CENTER ON BUDGET AND POLICY PRIORITIES

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A "REALITY CHECK" ON RECENT ARGUMENTS IN FAVOR OF THE ADMINISTRATION'S NEW "ECONOMIC GROWTH" PLAN

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While promoting his new "economic growth" plan, President Bush and other Administration officials have made a number of statements that are technically accurate but nevertheless quite misleading. These arguments primarily (but not exclusively) involve a deceptive use of averages. The Center on Budget and Policy Priorities has released several analyses examining these arguments. Here is a short summary that looks at some of the statements the President made this week.

Arguments shown in quotes are from the President's January 22 speech in St. Louis:[1]

"92 million Americans will keep an average of $1,083 more of their own money when this tax plan goes through..."

This statement is misleading because the average is skewed upward by the very large tax cuts that would go to a small number of high-income taxpayers. For an example of how averages can be deceptive, consider a group of five individuals — four of whom each receive $100 tax cuts and one who receives a $4,600 tax cut. The average tax cut for the group is $1,000, but four of the five receive far less than this amount. The Administration's use of averages suffers from a similar distortion. Data from the Urban Institute-Brookings Institution Tax Policy Center show that 80 percent of tax filers would receive less than the $1,083 "average" amount, while about half of tax filers would receive $100 or less. The White House produced the $1,083 average figure by averaging together high-income people who would get massive tax cuts — the average tax cut would be $90,000 for people who make more than $1 million per year — with the much larger number of Americans who would get small tax cuts.

Thus, while $1,083 may be the average tax cut amount, it does not accurately reflect what an "average" American would receive. The Tax Policy Center data show that the average tax cut for those in the middle fifth of the income spectrum would be $256.

For further discussion, please see: "Administration's Use of 'Average' Tax Cut Figures Creates Misleading Impression About the Tax Cuts Most Households Would Receive" at http://www.cbpp.org/1-9-03tax.htm.

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[1] "Taking Action to Strengthen Small Businesses," Remarks by the President on the Economy, The White House, January 22, 2003.

"23 million small business owners will receive an average tax cut of $2,042 under this plan..."

This statement, as well, reflects a misleading use of averages. The Urban-Brookings Tax Policy Center data show that 79 percent of returns with small business income would receive less than this $2,042 "average" amount and that 52 percent would get less than $500. The average is skewed by a small number of high-income returns with small business income who are getting very large tax cuts.

In addition, the Administration uses a definition of "small business owner" which includes a substantial number of wealthy investors who don't actually run small businesses but simply have passive investments in them. For example, President Bush and Vice President Cheney count as "small business owners" under this definition. Defining "small business owner" in this way pumps up the average tax cut that small business owners are said to receive.

For further discussion, see: "President's Radio Address and Other Administration Statements Exaggerate Tax Plan's Impact on Small Businesses" at http://www.cbpp.org/1-18-03tax.htm.

"More than 40% of the people who receive dividends make under $50,000 a year. Many of them are seniors. Three-fourths of the people in America who receive dividends make less than $100,000 a year."

These statements mislead because they count a person with $20 in dividend income the same as a person with $20,000 in dividend income. While many people receive dividends, most receive only small amounts. The distribution of dividend income is very skewed.

- People with income below $50,000 account for over 40 percent of those receiving dividends, but they get only 18.5 percent of all dividend income.

- Furthermore, according to the Urban Institute-Brookings Institution Tax Policy Center, people under $50,000 would receive only 6.7 percent of the tax cut from the Administration's proposal to eliminate the taxation of dividends.

- Similarly, while people with incomes below $100,000 make up three-fourths of those who receive dividends, they get only 37 percent of all dividend income and would receive only 21 percent of the proposed tax cut on dividends.

For further discussion, see: "Who Belongs to the 'Investor Class'?" at http://www.cbpp.org/1-6-03tax2.htm

The averages are also misleading with respect to the elderly. It's true that a significant share of the benefits of the dividend exemption would go to individuals over 65. These benefits, however, would be mostly concentrated among a small number of high-income elderly individuals. Nearly 43 percent of the benefits of the dividend exemption that would go to the elderly would go to the 2.5 percent of elderly people with incomes above $200,000. Elderly people with incomes below $50,000 — who make up two-thirds of all elderly people in the nation — would receive only 11 percent of the dividend tax cut going to the elderly and only 4 percent of the total dividend tax cut. The Administration statistic may leave the impression that the dividend tax cut would broadly benefit seniors; this is untrue. In fact, many seniors would be worse off if the large tax cut reduced the resources available for important services and benefits on which they rely.

For more, see: "Impact of the Dividend Tax Cut on the Elderly" at http://www.cbpp.org/1-7-03tax.htm.

"A family of four with an income of $40,000 will receive a 96 percent tax cut."

This statement is true with regard to the federal *income* taxes this family pays, but not with regard to the family's total federal tax bill. This family would receive a 96 percent cut in federal income taxes; its federal income tax liability would fall from $1,178 to $45. But this family pays much more in payroll taxes than income taxes. When one includes the family's $3,060 in payroll taxes, it would receive a more modest 27 percent cut in federal income and payroll taxes. Furthermore, this $3,060 figure includes only the *employee* share of payroll taxes. Most economists have concluded that workers bear the burden of both the employee and the employer payroll taxes, with the employer portion being passed on to workers in the form of lower wages. If one includes both the employer and employee portions, the family pays $6,120 in payroll taxes and receives a 16 percent reduction in federal income and payroll taxes under the Administration's plan.

A recent analysis from the Urban Institute-Brookings Institution Tax Policy Center shows that among tax filers with wage earnings, 90 percent of those with income below $100,000 pay more in payroll taxes than in individual income taxes.[2]

Finally, the tax-cut proposals that would benefit this family — acceleration of the widening of the 10 percent bracket, the increase in the standard deduction for married filers, and the increase in the child tax credit to $1,000 — constitute less than one-quarter of the overall cost of the package. As a result, three-quarters of the proposal could be dropped without affecting this family's tax benefit.

For more, see: "President's Own Example Shows Bulk of Tax Package Irrelevant to Middle-Income Americans" at http://www.cbpp.org/1-13-03tax.htm.

"The Council of Economic Advisors said these proposals over the next three years will create 2.1 million jobs."

This statement glosses over the fact that the CEA estimates show the plans will create only 190,000 jobs in 2003 — which simply equals the number of jobs the Labor Department says we

[2] William Gale and Jeffrey Rohaly, "Three-Quarters of Filers Pay More in Payroll Taxes Than in Income Taxes," *Tax Notes*, January 6, 2003.

lost just in the last two months. These 190,000 jobs equal only 0.1 percent to 0.2 percent of the U.S. workforce.

In addition, the CEA estimates show the plan could pump up jobs in 2004 — an election year — but that after 2004, the plan would actually reduce the rate of job growth. This outcome is not surprising, given the plan's effect in swelling medium and long term deficits.

Finally, some have argued that the majority of Americans now own stocks and would benefit from the Administration's proposal to eliminate taxation of dividends.

It's true that over half of Americans own stocks. Middle-income people with stocks, however, are likely to have them primarily in retirement accounts, which already are tax advantaged. The ownership of taxable stocks and mutual funds is highly concentrated. Using data from the Federal Reserve's Survey of Consumer Finance, New York University economist Edward Wolff estimated that in 1998, the top 10 percent of households in terms of net worth owned 85 percent of taxable stocks and mutual funds, with the wealthiest 1 percent owning 49 percent of taxable stocks and mutual funds. Despite the growing number of Americans who have some stocks, the benefits of the dividend tax cut would flow primarily to very wealthy individuals.

For further information, see: "Who Belongs to the 'Investor Class'?" at http://www.cbpp.org/1-6-03tax2.htm.