENTATIVE, UTICA, MICHIGAN

“We knew a lot of those people were bused in,” Farrington said. “This wasn’t a grassroots effort.”

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If the unions can justify their existence to the workers, they’ll get the workers’ support,” said state Rep. Joe Haveman (R-Holland). “We’re basically saying the unions will have to do the kinds of things we’ve come to expect in the private sector.”

‘Trying to Make State Competitive’
State Rep. Aric Nesbitt (R-Lawton) said the presence and behavior of the protesters didn’t have any effect on him.

“When it comes down to it, we are trying to make Michigan more competitive nationally and internationally,” Nesbitt said. “It all comes down to more and better jobs.”

State Rep. Frank Foster (R-Pellston) said he thinks Michigan GOP lawmakers aren’t likely to be influenced by protesters shouting at the Capitol.

“I think a lot of us saw what happened in Wisconsin,” Foster said. “By comparison it didn’t seem like what happened here today was much.”

‘Support in Union Ranks Dwindling’
“It just tends to show that support in union ranks is dwindling,” Foster said. “We took some tough votes last year and there were protesters here a lot then, too. On this issue we voted on today, we’d done our research. We were confident in our positions.”

Democrats offered several amendments to the bills, including one that would have postponed the legislation from taking effect until 2014 and another that would have made the legislation null and void if Michigan’s unemployment rate didn’t drop by 1 percentage point per year.

Republicans easily rejected all of the attempted amendments.

During the comment period just prior to the final vote on SB 116, Democrats made long statements against the legislation. The longest was basically a filibuster attempt by state Sen. Bert Johnson (D-Highland Park), who read a report that included a summary of the history of labor unions in the U.S. and what appeared to be an anti-right-to-work analysis.

Jack Spencer (spencer@mackinac.org) is capital affairs specialist for Michigan Capitol Confidential, a news service of the Mackinac Center for Public Policy, where a version of this article first appeared. Used with permission.
Illinois Legislature Sends Signal: No Raises

Continued from page 1

not subject to collective bargaining.

On November 28 the House voted 84–29 in favor of the resolution. On December 7 a state judge ruled raises must be paid, but Quinn announced the state would appeal the ruling.

The average cost-of-living allowance during the past five years for Illinois state employees was 4.25 percent, while the Consumer Price Index has averaged an increase of 1.95 percent between 2007 and 2010, according to the resolution.

Governor’s Contracts

The General Assembly may have the “power of the purse,” but it has no say in what goes into contracts. The governor essentially can write checks that lawmakers can’t back.

For example, former governor Rod Blagojevich, now serving time in federal prison for unrelated corruption charges, negotiated in 2002 with the American Federation of State, County and Municipal Employees to reach a 10-year contract that was called one of the “best” public employee contracts in the nation.

“OK, so you got a very good contract, and now we’re in a calamity,” said state Rep. Ed Sullivan (R-Mundelein).

“Our concern from the General Assembly is we can’t afford it. We don’t want to get into more problems where we get sued because we don’t appropriate the money. That’s where we get involved. What’s the answer?”

A Quinn spokesman would not say if the governor would abide by a cap set by the legislature.

“This is a nonbinding resolution, and they took no action on it today. We were there to address questions and share information on immediate fiscal challenges and [the] state of the budget,” said Abdon Pallasch, Quinn’s assistant budget director.

“To be clear, Gov. Quinn’s administration is focused on comprehensive pension reform to restore the system, ensure public employees have access to benefits, and prevent out-of-control pension costs from eating up core services like education and health care,” he said.

‘Will of the House’

Even though it’s a nonbinding resolution, it’s still a message from the General Assembly to the governor and the unions.

“That’s all it is. It’s saying this is the will of the House. Just by holding hearings on it even before the vote on it they’re sending a message,” said Christopher Mooney, a political science professor at the University of Illinois at Springfield, noting the “message” can be cranked up even stronger—by getting the Senate to pass a companion resolution or by passing actual legislation instead of a resolution.

“This is sort of a first step. It’s not just Quinn [that Madigan] is sending a message to. He’s sending a message to both sides in these negotiations. He’s trying to shore up Quinn’s backbone to not succumb [to pressure] and sending a message to the unions saying, ‘Look, if you didn’t notice, we’re pretty broke here and we’re hoping we don’t see any raises come through on this, or any significant raises,’” Mooney said.

Henry Bayer, director of AFSCME Council 31, which represents about 35,000 state workers, said those negotiations occurred through the collective-bargaining process “without any need for any House resolutions about what should take place at the bargaining table.

“We understand the realities. We also understand the budget problems the state is experiencing are not the result of collective bargaining, nor are they the result of unduly enriched state employees,” Bayer said. “The problems our state [is] confronting are due in large part ... to a fiscal collapse that took place in 2008 that we can thank Wall Street and the financial community for.”

Failed Layoffs

Quinn tried to lay off 2,600 AFSCME workers in 2009, but the union successfully sued to stop the layoffs. The two then worked out a plan to defer raises until July 2011 and cut costs through voluntary furloughs and health care savings.

In 2010, Quinn, facing a tough gubernatorial election against Republican state Sen. Bill Brady, brokered a deal with AFSCME that called for no layoffs or state facility closures for two years. In exchange, AFSCME agreed to concessions on salary hikes, health care costs, and furlough days. The concessions amounted to about $400 million.

Quinn hailed it as a breakthrough in negotiations with a union that was not obligated to come to the bargaining table. Brady, however, called it a “scandalous” “pay-to-play” scheme, noting AFSCME endorsed Quinn days after the deal.

Jayette Bolinski (jayette.bolinski@franklincenterhq.org) writes for IllinoisWatchdog.org. Used with permission of IllinoisWatchdog.org.
Higher Gas Tax Unlikely to Gain Support in Congress

By C. Kenneth Orski

Although some infrastructure advocates are hoping to use the current federal budget negotiations to win support for an increase in the federal gasoline tax, the idea is unlikely to gain support in Congress or with the Obama administration.

While the 2010 Simpson-Bowles deficit-reduction commission proposed raising the federal gas tax by 15 cents a gallon as part of a broad deficit-reduction plan, neither House Speaker John Boehner (R-OH) nor Senate Majority Leader Harry Reid (D-NV) has endorsed the idea.

Nor is an increase in the federal gasoline tax popular among their Capitol Hill colleagues. The rank-and-file do not sense a groundswell of public sentiment in favor of a higher gas tax. They see the pressure to raise it as coming from a narrow coalition of liberal advocacy groups and interests that stand to benefit from increased federal transportation spending.

The Obama administration is not eager to advocate a tax increase whose burden would fall most severely on the middle class—precisely the constituency the administration wishes to protect from the pain of any further tax increases. Given this perception, it is almost certain that a federal gas tax increase will remain off the table in the fiscal cliff negotiations and probably in the next session of Congress as well.

More State Responsibility

Instead, look for the states to assume a larger share of responsibility for funding their transportation needs.

An early harbinger may be the state of Arkansas, whose voters recently approved a half-cent statewide sales tax increase to back a $1.3 billion bond issue to fund highway construction over the next 10 years. The measure has been called “the largest infusion of new tax dollars into a state transportation system in recent history” by the Pew Center on the States. There are also signs that some jurisdictions are willing to raise local money to build streetcar lines.

In addition to greater local financial participation, look for a shift from federal funding to public and private financing of large infrastructure projects. The shift will be fueled by a vastly expanded Transportation Infrastructure Finance and Innovation Act (TIFIA) lending authority—by more than 600 percent, from $122 million in FY 2012 to $750 million in FY 2013—and by a large reservoir of equity in pension funds and private infrastructure investment funds looking for attractive investment opportunities.

More Tolling

This means an expanded role for tolling, because TIFIA and private sources of capital can be used to finance only facilities that are backed by a dedicated stream of revenue to cover interest on the loan and repay the loan itself. Tolls are viewed by many as a fairer way to pay for new and reconstructed highways and bridges because, unlike the gas tax, they are paid only by users of the given tolled facility. In other words, drivers in Montana will not be required to pay for a road or bridge built for and benefiting residents of, say, New York.

The likely prospect that financing will replace stagnant or dwindling federal funding dominated discussion among financial practitioners at the American Road & Transportation Builders Association’s Public-Private Partnership Conference in Washington on October 10–11.

TIFIA Loan Interest

Participants were encouraged to hear that 19 projects worth $27.5 billion already have submitted letters of interest for TIFIA loans in the past three months. More applications are certain to follow as it becomes clear the Highway Trust Fund no longer can continue to serve as a source of investment capital for transportation infrastructure.

In sum, rather than hoping for an increase in the gas tax, the transportation community should look forward to three new trends as the most likely response to the perceived inadequacy of current transportation revenue: greater financial participation by state and local taxpayers, a shift from federal funding to private and public financing, and an expanded use of tolling.

C. Kenneth Orski (korski@verizon.net) is editor and publisher of Innovation NewsBriefs, a transportation newsletter. Used with permission of innobriefs.com.
Republican Leaders Offer $800 Billion in Revenue; Other Republicans Balk

By Steve Stanek

House Speaker John Boehner (R-OH) and other Republican leaders in Congress have offered to overhaul the federal tax code to take another $800 billion in taxes over the next 10 years, but some Republican legislators are already saying no to the deal.

Boehner’s leadership team, including House Majority Leader Eric Cantor (R-VA) and House Budget Committee Chairman Paul Ryan (R-WI), have publicly endorsed a plan that would raise the revenue from households that earn more than $250,000 a year—the same group President Barack Obama has repeatedly targeted for higher taxes.

They made the offer to avoid the “fiscal cliff,” which would end the Bush-era tax rate cuts and shrink federal spending beginning in 2013.

The major difference between the Republicans’ and president’s proposals is how the federal government would take additional money. The Republican leaders would do it by extending current tax rates but reducing or eliminating tax deductions and exemptions, thus subjecting more income to tax. Obama and Democrat leaders prefer to raise tax rates.

‘Will Allow More Spending’

Some of the Republican Party’s more conservative legislators almost immediately slammed the Boehner proposal.

“Speaker Boehner’s $800 billion tax hike will destroy American jobs and allow politicians in Washington to spend even more, while not reducing our $16 trillion debt by a single penny,” said Senator Jim DeMint (R-SC) in a statement. “This isn’t rocket science. Everyone knows that when you give politicians more money, they spend it. This is why Republicans must oppose tax increases and insist on real spending reductions that shrink the size of government and allow Americans to keep more of their hard-earned money.”

Democratic Party leaders also were none too keen on the proposal.

“The Republican letter released today does not meet the test of balance. In fact, it actually promises to lower rates for the wealthy and sticks the middle class with the bill,” White House Communications Director Dan Pfeiffer said in a statement. “Until the Republicans in Congress are willing to get serious about asking the wealthiest to pay slightly higher tax rates, we won’t be able to achieve a significant, balanced approach to reduce our deficit.”

In addition to raising taxes on high-income earners, the Boehner proposal would reduce entitlement spending $800 billion over the next 10 years. This would happen by cutting federal health program spending, including by raising the Medicare eligibility age from 65 to 67, and saving $200 billion by applying a lower measure of inflation to all federal programs, including Social Security benefits.

All For Eligibility, Inflation Changes

“I’m all for both increasing the eligibility age for Medicare from 65 to 67, which would just match the eligibility age for Social Security by the way in which it is slowly increasing to age 67, and using the Chained-CPI as a better measure of inflation to tie cost of living increases,” said Jason Fichtner, a senior research fellow at the Mercatus Center at George Mason University who previously served in several positions at the Social Security Administration, including as deputy commissioner of Social Security (acting) and chief economist.

“Chained CPI” refers to a method of calculating consumers’ costs by accounting for substitutions people can make to avoid certain price increases.

Fichtner said it’s important that beneficiaries maintain their purchasing power as prices increase due to inflation and added, “But the measure of inflation is important. The Social Security Act specifies that any cost-of-living adjustment be based on the percentage increase in the Consumer Price Index for urban wage earners and clerical workers: CPI-W. But the CPI-W doesn’t take into account substitution effects.”

“For example, if the price of bananas goes up due to a supply shock, consumers may buy fewer bananas but more apples and oranges,” he explained. “So while the CPI-W would record a higher inflation price for bananas, it wouldn’t take into account the overall switch in the quantity and types of goods purchased, thus over-stating the true measure of inflation. A different measure, the Chained-CPI, takes into account these substitution effects.”

Steve Stanek (sstanek@heartland.org) is a research fellow at The Heartland Institute and managing editor of two Heartland publications, Budget & Tax News and FIRE Policy News.

“Laying Down The Law

Kurtis B. Reeg is a policy advisor for legal affairs at The Heartland Institute and managing partner of Reeg Laywers, LLC. With more than 30 years of trial and appellate experience, Reeg is a frequent speaker at local, regional and national seminars and has published numerous articles.

He has represented clients in a wide variety of products liability, class action and toxic tort litigation, insurance coverage and underlying defense.

His depth of experience — including litigation involving aviation, biotechnology, chemicals, construction equipment, drugs and medical devices, hydraulic equipment, ladders, lead, machinery of various types, mold, pesticides, safety equipment, vehicles, matters related to asbestos, silica, herbicides, chemicals and environmental hazards — makes him uniquely qualified to speak on many legal issues.

To book Reeg as a speaker, or for more information, contact Nikki Comerford (ncomerford@heartland.org), 312/377-4000.
The Heartland Institute is a 29-year-old national nonprofit organization based in Chicago. Its mission is to discover, develop, and promote free-market solutions to social and economic problems. For more information, visit our Web site at heartland.org or call 312/377-4000.

**PolicyBot™** is The Heartland Institute's online database and search engine offering reviews and the full text of more than 25,000 articles and reports from 350 think tanks and advocacy groups.

Alberta has the highest level of economic freedom among all Canadian provinces and U.S. states, according to a new report by the Fraser Institute, Canada’s leading public policy think tank. The “Economic Freedom of North America 2012” report ranks Saskatchewan second among the provinces and third overall. Canadian provinces make up four of the top 10 jurisdictions, with Newfoundland and Labrador and British Columbia coming in ninth and 10th among all provinces and U.S. states.

The report examines key indicators of economic freedom in the Canadian provinces and U.S. states based on size of government, taxation, rule of law and property rights, and regulation, using data from 2010, the most recent year available. A separate chapter compares the economic freedom levels of the Mexican states.


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Freedom from Government
Economic freedom represents the ability of individuals and families to make their own economic decisions, free from government interference.

The study measures economic freedom at two levels: sub-national and all-government (comprising federal, state/provincial, and municipal/local). This year’s report includes a “world-adjusted” index for Canada and the United States at the all-government level using data from Fraser Institute’s “Economic Freedom of the World: 2012 Annual Report,” which ranked Canada fifth of 144 nations and territories, well ahead of the United States at 16th.

“The link between economic freedom and prosperity is clear: Provinces that support low taxation, limited government, and flexible labor markets benefit from greater economic growth,” said report coauthor Fred McMahon in a statement.

In contrast, provinces with reduced levels of economic freedom see lower living standards for families and fewer economic opportunities,” he added.

More Freedom, More GDP
Reinforcing the connection between economic freedom and prosperity, the report shows the Canadian provinces with the most economic freedom (Alberta, Saskatchewan, Newfoundland and Labrador) had an average per-capita GDP of $60,163 (Cdn) in 2010, while the three provinces with the least economic freedom (Quebec, Nova Scotia, Prince Edward Island) averaged only $45,872 (Cdn).

Canadian provinces are ahead of U.S. states in average levels of economic freedom. Overall, Canadian provinces averaged a score of 6.8 out of 10 compared to 6.7 out of 10 for U.S. states.

“The Canadian provinces with the most economic freedom have dynamic, growing economies and offer significant economic benefits for families,” McMahon said.

Economic freedom is based on the cornerstones of personal choice, voluntary exchange, freedom to compete, and security of private property. Research shows people living in jurisdictions with high levels of economic freedom enjoy greater economic growth, higher incomes, more individual freedom, and longer life spans.

The “Economic Freedom of North America” report is an offshoot of the Fraser Institute’s “Economic Freedom of the World” index, the result of a quarter-century of work by more than 60 scholars, including three Nobel laureates.

Source: Fraser Institute


Canadian Provinces Lead North America in Economic Freedom

An Issue for Winners
Under the FairTax, almost everyone is a Winner.

Opponents of the FairTax live in a make-believe world where they try to claim “it will never happen,” or that “it’s a political loser,” but in reality the FairTax is a Winner.

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INTERNET INFO
Fees, Taxes on Wireless Services Keep Climbing

By Matthew Glans

Growing almost as fast as the wireless communications industry are the fees and taxes paid by wireless phone users.

Even as revenue earned per wireless phone falls, taxes and fees climb. In a new report, Scott Mackey of KSE Partners examines the burden these taxes and fees add to wireless phone users’ monthly bills.

Mackey concludes the taxes and fees have climbed steadily, from an average of 16.26 percent of wireless bills in July 2010 to 17.18 percent in July 2012. This amounts to a 5.5 percent increase in burden in just two years.

“Wireless consumers now pay the highest combined tax and fee burden since I began tracking rates in 2003, more than 3 percentage points above the 14.13 percent rate in 2007, which marked the low point for wireless taxes and fees during the last decade,” Mackey wrote.

Mackey found wireless fees were increasing across almost all taxing levels. All told, the average amount that wireless users paid in taxes, fees, and surcharges per month increased from $7.84 to $8.07 from 2010 to 2012.

According to CTIA, an international nonprofit membership organization representing the wireless communications industry, as of June 2012 approximately 322 million wireless subscriber connections existed in the United States alone. Wireless phone services are quickly becoming the primary phone carrier for Americans. About 34 percent of U.S. households are currently wireless-only, and that figure is on the rise.

Surge in Federal Surcharge

Mackey wrote the main culprit behind the increased wireless tax and fee burden over the past two years is the federal Universal Service Fund (USF). Mackey noted rapid growth in the USF surcharge and contends it has grown to where it is hindering development in the wireless industry.

“The federal USF surcharge has nearly tripled over the last decade, from 2.07 percent in 2003 to 5.82 percent in 2012,” he wrote. “In fact, the 5.82 percent federal USF rate in 2012 almost exceeds the combined federal rate imposed in 2005, when the 3 percent federal excise tax still applied to wireless service.”

Mackey concludes the report by recommending against tax increases on wireless services, arguing they slow wireless development. Instead of imposing narrow wireless taxes, he favors broad-based taxes that encourage development of new technology and do not distort consumer choices.

Drag on Wireless Development

“Higher taxes on wireless service, coupled with increased taxes on wireless investments, may lead to slower deployment of wireless network infrastructure, including 4G wireless broadband technologies that an increasingly mobile workforce relies on for economic success,” he wrote. “States should study their existing communications tax structure and consider policies that transition their tax systems away from narrowly based wireless taxes and toward broad-based tax sources that do not distort consumer purchasing decisions and do not slow investment in critical infrastructure like wireless broadband.”

Mackey’s report brought quick reactions from several technology experts. CTIA President Steve Largent said the rising taxes and fees on wireless services have led to the need for substantial communications tax reform. On his CTIA blog, Largent cited Mackey’s report and called for passage of the Wireless Tax Fairness Act.

‘Need Relief’

“This is a truly troublesome trend, which is why we are advocating for the U.S. Senate to pass the Wireless Tax Fairness Act (S. 543). The U.S. House already passed the bipartisan bill last year, but we need the Senate to do the same so millions of wireless customers can get some much needed financial relief,” Largent wrote.

The Wireless Tax Fairness Act would put a five-year moratorium on discriminatory state wireless phone and data service tax increases. While the moratorium wouldn’t prevent governments from creating new taxes and fees on all communications, it would disallow them from targeting any one service.

A five-year freeze would slow the rate of tax increases while allowing for more time to create a new taxing system for wireless that is more carefully developed, fair, and non-disruptive, according to CTIA.

Matthew Glans (mglans@heartland.org) joined the staff of The Heartland Institute in November 2007 as legislative specialist for insurance and finance. In 2012 Glans was named senior policy analyst.
Amendment to Defense Bill Could Sneak in Internet Tax

By Matthew Glans

A bill to fund the U.S. military could end up allowing states to tax consumer purchases made over the Internet. An amendment to the National Defense Authorization Act that Sens. Richard Durbin (D-IL) and Mike Enzi (R-WY) have introduced during the lame duck session of Congress would add their Marketplace Fairness Act proposal to the bill. If passed with the amendment, the bill would allow states to collect sales tax on Internet purchases, even if an online retailer has no physical presence in the state.

The response from Internet sales tax opponents was swift.

“This proposal, and other online sales tax collection proposals like it, would allow states to penalize the innovative e-commerce business model by targeting small online businesses as convenient sources (and collectors) of revenue,” said Ed Black, president and CEO of the Computer & Communications Industry Association, in a statement.

‘Nexus’ Obstacle
One of the main arguments against proposals like the Marketplace Fairness Act is that it violates the U.S. Supreme Court’s 1992 decision in Quill Corp. v. North Dakota, which held a state must prove a company has “substantial nexus” in the state before taxes can be imposed. Since this ruling the nexus or “physical presence” standard has blocked imposition of tax collection requirements on out-of-state retailers.

“Severing the relationship between taxation and physical presence would be a fundamental transformation in how we consider taxes,” Black said. “Such a significant step deserves more extensive consideration than attachment to the unrelated Defense Authorization bill.”

He added, “What we need are pro-growth policies that foster innovation and progress—rather than protecting existing business models at the expense of consumers and growth.”

Supporters of online taxes argue they are needed to restore a balance between online and bricks-and-mortar retailers.

Governor’s Support
In a December 3 column in the Rapid City Journal, South Dakota Gov. Dennis Daugaard wrote, “Online shopping has given every South Dakotan access to more goods and services than ever before, if they are willing to pay for shipping. There is nothing wrong with this. We should not, however, disadvantage our local retailers or our state budget by allowing out-of-state online businesses to avoid paying sales tax.

“We need Congress to act, and I support congressional efforts to simplify and standardize remittance of sales taxes collected from online purchases,” Daugaard continued.

Eliminating the physical presence standard would undermine tax competition and place an undue burden on consumers and businesses, said Steve DelBianco, executive director of NetChoice, a coalition of trade associations, e-commerce businesses, and online consumers.

“The ironically named Marketplace Fairness Act creates unique new tax burdens on e-commerce sellers, unfairly advantaging big box retailers and e-commerce juggernaut Amazon.com,” DelBianco said in a statement. “Those established power players will further extend their market dominance while their customers and small Internet retailers will be left holding the bill.”

Matthew Glans (mglans@heartland.org) joined the staff of The Heartland Institute in November 2007 as legislative specialist for insurance and finance. In 2012 Glans was named senior policy analyst.

IN OTHER WORDS...

“Illinois has a reputation for being an expensive and difficult place to do business, a big reason why the state has the ninth-highest unemployment rate in the country, higher than every state that borders it. Employers want to locate where they are welcome.

“So you might expect that the people who write laws in Illinois—land of 8.8 percent unemployment, $96 billion pension debt, $8 billion in unpaid bills—would be falling all over themselves to welcome business.

“Think again.

“Last week, the Illinois Senate narrowly passed a bill that would require publicly traded companies doing business here to release how much they pay in state income taxes. The sponsors suggest that something sinister must be going on, because many companies don’t pay state income tax. ...

“If companies have earnings in Illinois and they’re not paying state tax on those earnings, we suppose two things could be going on.

• They could be committing fraud. This is why you have prosecutors.

• They could be availing themselves of tax laws enacted by the Illinois House and Senate to persuade them to do their business here.

“Does the latter come as a shock to the sponsors of the Senate tax-disclosure bill, that businesses would take advantage of the laws they passed?”

— Chicago Tribune editorial, December 3, 2012
“Good tax systems are stable and predictable. From the beginning, however, the Bush tax cuts made policy less predictable because the tax changes were set to expire at the end of 2010.”

By Matthew Mitchell and Andrea Castillo

Critics of the Bush tax cuts often dismiss the tax changes as a failed experiment in free-market economics. Noting economic growth was slower in the years following the cuts than in the years preceding them, some critics see the experience as evidence that tax cuts simply do not work.

But the claim that these tax cuts exemplified free-market economic thinking is baseless. The Bush tax cuts had a number of problems from a market-oriented perspective: They were phased in slowly, set to expire within a decade, entailed a Keynesian emphasis on stimulating aggregate demand, and—above all—were undertaken without any effort to reduce spending.

In light of these problems, there is no reason to overturn decades of theoretical and empirical research supporting the link between low taxation and growth. The episode offers a cautionary lesson in how not to cut taxes.

Staggered Reforms


The 2001 tax cut immediately reduced marginal income tax rates, but by a small amount. Each of the top four rates was reduced by 0.5 percentage points in the first year. In 2002, a new bottom marginal rate reduced the tax applied to the first several thousand dollars of income from 15 percent to 10 percent.

As originally designated in the 2001 law, all tax changes were scheduled to take effect by 2006. The top marginal income tax rate was to have fallen from 39.6 percent to 35 percent, while the bottom rate was to have fallen from 15 percent to 10 percent.

The 2003 tax cut accelerated this process and immediately implemented income tax rate reductions that had not been scheduled to take effect for one to three more years. In addition, the 2003 law immediately cut the top marginal capital gains tax rate for assets held more than a year from 20 percent to 15 percent and the bottom long-term capital gains rates from 8 and 10 percent to 5 percent (and eventually to 0 by 2009).

In addition to reducing marginal tax rates, each tax cut also included a number of additional provisions. The 2001 tax cut, for example, included a one-time retroactive “tax rebate.” The Treasury sent checks (up to $300 for singles and $600 for married couples) to taxpayers who had filed their taxes in 2000. It also increased the standard deduction for joint filers, expanded the per-child tax credit, increased the tax credit for qualifying child care expenses, introduced a new deduction for qualified property owners, and created or expanded various education credits and deductions. The 2003 cut accelerated the implementation of these provisions as well.

Despite the shortcomings of these tax cuts, there is strong theoretical and empirical support for low taxation. Keynesian models, for example, emphasize the short-run benefits of tax cuts, stressing that they put money in the pockets of consumers and in the accounts of businesses. According to the Keynesian view, this increases purchasing power and boosts aggregate demand.

The “real business cycle” school of thought, on the other hand, focuses on the longer run and emphasizes that low marginal tax rates tend to increase peoples’ incentives to work and save, increasing aggregate output.

Finally, growth models teach us that lower and more uniform rates can improve long-run economic growth because high tax rates can be an impediment to investment in research and development, and because tax policies that favor one sector over another can drive labor and capital (including human capital) into less-taxed but lower-productivity sectors.

Problems Unpredictability

Good tax systems are stable and predictable. From the beginning, however, the Bush tax cuts made policy less predictable because the tax changes were set to expire at the end of 2010.

This automatic expiration date was an unfortunate consequence of the fact that the tax changes were passed under a legislative procedure known as reconciliation. Since it was unclear that his allies in the Senate could procure the 60 votes necessary to enact the 2001 tax cut, President George W. Bush decided to use reconciliation because it permits budget legislation to pass the Senate with a simple majority of senators.

However, there was a catch. The Byrd Rule, adopted in 1985, prohibits the use of reconciliation to pass legislation that increases the deficit beyond a 10-year term. Because the 2001 and 2003 tax acts made no serious effort to cut spending, the cuts were projected to add hundreds of billions of dollars to the deficit. Thus they had to expire at the end of 2010. The Tax Act of 2010 gave the rates another two years of life, but their looming expiration at the end of 2012 now constitutes one part of a “fiscal cliff” that threatens to tighten fiscal policy in the first part of 2013.

Tax cuts with expiration dates have two deleterious longer-run effects.

First, expiration dates diminish the potency of tax cuts by discouraging some investments at the margin that would have taken place if lower tax rates had been promised for a longer period of time. For example, longer-term investments—in new employees, new equipment, or new facilities—would have looked more attractive if rates hadn’t been scheduled to increase in a few years.

Second, sunset provisions may increase poli-
economic benefit. They found that fewer than 25 percent of households increased consumer spending because of the rebate. Most survey respondents used the tax rebate to pay off debt rather than spend more.

The most significant problem with the Bush tax cuts was that they were not matched with spending cuts. In fact, Washington went on a historic spending binge: From 2001 to 2009, federal spending leapt from 18.2 to 25.2 percent of GDP. This was the largest such increase in any eight-year period since World War II.

In contrast, eight years after the so-called Kennedy tax cuts, spending as a share of GDP had increased just 1.1 percentage points, and eight years after the Reagan tax cuts, spending as a share of GDP had actually fallen 1.1 percentage points.

A tax cut without a spending cut can raise two problems, one involving economic incentives, the other political incentives.

A tax cut without a spending cut is not a tax cut; it is a tax deferral. To the extent that people are forward-looking and can see that deficits require future tax hikes, they will forgo current consumption in order to save for the inevitable tax increase. In this case, government borrowing will crowd out, or displace, private consumption and investment, reducing the effectiveness of the tax cut.

The idea that humans are perfectly forward-looking may strike some as implausible. And indeed, there is a great deal of economic debate about this theory.

‘Fiscal Illusion’

Unfortunately, to the extent that people are not forward-looking, a tax cut without a spending cut raises a completely different problem, this one involving political incentives. In this scenario, shortsighted voters can be deluded into thinking government spending is less expensive than it really is.

This idea, originally developed by Italian economist Amilcare Puviani, is known as “fiscal illusion” and has become a central part of the research program of Nobel laureate James Buchanan. Buchanan contends the opaque nature of deferred taxation causes people to improperly discount the cost of government services and therefore to demand more of them than they normally would.

This phenomenon causes bad policy to beget more bad policy; poorly considered tax reform entices voters to demand more government services, which will need to be paid for with much higher taxes in the future.

Buchanan’s emphasis on fiscal illusion challenges an argument for tax cuts that is often associated with another free-market Nobel laureate, Milton Friedman. This is the idea that a tax cut deprives government of resources, which “starves the beast” and eventually reins in spending.

Among policy pundits, Friedman’s view is much better known than Buchanan’s view. Nevertheless, the data seem to support Buchanan’s view. At the federal level, where the government is allowed to finance operations by borrowing, tax cuts seem to have done nothing to restrain the government’s ability to spend.

Partial Bill, Bigger Government

Moreover, empirical research analyzing U.S. quarterly data from 1959 to 2007 by West Virginia economist Andrew T. Young suggests the fiscal illusion effect is real: When voters are not presented with the bill for big government, they demand bigger government. David and Christina Romer recently corroborated Young’s finding using a different data set and different techniques.

Even if we ignore the Great Recession, economic growth averaged just 2.5 percent in the 26 quarters following passage of the 2001 tax cut. To put this in perspective, economic growth had averaged 3.7 percent in the 26 quarters preceding the cut.

Proponents might well respond that growth would have been worse in the absence of the tax cuts, and the truth is that we will never know what would have happened had they not passed. To complicate matters, many other policies—from trade to regulation to monetary policy—became decidedly less market-oriented in the first decade of the twenty-first century, and it is not easy to disentangle the effects of these policies from each other.

What we do know, however, is that the tax cuts themselves were theoretically flawed. They were phased in slowly, expired quickly, focused inordinately on boosting aggregate demand, and—most significantly—synchronized with massive spending increases, all of which made them less effective.

This episode also reveals that government cannot be contained by tax cuts alone. As long as policymakers have the option of financing their programs with deficit spending, taxpayers will underestimate the true cost of government programs and the “beast” will continue to grow while adding to future tax burdens.

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"At the federal level, where the government is allowed to finance operations by borrowing, tax cuts seem to have done nothing to restrain the government’s ability to spend.”
Scranton Commuter Tax Faces Widespread Opposition

By Eric Boehm

Hard-up for cash to meet growing employee costs and swelling debt payments, the city of Scranton, Pennsylvania is hungrily eyeing the paychecks of workers who don’t live in the city.

If a three-judge panel in Lackawanna County Court gives its consent, Scranton will move ahead with a plan to tax the income of individuals who work in the city but live beyond its borders.

Alexander Chelik says the whole thing reminds him of that famous phrase from the American Revolution.

‘Taxation Without Representation’

“One of the principles that our country was founded upon was no taxation without representation,” said Chelik, the longtime mayor of Mayfield, a borough of 1,800 residents located about 15 miles north of Scranton.

Chelik is leading the opposition to the proposed tax, which he says is little more than a cash grab by a city that has eaten through its own revenue and is now scavenging for more tax dollars by going after commuters.

“[Commuters] have no say in the running of the city government, and now the city wants to impose a tax on them to bail them out,” he said.

Scranton is operating under the state’s program for fiscally distressed municipalities, known as Act 47, and state officials agreed to include the new tax in a recovery plan that was approved for the city last August. The city also must win approval from Lackawanna County Court, where it will argue the commuter tax is necessary because all existing tax revenue has been tapped out.

The 1 percent earned-income tax on people who work in the city but live elsewhere is expected to generate about $2.5 million in 2013 and $4 million in 2014 and 2015. The city will have to go before the court each year to get permission to impose the tax.

The earned-income tax on city residents will remain unchanged at 3.4 percent in the proposed 2013 budget. The city’s real estate taxes are set to increase by 12 percent.

Strong Business Opposition

A survey of more than 700 businesses conducted by the Greater Scranton Chamber of Commerce found 84 percent opposed the new tax.

“The imposition of the commuter tax will make it more difficult to recruit employees and more expensive to keep them,” Austin Burke, president of the chamber, said in a letter sent last month to Scranton Mayor Chris Doherty.

Doherty did not return calls for comment, though he told the Scranton Times-Tribune “we’ve raised taxes everywhere” and defended the commuter levy as a “temporary tax.”

Scranton’s proposed budget for 2013 is $109 million, up from $85 million this year. The increase is mostly the result of a $17 million court-ordered arbitration settlement with the city’s police and fire unions and a $4 million increase in contributions to the city’s pension fund.

The city is more than $300 million in debt, including a $113 million unfunded pension liability.

Eric Boehm (eric@paindependent.com) writes for the Pennsylvania Independent, where a version of this article first appeared. Used with permission.
Fantasies Filling the Heads of San Antonio Streetcar Backers

By Randal O'Toole

The idea that an expensive nineteenth-century technology will help meet the transportation and economic development needs of twenty-first-century urban areas makes sense only in a fantasy world where cost is no object and transport consumers are so hypnotized by shiny steel wheels on steel rails that they ignore the huge inherent disadvantages of a fixed-guideway system that doesn’t go where people want to go, takes a long time to get to where it does go, and can’t get out of its own way in the event of any kind of a problem.

Yet that’s what’s afoot in San Antonio, Texas. Plans to build streetcar lines in San Antonio are based on several critical fallacies, including claims that streetcars are superior to buses in their ability to attract riders and that streetcars promote economic development. In fact, streetcars are slower, less flexible, less capable of moving large numbers of people, and far more expensive than buses.

The biggest argument for streetcars is that they promote economic development. This is mainly based on the experience in Portland, where officials claim a streetcar generated billions of dollars of economic development. In fact, that development was attracted by roughly a billion dollars worth of tax breaks, development was attracted by roughly a billion dollars of subsidies while the other received none other than the streetcar.

According to the city’s own tally, the first neighborhood received more than 75 times as much investment as the second. Clearly, it was the subsidies, not the streetcar, that attracted the new development. City officials who think a streetcar alone will generate new development have been misled.

Streetcars impose huge costs on taxpayers. Cities with streetcar lines spend three to four times as much to operate a streetcar one mile as they spend on buses. Far from moving large numbers of people, most streetcars actually carry fewer people, on average, than the average buses in those cities, and the cost of moving one person one mile is two to seven times greater by streetcar than by bus.

Low-Capacity Transit

Though streetcar advocates like to call streetcars “high-capacity transit,” they are actually one of the lowest-capacity forms of transit available. So-called modern streetcars can move only about 2,000 people per hour, most of them standing. By comparison, standard 40-foot buses can move well over 6,000 people per hour through city streets, all of them comfortably seated.

Double-decker buses are now available that can double this throughput without occupying any more street space. Claims that streetcars have some kind of a “rail advantage” that attracts travelers who won’t ride a bus are purely hypothetical. If there are people so snobbish that they will ride public transit vehicles only if those vehicles are on rails, taxpayers shouldn’t be asked to subsidize them.

As a practical matter, transit ridership is more sensitive to frequency, speed, and convenience than to whether tires are made of rubber or steel, and buses can operate faster, more frequently, and to more destinations than streetcars. So it is no wonder that, of seven cities with streetcars in the United States, the only two where streetcars attract more riders per vehicle mile than buses can do so only because they offer most or all streetcar rides for free to the riders.

Farebox Fantasies

Ridership projections for San Antonio streetcars assume the line would attract the average number of riders per mile carried by streetcars in the seven other American cities that have them. But the projections also assume streetcar fares would cover 15 percent of operating costs. The projections ignored the fact that most of the streetcar lines that attract large numbers of riders charge no fares, and that farebox revenues cover only 8 percent of the costs of operating the seven existing streetcar lines.

Streetcars don’t even have the virtue of saving energy or reducing air pollution. The average streetcar line today uses twice as much energy to move someone one passenger mile as the average car. In places such as Texas, where a major portion of the electricity used to power streetcars comes from burning fossil fuels, the streetcars end up causing more pollution per passenger mile than cars.

Stagnant Streetcar Technology

Proponents of streetcars often object to the description of streetcars as a nineteenth-century technology by saying automobiles are also a nineteenth-century technology. Yet automotive technology has advanced considerably since 1900, while streetcar technology has not.

For example, in 1900, motorcars had a top speed of about 15 miles per hour; today, people routinely drive five times that fast. By comparison, in 1900 streetcars traveled at average speeds of about 8 miles per hour, about the same as streetcars today.

Streetcars are an obsolete technology that does not belong in modern cities. They do not promote mobility; they do not promote economic development; they do not protect the environment. San Antonio should reject the idea of building a streetcar line.

Randal O'Toole (rot@cato.org) is a Cato Institute senior fellow working on urban growth, public land, and transportation issues and author of “The Streetcar Fantasy,” released by The Heartland Institute in December 2012.

INTERNET INFO

Education Funds Being Wasted on Master’s Degrees

By Ashley Bateman

Although research finds no link between master’s degrees in education and better instruction, states spent nearly $15 billion in the 2007–08 school year on this “master’s degree pay bump,” according to a summer report. “The Sheepskin Effect and Student Achievement” puts numbers to a long-studied difficulty. Though some research has shown the instruction of math and science teachers improves when they earn a master’s degree, 90 percent of teachers who hold master’s degrees are no more effective than those without them.

The economic research demonstrating this has been clear for a long time, says Jason Richwine, a Heritage Foundation senior policy analyst. “The real contribution [the report] adds is it quantifies how much money is actually being spent on the master’s [pay] ‘bump,’” Richwine said. “We’ve known for a while that the master’s degree is not a useful thing for the teachers to get. It’s making education reform a bipartisan issue.”

The pay bump artificially increases the number of master’s degrees, the authors found, and soaks up funds school districts could use on measures that increase student performance. Districts also often pay extra to reimburse teachers for graduate school tuition, but the authors found teachers did not earn enough to offset their master’s degree costs.

Huge Spending Spike

Report authors Raegen Miller and Marguerite Roza first studied master’s bumps in 2003–04, finding they caused districts nationwide to allocate an extra $8.6 billion. Since then, that extra spending has grown 72 percent.

“What was most startling to me was how much it grew in the time span [from when] we did the first analysis to the second,” Roza said. “We’ve always known it’s been a problem, and while we ignored it, it doubled.”

A recent influx in master’s degree earners means states have continued to pour money into step pay systems, which compensate employees according to length of service and credentials. “Right now what we do is precisely backwards,” said Marcus Winters, a Manhattan Institute senior fellow and author of Teachers Matter. “We have a system that makes it difficult to become a teacher and then we compensate them based on credentials and years in the classroom, versus how effective a teacher actually is.”

Instead of requiring years of teaching credentials statistically proven to be useless, Richwine said teacher training should focus on apprenticeships. These have proven more effective and less costly, he said.

‘Appetite’ for Reform

“Right now, with constrained resources [there is] lots of appetite for doing things differently … to make a tradeoff on what really matters,” Roza said. Illinois, Oregon, and other states are working to pinpoint wasted spending and improve funding decisions after viewing the first report’s results, Roza said. “Many [teacher training institutions] felt threatened at the potential incentive to end teachers’ getting a master’s degree,” she said. “This time around it seems like states have a big push to improve education.”

Ashley Bateman (bateman.ae@googlemail.com) writes from Williamsburg, Virginia. This article first appeared in School Reform News and is reprinted with permission.

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Concerns over the perilous financial condition of the U.S. Postal Service have caused observers, including Postmaster General Patrick Donahoe, to compare the agency’s prospects to the spiraling economic crisis in Greece.

While the scope of the problem warrants the comparison and its finances are unsustainable without genuine reform, the Postal Service’s reaction to its bleak budgetary prospects offers some encouragement, according to a new study from the Tax Foundation.

“Although the postmaster general has made the Greek analogy only a few times in passing, the topic is worth considering in more detail,” said Tax Foundation Fellow Michael Schuyler. “Greece’s disastrous experience holds valuable lessons, applicable to the Postal Service, regarding the dangers of large and persistent deficits and the desirability of addressing financial problems sooner rather than later.”

**Already in Default**

Even without the postmaster general’s comments, the Greek analogy would have come to mind on August 1, when the Postal Service defaulted on a $5.5 billion contribution to the Retiree Health Benefits Fund.

The USPS also maxed out its credit line at the U.S. Treasury in September, reaching its statutory borrowing limit of $15 billion. The USPS has warned it will be perilously short of cash throughout 2013, meaning if receipts are even slightly below expectations or costs above, it may be unable to pay workers and suppliers promptly and in full.

A further blow landed on November 15, when the Postal Service reported it lost $15.9 billion in 2012. The deficit consists of the August and September payments on which it defaulted plus $4.8 billion of other losses.

Thankfully, the Postal Service’s problems are less serious and easier to solve than Greece’s.

**‘Attempting Self-Sufficiency’**

“Postmaster General Donahoe used the Greek analogy to help people understand the peril to mail users if the Postal Service were to resist the operational changes needed to control its costs,” said Schuyler. “Although some of the service’s proposals are open to criticism, it is to be praised for firmly rejecting the Greek approach and, instead, attempting proactively to return to financial self-sufficiency.”

In his report, Schuyler writes: “In three welcome respects, the Service is in much better shape than Greece. First, it has not attempted to deny or soft-pedal its problems. The plunge in mail demand that began in 2007 due to intensified electronic diversion and the severe 2007–2009 recession took the Service and most of the postal community by surprise, but the Service quickly saw and acknowledged what was happening and began adjusting its operations to the drop in mail volume.”

He also notes the USPS has shrunk its workforce 30 percent from 1999 to 2011, primarily through attrition and buyouts, while maintaining acceptable service quality. Greece until recently had been loath to adopt major workforce reductions.

And, writes Schuyler, the USPS losses “almost look good compared to the financial imbalances in Greece.”

Richard Morrison (morrison@taxfoundation.org) is manager of communications at the Tax Foundation.
**Sucker Bait:**
**Tax Rate Cuts for Lost Deductions**

By Jon Basil Utley

Mitt Romney’s campaign musings about how he would cut income tax rates by 20 percent (when half of Americans don’t even pay federal income taxes) has now floated the ultimate loser for all taxpaying Americans.

This is a $17,000 limit per person for all deductions including mortgage interest, charitable, and state taxes. The concept was first floated by President Barack Obama to limit charitable deductions to a maximum rate of 28 percent for high-income taxpayers, even though marginal tax rates are at 35 percent and may go to 39 percent at the end of this year. Once the principle is established to curtail deductions, future Congresses can then cut them more and more.

This was the Left’s attempt to get the camel’s nose under the tent, that is to start curtailing deductions, especially for large charitable and educational foundations. They have quickly jumped to note “bi-partisan” support for their agenda. “Romney is now admitting that middle-class tax increases on housing, health care and charitable deductions are on the table,” said Adam Fetcher, a spokesman for Obama.

### Safer than Rate Cuts

Deductions, the large ones left, are for home mortgage interest, state income taxes, and charitable deductions. They are supported by all sorts of interests. These include employees of non-profits, homeowners, residents of high income tax states such as New York and California, charities, real estate brokers, and a host of other Americans. Raising tax rates on the wealthy (over $200,000 income) is opposed only by a minority of Americans who actually pay these taxes.

Examples of higher rates after losses of deductions are legion. Former Presidents Bush 41 and Clinton raised rates after President Reagan cut out deductions supposedly in return for lower rates. Bruce Bartlett details the recent history in his book, *The Benefit and the Burden*. He writes how Reagan reduced the top rate to 50 percent and then, with the Tax Reform Act of 1986, took away many tax preferences in return for reducing the rate to 28 percent.

Subsequently George H.W. Bush raised the top tax rate to 31 percent and Clinton then raised it to 39 percent, but the tax preferences were not reinstated. With the next financial crisis rates could easily be put back to 50 percent. Although most of the agenda for higher taxes comes from the Left, a contingent of Republicans also supports higher taxes if the money goes for more “defense.”

As an aside to the above, Bartlett explains a forgotten feature of Clinton’s tax increase to 39 percent during the prosperous 1990s. Obama’s proposal to copy it is widely praised now as showing that higher taxes don’t affect economic growth. Clinton increased the threshold at which the highest rates kicked in from $80,000 to $250,000 of yearly income. In effect this meant there was no increase for most taxpayers.

### Threat to Non-Profits

There is another major tax attack coming on non-profits—that is, charitable and educational foundations and their think tanks. These vast sources of wealth are looked upon more and more hungrily by Washington’s taxers.

A good analogy is during medieval times when Europe’s kings desperately needed more money for their wars. They looked and saw church lands and monasteries as a vast source of untaxed wealth. It took them a while but soon they had seized such lands in most of Europe. The formerly wealthy Catholic Church never recovered its former power.

Although most Americans would think of charity, medical research, theaters, and schools as primary beneficiaries of tax-deductible donations, political education is the area most vital to maintaining our freedoms from the warfare-welfare state. Think of the Cato Institute, the ACLU, the Federalist Society, the Bill of Rights Institute, The Heritage Foundation, Brookings, the Hoover Institution, and the new state think tanks.

Tax-deductible donations and bequests at death to these non-profits and hundreds of others like them allow independent sources of wealth to challenge and (sometimes) limit government abuse and power. They don’t exist in most foreign nations precisely because governments don’t like them, so there is no tax deduction for supporting them. They are much of the reason we have preserved most liberties in America.

If Romney had won election and then become unpopular during the difficult times ahead, it’s quite possible he’d have had a Democratic Congress in 2014.

Then we’d have had the most toxic tax alliance, as history has proven time and again: a weak Republican president without strong anti-tax convictions and a Democratic Congress pushing him to approve their agenda. Think about how this already happened with former presidents Nixon, Bush 41, and Gerald Ford, or Bush 43, who caved in with a Medicare expansion, educational programs, and other big-government agenda line items.

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**Commentary**

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**Tax Rate Cuts for Lost Deductions**

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*Used with permission of The American Conservative.*
Rhode Island Treasurer Gina Raimondo joked that whenever she felt especially discouraged about Rhode Island’s problems, looking at Illinois always made her feel better.

R.I. Pensions Reformer Offers Lessons to Illinois

By William Bergman

In 2009, Gina Raimondo was working in the private sector in Rhode Island and raising a family.

She had been concerned about state government finances for some time. Then one day, incited by a news article, she decided to do something about it. She ran for treasurer of Rhode Island and won the 2010 election despite focusing on state pension systems—the “third rail” of state politics.

Many Rhode Islanders viewed her messages as reasonable ways to deal with a difficult problem. Raimondo led legislators in enacting major pension reforms.

On December 5, Raimondo discussed those reforms at a breakfast meeting with Chicago-area business, government, and academic leaders. The early morning meeting, hosted by the Union League Club of Chicago and the Institute for Truth in Accounting, attracted an overflow audience of more than 100 people.

Rhode Island’s finances had been in bad shape, and the Illinois audience was interested in learning what she did and how she did it. With an unfunded pension liability of more than $90 billion, and more than $8 billion owed to state vendors, Illinois has one of the nation’s worst fiscal situations.

Raimondo joked that whenever she felt especially discouraged about Rhode Island’s problems, looking at Illinois always made her feel better. Estimates from the Institute for Truth in Accounting show Illinois’ taxpayer burden is among the worst in the nation, more than twice as high as Rhode Island’s.

Fact-Based Inquiry

Raimondo said her pursuit of fact-based inquiry played a critical role in her success—first, in getting elected, and second, in gaining the confidence of state legislators and the public during policy development.

Raimondo refrained from providing specific reform proposals during her campaign. She was clear about her concern regarding the state’s pension plans, however, and focused her messages on the need to educate the public about the true depth and scope of the problems. Pressed for a campaign pledge not to change benefits in teacher pension plans, Raimondo refused. She lost the teachers union endorsement but won the election.

In June 2011 Raimondo’s office produced “Truth in Numbers,” a report that received positive responses and significant press coverage.

She said the report had four key objectives: estimating the current price tag for future obligations arising from past public services, identifying the main factors in the state’s structural pension deficit, understanding the implications of letting things stay as they were, and proposing a framework for solutions.

Foundation for Communication

Raimondo, her staff, and a private-sector advocacy initiative used the Truth in Numbers report to lay a foundation for communication to build broad support for a shared solution. She stressed her goal was retirement security for public workers, and for public benefit.

There were times, however, when push came to shove. Asked by one Democratic lawmaker why he should support the initiative given the likely loss of union votes in his district, Raimondo answered if he didn’t support the plan, she would be in his district campaigning against him.

That story prompted someone from the audience to ask how many lawmakers who supported the reforms lost in the 2012 election. “Nobody,” was Raimondo’s answer.

Rhode Island’s pension reforms have three major elements: development of a mixed defined-benefit and defined-contribution plan that shares investment risk with workers and retirees; suspension and then moderation of cost-of-living adjustments; and a higher retirement age.

Some in the audience, including Janet Eisenberg, a benefits specialist in the Chicago area, doubted Rhode Island has fixed its fiscal situation. She asked whether Rhode Island and other state governments need to do more, specifically mentioning the practice of many government pension plans of using much higher discount rates on investments than those used in the private sector. The higher the discount rate, the greater the expected return on investments, and the less money pension funds say they need to stay solvent.

Raimondo seemed to agree that discount rates in government plans are unrealistically high given the “volatile and uncertain world we live in today,” but she would not speculate on what Rhode Island’s funded ratio would be if the pensions used lower, more realistic assumptions.

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Six Reasons to Doubt the Wisdom of Carbon Taxes

By Randall Holcombe

One suggestion for dealing with greenhouse gas emissions is to implement a revenue-neutral tax on carbon emissions. If we implemented a carbon tax and cut income taxes by the same amount, we would be reducing taxes on something we want (income) and increasing taxes on something we don't (air pollution).

As good as it sounds, I'm skeptical of the merits of carbon taxes, even if our carbon dioxide emissions cause global warming. Fossil fuels have been the energy source behind the remarkable economic progress we have had since the beginning of the Industrial Revolution. Taxing that energy source will lower economic growth. Reducing income taxes should increase economic growth, but the issue is more complex than just which tax would, in theory, be the least detrimental to growth.

Here are six reasons for my skepticism about carbon taxes.

1. Fossil fuels have powered the Industrial Revolution. Let's say the Earth is 2 to 3 degrees warmer today than it would have been had the Industrial Revolution never occurred. Is that amount of warming worth it? Would you rather live in today's world, or have the standard of living of people in 1750 and an Earth 2 to 3 degrees cooler? If that is the cost of the remarkable economic progress that has resulted from the Industrial Revolution, most people would gladly accept the warming.

2. Carbon taxes would slow economic growth not only because they would make the power that fuels it more costly but also because carbon taxes are unlikely to be revenue-neutral, even when their advocates propose it. Look at the value-added tax in the European Union, which was proposed as a revenue-neutral tax reform but sparked a substantial growth of government across the EU countries. Look at the federal income tax, which started as a progressive tax with a top marginal tax rate of 7 percent.

A carbon tax would not be implement-ed by an omniscient benevolent government that would produce the “optimal” policy, but by a democratic process laced with special-interest politics and cron-yism. A new revenue source, even if intended by its architects to be revenue-neutral, ultimately would lead to bigger government, placing even more of a burden on the productive capacity of the economy.

3. If we are concerned about our children and grandchildren, then combining the first two points, would we make future generations better off by leaving them a world that is slightly cooler but also poorer?

4. We should weigh the benefits as well as the costs of global warming. What if the people arguing human use of fossil fuels is warming the planet are right? Carbon dioxide, which is often called a pollutant, is necessary for plant growth, and a higher concentration of CO2 in the atmosphere will mean healthier plants. A warmer climate will mean a longer growing season, so we can better feed our population. It would allow cultivation of land that currently is too far north. People in some places would surely be made worse off from a warmer planet, but people in other places—such as Siberia and Canada—would be better off. People are mobile, and populations would shift as climate change made some places more desirable than others. Global warming would bring benefits as well as costs.

5. There are benefits to waiting to deal with global warming, if it is a problem. One is that technology will develop so that it will become cheaper to reduce greenhouse gas emissions in the future. For example, Air Fuel Synthesis is a company that takes CO2 from the air and hydrogen from water to make oil. I don't know whether this is the winning technology, but over time more technological advances like this will occur, making it more cost-effective to deal with greenhouse gas emissions.

Also, people get wealthier over time (if we don't kill the goose that lays the golden eggs) and are willing to pay more for “green” energy. People in wealthier countries are choosing to spend their own money to buy solar panels to generate electricity, and to engage in other “green” activity without gov-ernment mandates telling them they have to. If it is desirable to do something to mitigate greenhouse gas emissions, there are some benefits to doing something later rather than now.

6. Carbon taxes could increase emissions of greenhouse gases. If the United States implement-ed carbon taxes unilaterally, that would raise the nation's cost of manufacturing, which would push manufacturing to other countries (such as China) where it produces higher emissions than in the relatively clean United States. The shift in manufacturing from low-emissions countries to high-emissions places would result in more greenhouse gas emissions.

People who are skeptical about global warming will, of course, see no reason for carbon taxes, but the six points above make the argument that people who think global warming is real and man-made also have good reason to question the desirability of carbon taxes.

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