The Tax-Cut Con By Paul Krugman

September 14, 2003, Sunday MAGAZINE DESK

Cutting taxes doesn't benefit the middle class, it doesn't create jobs or growth and it doesn't give Americans the country they want. Counting the cost of a 25-year crusade. 7242 words
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1. The Cartoon and the Reality

Bruce Tinsley's comic strip, ''Mallard Fillmore,'' is, he says, ''for the average person out there: the forgotten American taxpayer who's sick of the liberal media.'' In June, that forgotten taxpayer made an appearance in the strip, attacking his TV set with a baseball bat and yelling: ''I can't afford to send my kids to college, or even take 'em out of their substandard public school, because the federal, state and local governments take more than 50 percent of my income in taxes. And then the guy on the news asks with a straight face whether or not we can 'afford' tax cuts.''

But that's just a cartoon. Meanwhile, Bob Riley has to face the reality.

Riley knows all about substandard public schools. He's the governor of Alabama, which ranks near the bottom of the nation in both spending per pupil and educational achievement. The state has also neglected other public services -- for example, 28,000 inmates are held in a prison system built for 12,000. And thanks in part to a lack of health care, it has the second-highest infant mortality in the nation.

When he was a member of Congress, Riley, a Republican, was a staunch supporter of tax cuts. Faced with a fiscal crisis in his state, however, he seems to have had an epiphany. He decided that it was impossible to balance Alabama's budget without a significant tax increase. And that, apparently, led him to reconsider everything. ''The largest tax increase in state history just to maintain the status quo?'' he asked. ''I don't think so.'' Instead, Riley proposed a wholesale restructuring of the state's tax system: reducing taxes on the poor and middle class while raising them on corporations and the rich and increasing overall tax receipts enough to pay for a big increase in education spending. You might call it a New Deal for Alabama.

Nobody likes paying taxes, and no doubt some Americans are as angry about their taxes as Tinsley's imaginary character. But most Americans also care a lot about the things taxes pay for. All politicians say they're for public education; almost all of them also say they support a strong national defense, maintaining Social Security and, if anything, expanding the coverage of Medicare. When the ''guy on the news'' asks whether we can afford a tax cut, he's asking whether, after yet another tax cut goes through, there will be enough money to pay for those things. And the answer is no.

But it's very difficult to get that answer across in modern American politics, which has been dominated for 25 years by a crusade against taxes.

I don't use the word ''crusade'' lightly. The advocates of tax cuts are relentless, even fanatical. An indication of the movement's fervor -- and of its political power -- came during the Iraq war. War is expensive and is almost always accompanied by tax increases. But not in 2003. ''Nothing is more important in the face of a war,'' declared Tom DeLay, the House majority leader, ''than cutting taxes.'' And sure enough, taxes were cut, not just in a time of war but also in the face of record budget deficits. Nor will it be easy to reverse those tax cuts: the tax-cut movement has convinced many Americans -- like Tinsley -- that everybody still pays far too much in taxes.

A result of the tax-cut crusade is that there is now a fundamental mismatch between the benefits Americans expect to receive from the government and the revenues government collect. This mismatch is already having profound effects at the state and local levels: teachers and policemen are being laid off and children are being denied health insurance. The federal government can mask its problems for a while, by running huge budget deficits, but it, too, will eventually have to decide whether to cut services or raise taxes. And we are not talking about minor policy adjustments. If taxes stay as low as they are now, government as we know it cannot be maintained. In particular, Social Security will have to become far less generous; Medicare will no longer be able to guarantee comprehensive medical care to older Americans; Medicaid will no longer provide basic medical care to the poor.

How did we reach this point? What are the origins of the antitax crusade? And where is it taking us? To answer these questions, we will have to look both at who the antitax crusaders are and at the evidence on what tax cuts do to the budget and the economy. But first, let's set the stage by taking a look at the current state of taxation in America.

2. How High Are Our Taxes?

The reason Tinsley's comic strip about the angry taxpayer caught my eye was, of course, that the numbers were all wrong. Very few Americans pay as much as 50 percent of their income in taxes; on

average, families near the middle of the income distribution pay only about half that percentage in federal, state and local taxes combined.

In fact, though most Americans feel that they pay too much in taxes, they get off quite lightly compared with the citizens of other advanced countries. Furthermore, for most Americans tax rates probably haven't risen for a generation. And a few Americans -- namely those with high incomes -- face much lower taxes than they did a generation ago.

To assess trends in the overall level of taxes and to compare taxation across countries, economists usually look first at the ratio of taxes to gross domestic product, the total value of output produced in the country. In the United States, all taxes -- federal, state and local -- reached a peak of 29.6 percent of G.D.P. in 2000. That number was, however, swollen by taxes on capital gains during the stock-market bubble.

By 2002, the tax take was down to 26.3 percent of G.D.P., and all indications are that it will be lower still this year and next.

This is a low number compared with almost every other advanced country. In 1999, Canada collected 38.2 percent of G.D.P. in taxes, France collected 45.8 percent and Sweden, 52.2 percent.

Still, aren't taxes much higher than they used to be? Not if we're looking back over the past 30 years. As a share of G.D.P., federal taxes are currently at their lowest point since the Eisenhower administration. State and local taxes rose substantially between 1960 and the early 1970's, but have been roughly stable since then. Aside from the capital gains taxes paid during the bubble years, the share of income Americans pay in taxes has been flat since Richard Nixon was president.

Of course, overall levels of taxation don't necessarily tell you how heavily particular individuals and families are taxed. As it turns out, however, middle-income Americans, like the country as a whole, haven't seen much change in their overall taxes over the past 30 years. On average, families in the middle of the income distribution find themselves paying about 26 percent of their income in taxes today. This number hasn't changed significantly since 1989, and though hard data are lacking, it probably hasn't changed much since 1970.

Meanwhile, wealthy Americans have seen a sharp drop in their tax burden. The top tax rate -- the income-tax rate on the highest bracket -- is now 35 percent, half what it was in the 1970's. With the exception of a brief period between 1988 and 1993, that's the lowest rate since 1932. Other taxes that, directly or indirectly, bear mainly on the very affluent have also been cut sharply. The effective tax rate on corporate profits has been cut in half since the 1960's. The 2001 tax cut phases out the inheritance tax, which is overwhelmingly a tax on the very wealthy: in 1999, only 2 percent of estates paid any tax, and half the tax was paid by only 3,300 estates worth more than $5 million. The 2003 tax act sharply cuts taxes on dividend income, another boon to the very well off. By the time the Bush tax cuts have taken full effect, people with really high incomes will face their lowest average tax rate since the Hoover administration.

So here's the picture: Americans pay low taxes by international standards. Most people's taxes haven't gone up in the past generation; the wealthy have had their taxes cut to levels not seen since before the New Deal. Even before the latest round of tax cuts, when compared with citizens of other advanced nations or compared with Americans a generation ago, we had nothing to complain about -- and those with high incomes now have a lot to celebrate. Yet a significant number of Americans rage against taxes, and the party that controls all three branches of the federal government has made tax cuts its supreme priority. Why?

3. Supply-Siders, Starve-the-Beasters and Lucky Duckies

It is often hard to pin down what antitax crusaders are trying to achieve. The reason is not, or not only, that they are disingenuous about their motives -- though as we will see, disingenuity has become a hallmark of the movement in recent years. Rather, the fuzziness comes from the fact that today's anti-tax movement moves back and forth between two doctrines. Both doctrines favor the same thing: big tax cuts for people with high incomes. But they favor it for different reasons.

One of those doctrines has become famous under the name "supply-side economics." It's the view that the government can cut taxes without severe cuts in public spending. The other doctrine is often referred to as "starving the beast," a phrase coined by David Stockman, Ronald Reagan's budget director. It's the view that taxes should be cut precisely in order to force severe cuts in public spending. Supply-side economics is the friendly, attractive face of the tax-cut movement. But starve-the-beast is where the power lies.

The starting point of supply-side economics is an assertion that no economist would dispute: taxes reduce the incentive to work, save and invest. A businessman who knows that 70 cents of every extra dollar he makes will go to the I.R.S. is less willing to make the effort to earn that extra dollar than if he knows that the I.R.S. will take only 35 cents. So reducing tax rates will, other things being the same, spur the economy.

This much isn't controversial. But the government must pay its bills. So the standard view of economists is that if you want to reduce the burden of

taxes, you must explain what government programs you want to cut as part of the deal. There's no free lunch.

What the supply-siders argued, however, was that there was a free lunch. Cutting marginal rates, they insisted, would lead to such a large increase in gross domestic product that it wouldn't be necessary to come up with offsetting spending cuts. What supply-side economists say, in other words, is, "Don't worry, be happy and cut taxes." And when they say cut taxes, they mean taxes on the affluent: reducing the top marginal rate means that the biggest tax cuts go to people in the highest tax brackets.

The other camp in the tax-cut crusade actually welcomes the revenue losses from tax cuts. Its most visible spokesman today is Grover Norquist, president of Americans for Tax Reform, who once told National Public Radio: "I don't want to abolish government. I simply want to reduce it to the size where I can drag it into the bathroom and drown it in the bathtub." And the way to get it down to that size is to starve it of revenue. "The goal is reducing the size and scope of government by draining its lifeblood," Norquist told U.S. News & World Report.

What does "reducing the size and scope of government" mean? Tax-cut proponents are usually vague about the details. But the Heritage Foundation, ideological headquarters for the movement, has made it pretty clear. Edwin Feulner, the foundation's president, uses "New Deal" and "Great Society" as terms of abuse, implying that he and his organization want to do away with the institutions Franklin Roosevelt and Lyndon Johnson created. That means Social Security, Medicare, Medicaid -- most of what gives citizens of the United States a safety net against economic misfortune.

The starve-the-beast doctrine is now firmly within the conservative mainstream. George W. Bush himself seemed to endorse the doctrine as the budget surplus evaporated: in August 2001 he called the disappearing surplus "incredibly positive news" because it would put Congress in a "fiscal straitjacket."

Like supply-siders, starve-the-beasters favor tax cuts mainly for people with high incomes. That is partly because, like supply-siders, they emphasize the incentive effects of cutting the top marginal rate; they just don't believe that those incentive effects are big enough that tax cuts pay for themselves. But they have another reason for cutting taxes mainly on the rich, which has become known as the "lucky ducky" argument.

Here's how the argument runs: to starve the beast, you must not only deny funds to the government; you must make voters hate the government. There's a danger that working-class families might see government as their friend: because their incomes are low, they don't pay much in taxes, while they benefit from public spending. So in starving the beast, you must take care not to cut taxes on these "lucky duckies." (Yes, that's what The Wall Street Journal called them in a famous editorial.) In fact, if possible, you must raise taxes on working-class Americans in order, as The Journal said, to get their "blood boiling with tax rage."

So the tax-cut crusade has two faces. Smiling supply-siders say that tax cuts are all gain, no pain; scowling starve-the-beasters believe that inflicting pain is not just necessary but also desirable. Is the alliance between these two groups a marriage of convenience? Not exactly. It would be more accurate to say that the starve-the-beasters hired the supply-siders -- indeed, created them -- because they found their naïve optimism useful.

A look at who the supply-siders are and how they came to prominence tells the story.

The supply-side movement likes to present itself as a school of economic thought like Keynesianism or monetarism -- that is, as a set of scholarly ideas that made their way, as such ideas do, into political discussion. But the reality is quite different. Supply-side economics was a political doctrine from Day 1; it emerged in the pages of political magazines, not professional economics journals.

That is not to deny that many professional economists favor tax cuts. But they almost always turn out to be starve-the-beasters, not supply-siders. And they often secretly -- or sometimes not so secretly -- hold supply-siders in contempt. N. Gregory Mankiw, now chairman of George W. Bush's Council of Economic Advisers, is definitely a friend to tax cuts; but in the first edition of his economic-principles textbook, he described Ronald Reagan's supply-side advisers as "charlatans and cranks."

It is not that the professionals refuse to consider supply-side ideas; rather, they have looked at them and found them wanting. A conspicuous example came earlier this year when the Congressional Budget Office tried to evaluate the growth effects of the Bush administration's proposed tax cuts. The budget office's new head, Douglas Holtz-Eakin, is a conservative economist who was handpicked for his job by the administration. But his conclusion was that unless the revenue losses from the proposed tax cuts were offset by spending cuts, the resulting deficits would be a drag on growth, quite likely to outweigh any supply-side effects.

But if the professionals regard the supply-siders with disdain, who employs these people? The answer is that since the 1970's almost all of the prominent supply-siders have been aides to

conservative politicians, writers at conservative publications like National Review, fellows at conservative policy centers like Heritage or economists at private companies with strong Republican connections. Loosely speaking, that is, supply-siders work for the vast right-wing conspiracy. What gives supply-side economics influence is its connection with a powerful network of institutions that want to shrink the government and see tax cuts as a way to achieve that goal. Supply-side economics is a feel-good cover story for a political movement with a much harder-nosed agenda.

This isn't just speculation. Irving Kristol, in his role as co-editor of The Public Interest, was arguably the single most important proponent of supply-side economics. But years later, he suggested that he himself wasn't all that persuaded by the doctrine: "I was not certain of its economic merits but quickly saw its political possibilities." Writing in 1995, he explained that his real aim was to shrink the government and that tax cuts were a means to that end: "The task, as I saw it, was to create a new majority, which evidently would mean a conservative majority, which came to mean, in turn, a Republican majority -- so political effectiveness was the priority, not the accounting deficiencies of government."

In effect, what Kristol said in 1995 was that he and his associates set out to deceive the American public. They sold tax cuts on the pretense that they would be painless, when they themselves believed that it would be necessary to slash public spending in order to make room for those cuts.

But one supposes that the response would be that the end justified the means -- that the tax cuts did benefit all Americans because they led to faster economic growth. Did they?

4. From Reaganomics to Clintonomics

Ronald Reagan put supply-side theory into practice with his 1981 tax cut. The tax cuts were modest for middle-class families but very large for the well-off. Between 1979 and 1983, according to Congressional Budget Office estimates, the average federal tax rate on the top 1 percent of families fell from 37 to 27.7 percent.

So did the tax cuts promote economic growth? You might think that all we have to do is look at how the economy performed. But it's not that simple, because different observers read different things from Reagan's economic record.

Here's how tax-cut advocates look at it: after a deep slump between 1979 and 1982, the U.S. economy began growing rapidly. Between 1982 and 1989 (the first year of the first George Bush's presidency), the economy grew at an average annual rate of 4.2 percent. That's a lot better than the growth rate of the economy in the late 1970's, and supply-siders claim that these "Seven Fat Years" (the title of a book by Robert L. Bartley, the longtime editor of The Wall Street Journal's editorial page) prove the success of Reagan's 1981 tax cut.

But skeptics say that rapid growth after 1982 proves nothing: a severe recession is usually followed by a period of fast growth, as unemployed workers and factories are brought back on line. The test of tax cuts as a spur to economic growth is whether they produced more than an ordinary business cycle recovery. Once the economy was back to full employment, was it bigger than you would otherwise have expected? And there Reagan fails the test: between 1979, when the big slump began, and 1989, when the economy finally achieved more or less full employment again, the growth rate was 3 percent, the same as the growth rate between the two previous business cycle peaks in 1973 and 1979. Or to put it another way, by the late 1980's the U.S. economy was about where you would have expected it to be, given the trend in the 1970's. Nothing in the data suggests a supply-side revolution.

Does this mean that the Reagan tax cuts had no effect? Of course not. Those tax cuts, combined with increased military spending, provided a good old-fashioned Keynesian boost to demand. And this boost was one factor in the rapid recovery from recession that developed at the end of 1982, though probably not as important as the rapid expansion of the money supply that began in the summer of that year. But the supposed supply-side effects are invisible in the data.

While the Reagan tax cuts didn't produce any visible supply-side gains, they did lead to large budget deficits. From the point of view of most economists, this was a bad thing. But for starve-the-beast tax-cutters, deficits are potentially a good thing, because they force the government to shrink. So did Reagan's deficits shrink the beast?

A casual glance at the data might suggest not: federal spending as a share of gross domestic product was actually slightly higher at the end of the 1980's than it was at the end of the 1970's. But that number includes both defense spending and "entitlements," mainly Social Security and Medicare, whose growth is automatic unless Congress votes to cut benefits. What's left is a grab bag known as domestic discretionary spending, including everything from courts and national parks to environmental cleanups and education. And domestic discretionary spending fell from 4.5 percent of G.D.P. in 1981 to 3.2 percent in 1988.

But that's probably about as far as any president can shrink domestic discretionary spending. And because Reagan couldn't shrink the belly of the

beast, entitlements, he couldn't find enough domestic spending cuts to offset his military spending increases and tax cuts. The federal budget went into persistent, alarming, deficit. In response to these deficits, George Bush the elder went back on his "read my lips" pledge and raised taxes. Bill Clinton raised them further. And thereby hangs a tale.

For Clinton did exactly the opposite of what supply-side economics said you should do: he raised the marginal rate on high-income taxpayers. In 1989, the top 1 percent of families paid, on average, only 28.9 percent of their income in federal taxes; by 1995, that share was up to 36.1 percent.

Conservatives confidently awaited a disaster -- but it failed to materialize. In fact, the economy grew at a reasonable pace through Clinton's first term, while the deficit and the unemployment rate went steadily down. And then the news got even better: unemployment fell to its lowest level in decades without causing inflation, while productivity growth accelerated to rates not seen since the 1960's. And the budget deficit turned into an impressive surplus.

Tax-cut advocates had claimed the Reagan years as proof of their doctrine's correctness; as we have seen, those claims wilt under close examination. But the Clinton years posed a much greater challenge: here was a president who sharply raised the marginal tax rate on high-income taxpayers, the very rate that the tax-cut movement cares most about. And instead of presiding over an economic disaster, he presided over an economic miracle.

Let's be clear: very few economists think that Clinton's policies were primarily responsible for that miracle. For the most part, the Clinton-era surge probably reflected the maturing of information technology: businesses finally figured out how to make effective use of computers, and the resulting surge in productivity drove the economy forward. But the fact that America's best growth in a generation took place after the government did exactly the opposite of what tax-cutters advocate was a body blow to their doctrine.

They tried to make the best of the situation. The good economy of the late 1990's, ardent tax-cutters insisted, was caused by the 1981 tax cut. Early in 2000, Lawrence Kudlow and Stephen Moore, prominent supply-siders, published an article titled "It's the Reagan Economy, Stupid."

But anyone who thought about the lags involved found this implausible -- indeed, hilarious. If the tax-cut movement attributed the booming economy of 1999 to a tax cut Reagan pushed through 18 years earlier, why didn't they attribute the economic boom of 1983 and 1984 -- Reagan's "morning in America" -- to whatever Lyndon Johnson was doing in 1965 and 1966?

By the end of the 1990's, in other words, supply-side economics had become something of a laughingstock, and the whole case for tax cuts as a route to economic growth was looking pretty shaky. But the tax-cut crusade was nonetheless, it turned out, poised for its biggest political victories yet. How did that happen?

5. Second Wind: The Bush Tax Cuts

As the economic success of the United States under Bill Clinton became impossible to deny, there was a gradual shift in the sales strategy for tax cuts. The supposed economic benefits of tax cuts received less emphasis; the populist rationale -- you, personally, pay too much in taxes -- was played up.

I began this article with an example of this campaign's success: the creator of Mallard Fillmore apparently believes that typical families pay twice as much in taxes as they in fact do. But the most striking example of what skillful marketing can accomplish is the campaign for repeal of the estate tax.

As demonstrated, the estate tax is a tax on the very, very well off. Yet advocates of repeal began portraying it as a terrible burden on the little guy. They renamed it the "death tax" and put out reports decrying its impact on struggling farmers and businessmen -- reports that never provided real-world examples because actual cases of family farms or small businesses broken up to pay estate taxes are almost impossible to find. This campaign succeeded in creating a public perception that the estate tax falls broadly on the population. Earlier this year, a poll found that 49 percent of Americans believed that most families had to pay the estate tax, while only 33 percent gave the right answer that only a few families had to pay.

Still, while an insistent marketing campaign has convinced many Americans that they are overtaxed, it hasn't succeeded in making the issue a top priority with the public. Polls consistently show that voters regard safeguarding Social Security and Medicare as much more important than tax cuts.

Nonetheless, George W. Bush has pushed through tax cuts in each year of his presidency. Why did he push for these tax cuts, and how did he get them through?

You might think that you could turn to the administration's own pronouncements to learn why it has been so determined to cut taxes. But even if you try to take the administration at its word, there's a problem: the public rationale for tax cuts has shifted repeatedly over the past three years.

During the 2000 campaign and the initial selling of the 2001 tax cut, the Bush team insisted that the federal government was running an excessive budget surplus, which should be returned to taxpayers. By the summer of 2001, as it became clear that the projected budget surpluses would not materialize, the administration shifted to touting the tax cuts as a form of demand-side economic stimulus: by putting more money in consumers' pockets, the tax cuts would stimulate spending and help pull the economy out of recession. By 2003, the rationale had changed again: the administration argued that reducing taxes on dividend income, the core of its plan, would improve incentives and hence long-run growth -- that is, it had turned to a supply-side argument.

These shifting rationales had one thing in common: none of them were credible. It was obvious to independent observers even in 2001 that the budget projections used to justify that year's tax cut exaggerated future revenues and understated future costs. It was similarly obvious that the 2001 tax cut was poorly designed as a demand stimulus. And we have already seen that the supply-side rationale for the 2003 tax cut was tested and found wanting by the Congressional Budget Office.

So what were the Bush tax cuts really about? The best answer seems to be that they were about securing a key part of the Republican base. Wealthy campaign contributors have a lot to gain from lower taxes, and since they aren't very likely to depend on Medicare, Social Security or Medicaid, they won't suffer if the beast gets starved. Equally important was the support of the party's intelligentsia, nurtured by policy centers like Heritage and professionally committed to the tax-cut crusade. The original Bush tax-cut proposal was devised in late 1999 not to win votes in the national election but to fend off a primary challenge from the supply-sider Steve Forbes, the presumptive favorite of that part of the base.

This brings us to the next question: how have these cuts been sold?

At this point, one must be blunt: the selling of the tax cuts has depended heavily on chicanery. The administration has used accounting trickery to hide the true budget impact of its proposals, and it has used misleading presentations to conceal the extent to which its tax cuts are tilted toward families with very high income.

The most important tool of accounting trickery, though not the only one, is the use of "sunset clauses" to understate the long-term budget impact of tax cuts. To keep the official 10-year cost of the 2001 tax cut down, the administration's Congressional allies wrote the law so that tax rates revert to their 2000 levels in 2011. But, of course, nobody expects the sunset to occur: when 2011 rolls around, Congress will be under immense pressure to extend the tax cuts.

The same strategy was used to hide the cost of the 2003 tax cut. Thanks to sunset clauses, its headline cost over the next decade was only $350 billion, but if the sunsets are canceled -- as the president proposed in a speech early this month -- the cost will be at least $800 billion.

Meanwhile, the administration has carried out a very successful campaign to portray these tax cuts as mainly aimed at middle-class families. This campaign is similar in spirit to the selling of estate-tax repeal as a populist measure, but considerably more sophisticated.

The reality is that the core measures of both the 2001 and 2003 tax cuts mainly benefit the very affluent. The centerpieces of the 2001 act were a reduction in the top income-tax rate and elimination of the estate tax -- the first, by definition, benefiting only people with high incomes; the second benefiting only heirs to large estates. The core of the 2003 tax cut was a reduction in the tax rate on dividend income. This benefit, too, is concentrated on very high-income families.

According to estimates by the Tax Policy Center -- a liberal-oriented institution, but one with a reputation for scrupulous accuracy -- the 2001 tax cut, once fully phased in, will deliver 42 percent of its benefits to the top 1 percent of the income distribution. (Roughly speaking, that means families earning more than $330,000 per year.) The 2003 tax cut delivers a somewhat smaller share to the top 1 percent, 29.1 percent, but within that concentrates its benefits on the really, really rich. Families with incomes over $1 million a year -- a mere 0.13 percent of the population -- will receive 17.3 percent of this year's tax cut, more than the total received by the bottom 70 percent of American families. Indeed, the 2003 tax cut has already proved a major boon to some of America's wealthiest people: corporations in which executives or a single family hold a large fraction of stocks are suddenly paying much bigger dividends, which are now taxed at only 15 percent no matter how high the income of their recipient.

It might seem impossible to put a populist gloss on tax cuts this skewed toward the rich, but the administration has been remarkably successful in doing just that.

One technique involves exploiting the public's lack of statistical sophistication. In the selling of the 2003 tax cut, the catch phrase used by administration spokesmen was "92 million Americans will receive an average tax cut of $1,083." That sounded, and was intended to sound, as if every American family would get $1,083. Needless to say, that wasn't true.

Yet the catch phrase wasn't technically a lie: the Tax Policy Center estimates that 89 million people will receive tax cuts this year and that the total tax cut will be $99 billion, or about $1,100 for each of those 89 million people. But this calculation carefully leaves out the 50 million taxpayers who received no tax cut at all. And even among those who did get a tax cut, most got a lot less than $1,000, a number inflated by the very big tax cuts received by a few wealthy people. About half of American families received a tax cut of less than $100; the great majority, a tax cut of less than $500.

But the most original, you might say brilliant, aspect of the Bush administration's approach to tax cuts has involved the way the tax cuts themselves are structured.

David Stockman famously admitted that Reagan's middle-class tax cuts were a "Trojan horse" that allowed him to smuggle in what he really wanted, a cut in the top marginal rate. The Bush administration similarly follows a Trojan horse strategy, but an even cleverer one. The core measures in Bush's tax cuts benefit only the wealthy, but there are additional features that provide significant benefits to some -- but only some -- middle-class families. For example, the 2001 tax cut included a $400 child credit and also created a new 10 percent tax bracket, the so-called cutout. These measures had the effect of creating a "sweet spot" that could be exploited for political purposes. If a couple had multiple children, if the children were all still under 18 and if the couple's income was just high enough to allow it to take full advantage of the child credit, it could get a tax cut of as much as 4 percent of pretax income. Hence the couple with two children and an income of $40,000, receiving a tax cut of $1,600, who played such a large role in the administration's rhetoric. But while most couples have children, at any given time only a small minority of families contains two or more children under 18 -- and many of these families have income too low to take full advantage of the child tax credit. So that "typical" family wasn't typical at all. Last year, the actual tax break for families in the middle of the income distribution averaged $469, not $1,600.

So that's the story of the tax-cut offensive under the Bush administration: through a combination of hardball politics, deceptive budget arithmetic and systematic misrepresentation of who benefits, Bush's team has achieved a major reduction of taxes, especially for people with very high incomes.

But where does that leave the country?

6. A Planned Crisis

Right now, much of the public discussion of the Bush tax cuts focuses on their short-run impact. Critics say that the 2.7 million jobs lost since March 2001 prove that the administration's policies have failed, while the administration says that things would have been even worse without the tax cuts and that a solid recovery is just around the corner.

But this is the wrong debate. Even in the short run, the right question to ask isn't whether the tax cuts were better than nothing; they probably were. The right question is whether some other economic-stimulus plan could have achieved better results at a lower budget cost. And it is hard to deny that, on a jobs-per-dollar basis, the Bush tax cuts have been extremely ineffective. According to the Congressional Budget Office, half of this year's $400 billion budget deficit is due to Bush tax cuts. Now $200 billion is a lot of money; it is equivalent to the salaries of four million average workers. Even the administration doesn't claim its policies have created four million jobs. Surely some other policy -- aid to state and local governments, tax breaks for the poor and middle class rather than the rich, maybe even W.P.A.-style public works -- would have been more successful at getting the country back to work.

Meanwhile, the tax cuts are designed to remain in place even after the economy has recovered. Where will they leave us?

Here's the basic fact: partly, though not entirely, as a result of the tax cuts of the last three years, the government of the United States faces a fundamental fiscal shortfall. That is, the revenue it collects falls well short of the sums it needs to pay for existing programs. Even the U.S. government must, eventually, pay its bills, so something will have to give.

The numbers tell the tale. This year and next, the federal government will run budget deficits of more than $400 billion. Deficits may fall a bit, at least as a share of gross domestic product, when the economy recovers. But the relief will be modest and temporary. As Peter Fisher, under secretary of the treasury for domestic finance, puts it, the federal government is "a gigantic insurance company with a sideline business in defense and homeland security." And about a decade from now, this insurance company's policyholders will begin making a lot of claims. As the baby boomers retire, spending on Social Security benefits and Medicare will steadily rise, as will spending on Medicaid (because of rising medical costs). Eventually, unless there are sharp cuts in benefits, these three programs alone will consume a larger share of G.D.P. than the federal government currently collects in taxes.

Alan Auerbach, William Gale and Peter Orszag, fiscal experts at the Brookings Institution, have estimated the size of the "fiscal gap" -- the increase in revenues or reduction in spending that would be needed to make the nation's finances sustainable

in the long run. If you define the long run as 75 years, this gap turns out to be 4.5 percent of G.D.P. Or to put it another way, the gap is equal to 30 percent of what the federal government spends on all domestic programs. Of that gap, about 60 percent is the result of the Bush tax cuts. We would have faced a serious fiscal problem even if those tax cuts had never happened. But we face a much nastier problem now that they are in place. And more broadly, the tax-cut crusade will make it very hard for any future politicians to raise taxes.

So how will this gap be closed? The crucial point is that it cannot be closed without either fundamentally redefining the role of government or sharply raising taxes.

Politicians will, of course, promise to eliminate wasteful spending. But take out Social Security, Medicare, defense, Medicaid, government pensions, homeland security, interest on the public debt and veterans' benefits -- none of them what people who complain about waste usually have in mind -- and you are left with spending equal to about 3 percent of gross domestic product. And most of that goes for courts, highways, education and other useful things. Any savings from elimination of waste and fraud will amount to little more than a rounding-off error.

So let's put a few things back on the table. Let's assume that interest on the public debt will be paid, that spending on defense and homeland security will not be compromised and that the regular operations of government will continue to be financed. What we are left with, then, are the New Deal and Great Society programs: Social Security, Medicare, Medicaid and unemployment insurance. And to close the fiscal gap, spending on these programs would have to be cut by around 40 percent.

It's impossible to know how such spending cuts might unfold, but cuts of that magnitude would require drastic changes in the system. It goes almost without saying that the age at which Americans become eligible for retirement benefits would rise, that Social Security payments would fall sharply compared with average incomes, that Medicare patients would be forced to pay much more of their expenses out of pocket -- or do without. And that would be only a start.

All this sounds politically impossible. In fact, politicians of both parties have been scrambling to expand, not reduce, Medicare benefits by adding prescription drug coverage. It's hard to imagine a situation under which the entitlement programs would be rolled back sufficiently to close the fiscal gap.

Yet closing the fiscal gap by raising taxes would mean rolling back all of the Bush tax cuts, and then some. And that also sounds politically impossible.

For the time being, there is a third alternative: borrow the difference between what we insist on spending and what we're willing to collect in taxes. That works as long as lenders believe that someday, somehow, we're going to get our fiscal act together. But this can't go on indefinitely. Eventually -- I think within a decade, though not everyone agrees -- the bond market will tell us that we have to make a choice.

In short, everything is going according to plan.

For the looming fiscal crisis doesn't represent a defeat for the leaders of the tax-cut crusade or a miscalculation on their part. Some supporters of President Bush may have really believed that his tax cuts were consistent with his promises to protect Social Security and expand Medicare; some people may still believe that the wondrous supply-side effects of tax cuts will make the budget deficit disappear. But for starve-the-beast tax-cutters, the coming crunch is exactly what they had in mind.

7. What Kind of Country?

The astonishing political success of the antitax crusade has, more or less deliberately, set the United States up for a fiscal crisis. How we respond to that crisis will determine what kind of country we become.

If Grover Norquist is right -- and he has been right about a lot -- the coming crisis will allow conservatives to move the nation a long way back toward the kind of limited government we had before Franklin Roosevelt. Lack of revenue, he says, will make it possible for conservative politicians -- in the name of fiscal necessity -- to dismantle immensely popular government programs that would otherwise have been untouchable.

In Norquist's vision, America a couple of decades from now will be a place in which elderly people make up a disproportionate share of the poor, as they did before Social Security. It will also be a country in which even middle-class elderly Americans are, in many cases, unable to afford expensive medical procedures or prescription drugs and in which poor Americans generally go without even basic health care. And it may well be a place in which only those who can afford expensive private schools can give their children a decent education.

But as Governor Riley of Alabama reminds us, that's a choice, not a necessity. The tax-cut crusade has created a situation in which something must give. But what gives -- whether we decide that the New Deal and the Great Society must go or that taxes aren't such a bad thing after all -- is up to us. The American people must decide what kind of a country we want to be.