Trickle-Down Tax Cuts Don't Create Jobs

By Seth Hanlon and Alexandra Thornton August 24, 2017

President Donald Trump and House Republicans have proposed trillions of dollars in tax cuts, predominantly for high-income individuals and corporations. These tax cuts would come at the expense of middle-class families' economic security and investments in our economy, such as education, scientific research, and infrastructure. While the administration and House Republicans plan to advance their agenda through Congress this fall, public opinion is crystal clear that the American people do not support the tradeoff between tax cuts for millionaires and economic security for working families.[1] Trump and House Republicans are therefore taking a page out of an old playbook: claiming that tax cuts will trickle down to working families in the form of stronger economic growth. But recent history and an abundance of economic research show that trickle-down tax cuts don't create growth or jobs; they lead only to widening inequality between the top 1 percent of income earners and everyone else.[2]

Trickle-down tax cuts have consistently failed to benefit working families

The past quarter century has tested the supply-side theory that top-bracket tax cuts would boost economic growth and jobs. This theory has decidedly failed.

- In 1993, President Bill Clinton raised taxes on top earners from 31 percent to 39.6 percent. Conservatives predicted disaster;[3] instead, the economy boomed. 23 million jobs were created and the economy grew for 32 straight quarters in what was then the longest expansion in history.[4]

- By contrast, in 2001 and 2003, President George W. Bush cut income taxes substantially, lowering the top rate to 35 percent while also lowering top rates on capital gains and dividends. Conservatives maintained that the tax cuts would turbocharge economic growth; in fact, conservative think tank The Heritage Foundation predicted that growth would be so strong that the United States would entirely pay off its debt by 2010.[5] Instead, the ensuing years saw weak growth, followed by the 2008 economic collapse. And as economist Danny Yagan has found, the steep cuts in dividend tax rates signed into law by President Bush in 2003 did not increase corporate investment or worker pay.[6]

- The Bush-era tax rates stayed in place through 2012, but at the end of that year, President Barack Obama struck a deal to restore the 39.6 percent top tax rate and raise the tax rates on capital gains and dividends. Again, many conservatives predicted doomsday.[7] However, the economy grew steadily, and the expansion is still continuing.

As Figure 1 shows, job growth has been much stronger following the two most recent increases in the top tax rate. Given that there are innumerable factors behind how the economy performs, this recent history certainly does not prove that raising taxes on the rich causes the economy to grow or that cutting taxes on the rich causes it to lag. It does, however, provide powerful evidence refuting the claims made by the proponents of trickle-down tax cuts.

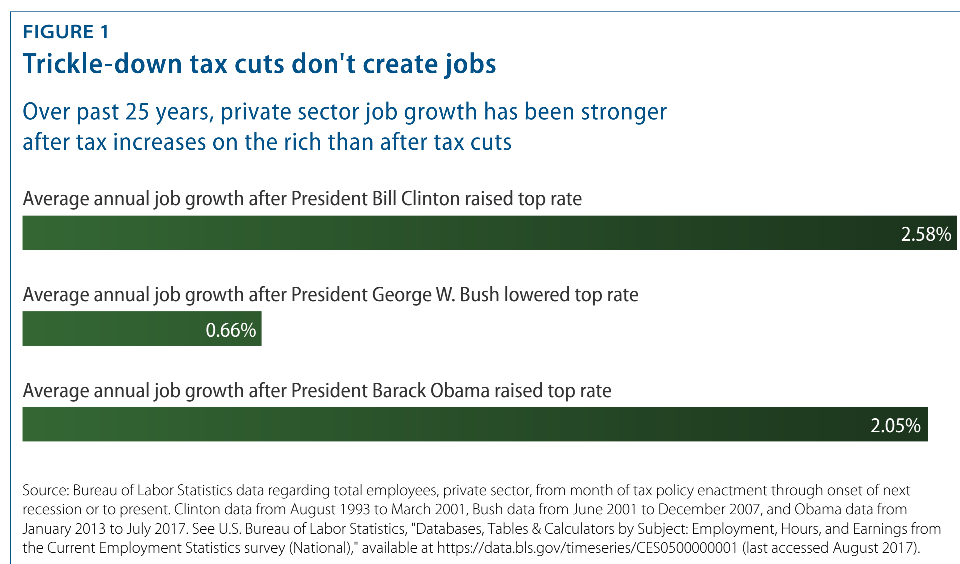

FIGURE 1

Trickle-down tax cuts don't create jobs

Over past 25 years, private sector job growth has been stronger after tax increases on the rich than after tax cuts

Source: Bureau of Labor Statistics data regarding total employees, private sector, from month of tax policy enactment through onset of next recession or to present. Clinton data from August 1993 to March 2001, Bush data from June 2001 to December 2007, and Obama data from January 2013 to July 2017. See U.S. Bureau of Labor Statistics, "Databases, Tables & Calculators by Subject: Employment, Hours, and Earnings from the Current Employment Statistics survey (National)," available at https://data.bls.gov/timeseries/CES0500000001 (last accessed August 2017).

Conservatives often point to President Ronald Reagan's 1981 tax cuts as evidence that supply-side tax cuts accelerate economic growth.[8] In fact, despite the legend, there is little evidence that the personal income tax cuts enacted by President Reagan in 1981 meaningfully boosted the economy; as research by Reagan's own chief economist has found, the so-called Reagan recovery of the early 1980s was driven by monetary policy, not tax cuts.[9]

State experiences can guide federal policymakers

Kansas' supply-side experiment illustrates the dangers of trickle-down tax cuts, while California has proven that making the wealthy pay their fair share is consistent with strong growth. In 2012, in what Gov. Sam Brownback (R-KS) called a "real live experiment" in supply-side tax policy, Kansas approved major tax cuts skewed toward the top earners and business owners.[10] That same year, California raised taxes on the highest earners—singles earning more than $250,000 per year and couples earning more than $500,000—making the top-bracket income tax rates the highest in the nation.[11]

Since then, California has enjoyed among the strongest economic growth rates of any state, while Kansas has lagged behind its neighbors, falling below average nationally in economic growth and job creation.[12] Kansas' tax cuts have severely worsened the state's fiscal situation, resulting in deep cuts to education and other state services.[13]

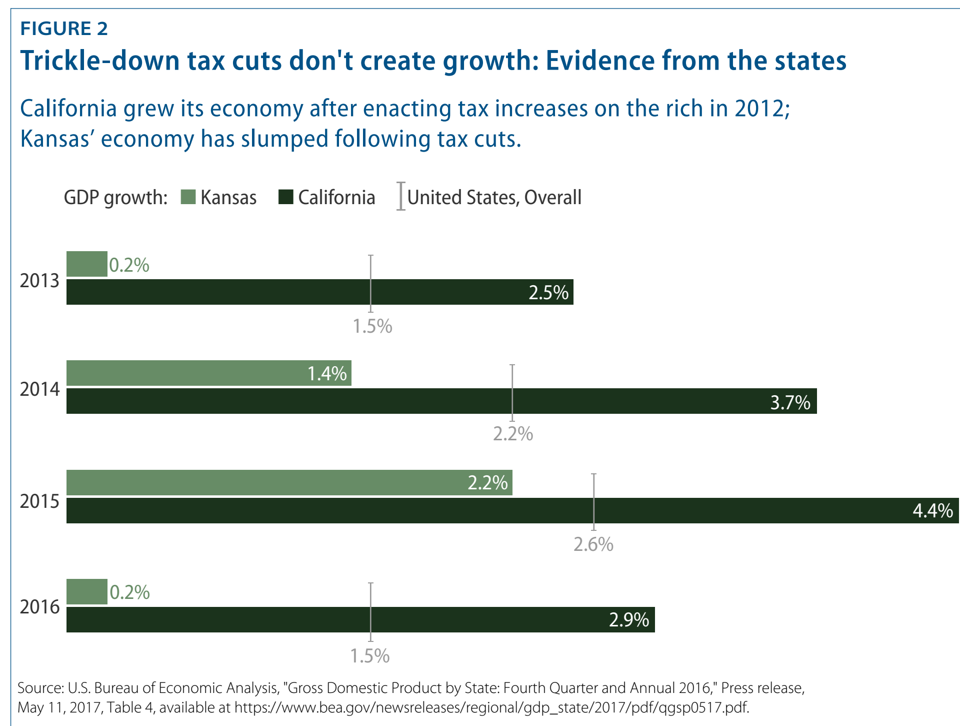

FIGURE 2

Trickle-down tax cuts don't create growth: Evidence from the states

California grew its economy after enacting tax increases on the rich in 2012; Kansas' economy has slumped following tax cuts.

Source: U.S. Bureau of Economic Analysis, "Gross Domestic Product by State: Fourth Quarter and Annual 2016," Press release, May 11, 2017, Table 4, available at https://www.bea.gov/newsreleases/regional/gdp_state/2017/pdf/qgsp0517.pdf.

Reducing top marginal tax rates can harm growth

As economist Jared Bernstein has found, the U.S. experience since World War II shows no correlation between the top marginal tax rate and per capita economic growth—nor between the top marginal tax rate and growth in employment, capital investment, productivity, or pretax median family incomes.[14] That is, cutting taxes at the top does not result in faster growth or rising living standards. Similarly, the non-partisan Congressional Research Service (CRS), examining the U.S. experience since 1947, found no association between the top marginal income or capital gains rates and per capita growth. As CRS determined, "The top tax rates appear to have little or no relation to the size of the economic pie," but tax policy "could be related to how the economic pie is sliced."[15] Indeed, top-bracket tax rates are correlated with growth in income inequality.[16]

The Brookings Institution's William Gale and Dartmouth College's Andrew Samwick comprehensively reviewed the economic literature on tax cuts and growth, concluding that tax cuts are unlikely to substantially boost growth and that tax cuts that increase deficits can harm growth.[17]

As with the significant cuts in domestic programs since 2011, the deficits resulting from unpaid-for tax cuts will undoubtedly be used to justify cutting programs that invest in the economy and support working families, harming our long-term prospects in the process.[18] Federal investments in education, research, and infrastructure all create jobs and grow the economy over the long term.[19] Researchers have found that Medicaid, nutrition assistance, and environmental protection all improve health outcomes and in turn increase productivity.[20] Programs that improve the economic security of low-income children—such as nutrition assistance, housing subsidies, and tax credits like the Earned Income Tax Credit—raise children's educational attainment and future earnings.[21] For these reasons, tax cuts that threaten critical investments undermine the goal of broad-based prosperity.

Seth Hanlon is a senior fellow at the Center for American Progress. Alexandra Thornton is senior director for Tax Policy at the Center.

Endnotes

1 Memo from Jeffrey Pollock, Geoff Garin, Mark Mellman, Michael Bloomfield, and Bryan Bennett, "Progressives Have Public Opinion on Their Side in the Upcoming Tax Fight," August 14, 2017, available at https://notonepenny.org/wp-content/uploads/2017/08/Progressives-Have-Public-Opinion-on-Their-Side-in-the-Upcoming-Tax-Fight-v1_0-1-1.pdf.

2 For further resources on taxes and the economy, see Harry Stein, "Stop Cutting Taxes for Corporations and the Wealthy" (Washington: Center for American Progress, 2017), available at https://www.americanprogress.org/issues/economy/reports/2017/04/10/430161/stop-cutting-taxes-corporations-wealthy; Center on Budget and Policy Priorities, "Tax Cuts for the Rich Aren't an Economic Panacea — and Could Hurt Growth" (2017), available at https://www.cbpp.org/research/federal-tax/tax-cuts-for-the-rich-arent-an-economic-panacea-and-could-hurt-growth; William G. Gale and Andrew A. Samwick, "Effects of Income Tax Changes on Economic Growth" (Washington: Brookings Institution, 2016), available at https://www.brookings.edu/wp-content/uploads/2016/07/09_Effects_Income_Tax_Changes_Economic_Growth_Gale_Samwick_.pdf.

3 Pat Garofalo, "FLASHBACK: In 1993, GOP Warned That Clinton's Tax Plan Would 'Kill Jobs,' 'Kill the Current Recovery,'" ThinkProgress, August 10, 2010, available at https://thinkprogress.org/flashback-in-1993-gop-warned-that-clintons-tax-plan-would-kill-jobs-kill-the-current-recovery-96adb3663484.

4 Center for American Progress, "Power of Progressive Economics: The Clinton Years" (2011), available at https://www.americanprogress.org/issues/economy/reports/2011/10/28/10405/power-of-progressive-economics-the-clinton-years.

5 Rob Wile, "About That Time The Heritage Foundation Said the Bush Tax Cuts Would Pay Off the National Debt by 2010," Business Insider, November 19, 2012, available at http://www.businessinsider.com/about-that-time-the-heritage-foundation-said-the-bush-tax-cuts-would-pay-off-the-natioanl-debt-by-2010-2012-11.

6 Danny Yagan, "Capital Tax Reform and the Real Economy: The Effects of the 2003 Dividend Tax Cut," *American Economic Review* 105 (12) (2015): 3531–3563, available at https://eml.berkeley.edu/~yagan/DividendTax.pdf.

7 Then-House Speaker John Boehner, "Speaker Boehner Calls for Bipartisan Action to Avert the Fiscal Cliff," YouTube, November 7, 2012, available at https://www.youtube.com/watch?v=ntg54qX1wbI; Paul Ryan, "The President's Tax Plan Will Cost Jobs," Press release, October 2, 2012, available at: http://www.presidency.ucsb.edu/ws/index.php?pid=102981.

8 Glenn Kessler, "Rand Paul's claim that Reagan's tax cuts produced 'more revenue' and 'tens of millions of jobs,'" *The Washington Post*, April 10, 2015, available at https://www.washingtonpost.com/news/fact-checker/wp/2015/04/10/rand-pauls-claim-that-reagans-tax-cuts-produced-more-revenue-and-tens-of-millions-of-jobs/?utm_term=.e8e7978a3c37; Jeremy Holden, "Hayes retells myth that Reagan ended recession with tax cuts," Media Matters for America, August 2, 2010, available at https://www.mediamatters.org/research/2010/08/02/hayes-retells-myth-that-reagan-ended-recession/168646.

9 Gale and Samwick, "Effects of Income Tax Changes on Economic Growth; Martin Feldstein and Douglas W. Elmendorf, "Budget Deficits, Tax Incentives, and Inflation: A Surprising Lesson from the 1983-1984 Recovery." In Lawrence H. Summers, ed., *Tax Policy and the Economy,* vol. 3 (Cambridge: MIT Press, 1989), available at http://www.nber.org/chapters/c10943.pdf; Feldstein, "Supply Side Economics: Old Truths and New Claims." Working Paper 1792 (National Bureau of Economic Research, 1986), available at http://www.nber.org/papers/w1792.

10 Scott Rothschild, "Brownback gets heat for 'real live experiment' comment on tax cuts," *Lawrence Journal-World*, June 19, 2012, available at http://www2.ljworld.com/news/2012/jun/19/brownback-gets-heat-real-live-experiment-comment-t.

11 Jessica Calefati and Josh Richman, "Proposition 30: A year later, California schools seeing benefits of tax measure," *The Mercury News*, November 2, 2013, available at http://www.mercurynews.com/2013/11/02/proposition-30-a-year-later-california-schools-seeing-benefits-of-tax-measure/; Tax Policy Center, "State Individual Income Tax Rates 2000-2017" (2017), available at http://www.taxpolicycenter.org/statistics/state-individual-income-tax-rates-2000-2017.

12 Center on Budget and Policy Priorities, "GOP Tax Plans Would Emulate Failed Kansas Experiment" (2017), available at http://www.cbpp.org/research/federal-tax/gop-tax-plans-would-emulate-failed-kansas-experiment; Greg Leiserson, "It's no surprise that the Kansas tax cut experiment failed to create jobs," Washington Center for Equitable Growth, June 15, 2017, available at http://equitablegrowth.org/research-analysis/its-no-surprise-that-the-kansas-tax-cut-experiment-failed-to-create-jobs/; Matthew A. Winkler, "California Leads U.S. Economy, Away From Trump," Bloomberg, May 10, 2017, available at https://www.bloomberg.com/view/articles/2017-05-10/california-leads-u-s-economy-away-from-trump.

13 Mitch Smith and Julie Bosman, "Kansas Supreme Court Says State Education Spending Is Too Low, *The New York Times*, March 2, 2017, available at https://www.nytimes.com/2017/03/02/us/kansas-supreme-court-school-spending.html; Rick Seltzer, "What's the Matter With Kansas Budget Cuts?", Inside Higher Ed, May 23, 2016, available at https://www.insidehighered.com/news/2016/05/23/kansas-cuts-criticized-hurting-large-research-universities.

14 Center on Budget and Policy Priorities, "Testimony of Jared Bernstein, Senior Fellow, Before the Joint Economic Committee" (2016), available at https://www.jec.senate.gov/public/_cache/files/440d3c24-ee1d-4d72-87b3-d07d954fc19c/bernstein-testimony-for-jec-4-20-16.pdf; Center on Budget and Policy Priorities, "Tax Cuts for the Rich Aren't an Economic Panacea — and Could Hurt Growth"; Center on Budget and Policy Priorities, "Large Job Growth Unlikely to Follow Tax Cuts for the Rich and Corporations," June 9, 2017, available at https://www.cbpp.org/research/federal-tax/large-job-growth-unlikely-to-follow-tax-cuts-for-the-rich-and-corporations.

15 Thomas L. Hungerford, "Taxes and the Economy: An Economic Analysis of the Top Tax Rates Since 1945" (Washington: Congressional Research Service, 2012), available at https://fas.org/sgp/crs/misc/R42729.pdf.

16 Thomas Piketty, Emmanuel Saez, and Stefanie Stantcheva, "Optimal Taxation of Top Labor Incomes: A Tale of Three Elasticities." Working Paper 17616 (The National Bureau of Economic Research, 2011), available at http://www.nber.org/papers/w17616; Hungerford, "Taxes and the Economy."

17 Gale and Samwick, "Effects of Income Tax Changes on Economic Growth."

18 Since 2010, nondefense, or discretionary, programs have been cut by 13 percent in real terms—adjusted for inflation—and by 18 percent when adjusted for inflation and population growth. See David Reich and Chloe Cho, "Unmet Needs and the Squeeze on Appropriations" (Washington: Center on Budget and Policy Priorities, 2017), available at https://www.cbpp.org/research/federal-budget/unmet-needs-and-the-squeeze-on-appropriations.

19 Congressional Budget Office, "The Macroeconomic and Budgetary Effects of Federal Investment" (2016), available at https://www.cbo.gov/sites/default/files/114th-congress-2015-2016/reports/51628-Federal_Investment.pdf.

20 Hilary Hoynes, Diane Whitmore Schanzenbach, and Douglas Almond, "Long-Run Impacts of Childhood Access to the Safety Net," *American Economic Review* 106 (4) (2016): 903–934, available at https://www.aeaweb.org/articles?id=10.1257/aer.20130375; Adam Isen, Maya Rossin-Slater, and W. Reed Walker, "Every Breath You Take—Every Dollar You'll Make: The Long-Term Consequences of the Clean Air Act of 1970." Working Paper 19858 (National Bureau of Economic Research, 2014), available at http://www.nber.org/papers/w19858; David W. Brown, Amanda E. Kowalski, and Ithai Z. Lurie, "Medicaid as an Investment in Children: What is the Long-Term Impact on Tax Receipts?". Working Paper 20835 (National Bureau of Economic Research, 2015), available at http://www.nber.org/papers/w20835.

21 Arloc Sherman and Tazra Mitchell, "Economic Security Programs Help Low-Income Children Succeed Over Long Term, Many Studies Find" (Washington: Center on Budget and Policy Priorities, 2017), available at https://www.cbpp.org/research/poverty-and-inequality/economic-security-programs-help-low-income-children-succeed-over.