

Public Interest Law Reporter

Volume 18
Issue 1 Fall 2012

Article 2

2012

On the Edge of the 'Fiscal Cliff': How the American Middle Class and Global Economy Bear Risk

Steven A. Montalto

Follow this and additional works at: <http://lawcommons.luc.edu/pilr>

 Part of the [Banking and Finance Law Commons](#), and the [Bankruptcy Law Commons](#)

Recommended Citation

Steven A. Montalto, *On the Edge of the 'Fiscal Cliff': How the American Middle Class and Global Economy Bear Risk*, 18 Pub. Interest L. Rptr. 1 (2012).

Available at: <http://lawcommons.luc.edu/pilr/vol18/iss1/2>

This Article is brought to you for free and open access by LAW eCommons. It has been accepted for inclusion in Public Interest Law Reporter by an authorized administrator of LAW eCommons. For more information, please contact law-library@luc.edu.

ON THE EDGE OF THE 'FISCAL CLIFF': HOW THE AMERICAN MIDDLE CLASS AND GLOBAL ECONOMY BEAR RISK

by STEVEN A. MONTALTO

In his letter to Jean Baptiste Le Roy, Benjamin Franklin wrote, “[I]n this world nothing can be said to be certain, except death and taxes.”¹ In fact, taxation and the debate regarding its role in federal government has remained at the core of American civic discussion since the Boston Harbor rebellion in 1773.²

Despite enduring taxation discussion, without Congressional action addressing the ‘fiscal cliff,’ and principally the outlook of the Bush tax cuts, Mr. Franklin would accept another certainty: the American middle class and global economy bear the risk of impending financial hardship.³

CORRELATION BETWEEN THE ‘FISCAL CLIFF’ AND THE BUSH TAX CUTS

The ‘fiscal cliff’ refers to a series of tax increases and spending cuts effective December 31, 2012, unless Congress meets established deficit reduction benchmarks.⁴ On the tax side, the ‘fiscal cliff’ references, among others, an expiration of the payroll tax holiday and the alternative minimum tax patch.⁵ Yet, totaling \$180 billion, “[T]he tax cuts enacted during President George W. Bush’s term represent the biggest slice of the [‘fiscal cliff’] pie.”⁶

The 2001 and 2003 Bush tax cuts enacted comprehensive tax reductions for most American taxpayers.⁷ The cuts included, “[M]arginal rate reductions, the introduction of a new 10 [percent] tax bracket, an expansion of the child tax credit, and a variety of other provisions.”⁸

In December 2010, Congress passed, and the President signed, a two-year extension of both Bush tax cuts.⁹ The extension included an automatic expiration on December 31, 2012.¹⁰

DEFINING AMERICAN MIDDLE CLASS

The term American middle class lacks precise definition.¹¹ In 2011, the U.S. Census Bureau reported median U.S. annual household income at \$50,000.¹² Accordingly, the Census divided the U.S. population into five income-based categories, each comprising 20 percent of the population. “If the middle 20 percent is truly the ‘middle-class,’ then middle class households make between \$38,500 and \$62,400 per year.”¹³

CONGRESSIONAL INACTION AND ITS EFFECT ON THE AMERICAN MIDDLE CLASS

Congressional inaction in addressing the expiring Bush tax cuts will immediately impact the American middle class through an increase in annual tax liability and a subsequent reduction in disposable income.¹⁴

If allowed to fall off the 'fiscal cliff,' at least 90 percent of American taxpayers will see taxes rise.¹⁵ In 2013, the American middle class, defined as Americans with income between \$38,500 and \$62,400 per year, will see taxes increase at least \$2,000.¹⁶ "For most taxpayers, the bulk of the increase would be triggered by the expiration of tax cuts enacted in 2001 and 2003 during the George W. Bush administration."¹⁷

The Bush tax cuts provided a middle class family of four a \$1,825 annual saving.¹⁸ Yet, if allowed to expire, federal income tax brackets revert to pre-2001 levels for American middle class taxpayers.¹⁹ Connecticut residents will see the highest 2013 tax increase with an additional \$5,783 in tax liability.²⁰ Mississippi residents will be least impacted, with an anticipated 2013 increase of \$1,310.²¹

Further, the Bush tax cuts offered middle class taxpayers a \$1,000 tax credit per child.²² An expiration would revert the tax credit to \$500 per child.²³ In essence, this relapse acts as an additional tax hike by increasing pre-tax personal income by \$500 per child.²⁴

Quantifying this effect, a Bush tax cut expiration, "[W]ill reduce [middle class] after-tax income by about 4 percent . . . if you're spending every dollar you've got makes a noticeable dent in your budget."²⁵ Thus, if a middle class taxpayer earned equal personal income in 2012 and 2013, an expiration of the Bush tax cuts will simply result in less to spend in 2013.²⁶

Therefore, Congressional inaction will immediately impact the American middle class through an increase in federal income tax liability and subsequent reduction in disposable income.²⁷ However, a Bush tax cut expiration, by way of the 'fiscal cliff,' will span outside domestic borders.²⁸

CONGRESSIONAL INACTION AND ITS EFFECT ON THE GLOBAL ECONOMY

Congressional inaction in addressing the Bush tax cuts will further impact the global economy through both a reduction in U.S. domestic growth and a subsequent decline in global manufacturing and investment.²⁹

Economists estimate Congressional inaction will draw between \$400 billion and \$720 billion from U.S. domestic growth.³⁰ Growth reduction of this magnitude will mean as much as 4.6 percent of gross domestic product could be lost.³¹ An economist at the Tax Foundation stated the U.S. is, “[T]eetering on zero growth,” and that, “This sort of domestic policy would immediately impact demand and really shock investors.”³²

Quantifying the global risk, it has been estimated that the, “[D]ramatic fiscal tightening implied by the fiscal cliff could tip the U.S. and possibly the global economy into recession. . . . At the very least it would be likely to halve the rate of global growth in 2013.”³³ Thus, Congressional inaction will likely decrease domestic demand by reducing U.S. imports and exports and slow global growth.³⁴

In fact, Congressional inaction has already played a role in global economics.³⁵ U.S. manufacturers have delayed orders, capital improvements, and employment expansion out of global recession fears.³⁶ Jay Timmons, President of the National Association of Manufacturers affirmed that as a result of ‘fiscal cliff’ uncertainty U.S. manufacturers have, “[B]asically stop[ped] in their tracks.”³⁷ The national delay in investment is of even greater concern.³⁸ “[T]he rate of economic growth is slowing, from 4.1 [percent] at the end of last year to an anemic 1.5 [percent].”³⁹ This national delay will affect the global economy’s ability to recover from recent economic recession.⁴⁰ A delay in economic recovery will ultimately be felt by those in the American middle class.⁴¹

Therefore, Congressional inaction regarding the Bush tax cuts will immediately impact the global economy by reducing U.S. domestic growth and reducing global manufacturing and investment.⁴²

CONCLUSION

Without Congressional action, the American middle class and global economy bear the risk of impending financial hardship.⁴³ Perhaps even Mr. Franklin did not envision how the ensuing taxation debate would play in contemporary civic discussion.⁴⁴ However, if the only certainty in life is death and taxes, taxation debate is always around the corner.⁴⁵

NOTES

- 1 Benjamin Franklin, *THE WRITINGS OF BENJAMIN FRANKLIN* 69 (1905).
- 2 Katie Couric, *The Story Behind the Bush Era Tax Cuts*, CBS NEWS (Dec. 3, 2010), http://www.cbsnews.com/8301-18563_162-7111732.html.
- 3 Bruce Watson, *What the 'Fiscal Cliff' Will Mean for You*, AOL DAILY FIN. (Aug. 6, 2012), <http://www.dailyfinance.com/2012/08/06/what-the-fiscal-cliff-will-mean-for-you>.
- 4 Jill Schlesinger, *What is the "Fiscal Cliff"? A Q&A*, CBS NEWS (Sept. 10, 2012), http://www.cbsnews.com/8301-505123_162-57509298/what-is-the-fiscal-cliff-a-q-a; see also Rick Newman, *How Much the 'Fiscal Cliff' Will Cost You*, U.S. NEWS AND WORLD REPORT (Nov. 14, 2012), <http://www.finance.yahoo.com/news/much-fiscal-cliff-cost-205758024.html>.
- 5 Dylan Matthews, *Everything You Need to Know About the Fiscal Cliff in One Post*, WASH. POST (July 16, 2012), <http://www.washingtonpost.com/blogs/ezra-klein/wp/2012/07/16/everything-you-need-to-know-about-the-fiscal-cliff-in-one-post>.
- 6 Jeff Cox, *How Much Will It Cost You If Bush Tax Cuts End? A Lot*, CNBC (Aug. 15, 2012), http://www.cnbc.com/id/48674247/How_Much_Will_It_Cost_You_If_Bush_Tax_Cuts_End_A_Lot.
- 7 William Ahren & Nick Kasprak, *Fate of Bush Tax Cuts Uncertain As Expiration Approaches*, TAX FOUNDATION (Apr. 11, 2012), <http://taxfoundation.org/article/fate-bush-tax-cuts-uncertain-expiration-approaches>.
- 8 *Id.*
- 9 Richard Wolf, *Obama Announces Tentative Deal to Extend Bush Tax Cuts*, USA TODAY (Dec. 6, 2010), <http://content.usatoday.com/communities/theoval/post/2010/12/obama-addresses-possible-deal-on-bush-tax-cuts/1#.UGpLIU2HIeo>.
- 10 Jeanne Sahadi, *Bush Tax Cuts: The Real Endgame*, CNN MONEY (Nov. 28, 2011), http://money.cnn.com/2011/11/28/news/economy/bush_tax_cuts/index.htm.
- 11 Allison McCartney, *What is the American "Middle Class"?*, PBS NEWSHOUR EXTRA (Sept. 24, 2012), http://www.pbs.org/newshour/extra/features/economics/july-dec12/middleclass_09-24.html.
- 12 *Id.*
- 13 *Id.* Compare Alicia Munnell, *Is 250K a Middle-Class Income?*, WALL ST. J. (Oct. 17, 2012), http://articles.marketwatch.com/2012-10-17/finance/34513774_1_household-income-income-distribution-middle-class.
- 14 Wyatt Andrews, *Unresolved Fiscal Cliff Could Raise Taxes for 90 Percent of U.S. Families*, CBS NEWS (Oct. 1, 2012), http://www.cbsnews.com/8301-18563_162-57524033/unresolved-fiscal-cliff-could-raise-taxes-for-90-percent-of-u.s-families.

15 Lori Montgomery, *Report: 90 Percent of Americans Would See Taxes Rise if Congress Doesn't Act on 'Fiscal Cliff'*, WASH. POST (Oct. 1, 2012), http://www.washingtonpost.com/business/economy/americans-would-pay-536-billion-more-in-taxes-if-congress-doesnt-act-on-fiscal-cliff-report-says/2012/10/01/e5e0635a-0bdc-11e2-bb5e-492c0d30bfff_story.html; *see also* Jeanne Sahadi, *AMT: Biggest Fiscal Cliff Tax Headache*, CNN MONEY (Nov. 13, 2012), http://money.cnn.com/2012/11/13/pf/taxes/fiscal-cliff-amt/index.html?hpt=hp_t2.

16 Montgomery, *supra* note 15; *see also* Terry Savage, *What the 'Fiscal Cliff' Means for You*, CHI. SUN TIMES (Nov. 7, 2012), <http://www.suntimes.com/business/savage/16224595-452/what-the-fiscal-cliff-means-to-you.html> (stating the 'fiscal cliff' will 'directly hit[]' the middle class" if no action is taken).

17 Montgomery, *supra* note 15.

18 Kelly Wallace, *\$1.35 Trillion Tax Cut Becomes Law*, CNN POLITICS (June 7, 2001), http://articles.cnn.com/2001-06-07/politics/bush.taxes_1_child-tax-credit-trillion-tax-tax-relief?_s=P M:ALLPOLITICS.

19 Bill Bischoff, *What End of Bush Tax Cuts Would Mean for You*, WALL ST. J. (May 16, 2012), <http://www.smartmoney.com/taxes/income/how-the-expiring-bush-tax-cuts-affect-you>.

20 Cox, *supra* note 6.

21 *Id.* *See also* David Jackson, *Obama Team: Millions Face Tax Hikes if All Bush Rates Expire*, USA TODAY (Jul. 24, 2012), http://content.usatoday.com/communities/theoval/post/2012/07/obama-team-millions-face-tax-hikes-if-all-bush-rates-expire/1#.UKV_dIc8CS0 ("Some 114 million families will see average tax hikes of \$1,600. . . if all the George W. Bush tax cuts are allowed to expire.").

22 Tamara Keith, *Bush Tax Cuts: The New Middle-Class Norm*, NPR (July 10, 2012), *at* <http://www.npr.org/2012/07/10/156493984/bush-tax-cuts-the-new-middle-class-norm>; *see* Suzy Khimm, *How the Fiscal Cliff Affects the Poorest Americans*, WASH. POST, Oct. 28, 2012, *available at* <http://www.washingtonpost.com/blogs/wonkblog/wp/2012/10/28/how-the-fiscal-cliff-would-affect-the-poorest-americans>.

23 *Id.*

24 *Id.* *See also* Watson, *supra* note 3.

25 *Id.*

26 Interview with Jeffrey Kwall, Research Professor, Kathleen and Bernard Beazley Institute at Loyola Univ. Chi. Sch. Of Law (Oct. 18, 2012); *see* Jackson, *supra* note 21.

27 *Id.*

28 Greg Morcroft, *Fiscal Cliff Biggest Global Economic Threat: Fitch*, WALL ST. J., Sept. 27, 2012, *available at* http://articles.marketwatch.com/2012-09-27/economy/34113959_1_fiscal-cliff-global-economy-domestic-threats.

29 Michael Schuman, *Will the Global Economy Tumble Off America's Fiscal Cliff?*, TIME, Nov. 13, 2012, *available at* <http://business.time.com/2012/11/13/will-the-global-economy-tumble-off-americas-fiscal-cliff> ("The U.S. fiscal cliff represents the single biggest near-term threat to the global economic recovery.").

30 *Id.* *See also* Cox, *supra* note 6.

31 Cox, *supra* note 6; *see also* Jackie Calmes, *The 'Fiscal Cliff' Explained*, N.Y. TIMES (Nov. 15, 2012), <http://www.nytimes.com/2012/11/16/us/politics/the-fiscal-cliff-explained.html?page-wanted=all>; *but see* Damian Paletta, *Pressure Rises on Fiscal Cliff*, WALL ST. J. (Nov. 9, 2012), <http://professional.wsj.com/article/SB100014241278873248941045578107363250113122.html>.

html ("If all spending cuts and tax increases are avoided, CBO forecast the U.S. economy would grow by about 1.7% next year.").

32 Ellen Freilich and Herbert Lash, *Global Shares Sink on "Fiscal Cliff," Europe Recession; Oil Up.*, REUTERS (Nov. 15, 2012), <http://www.reuters.com/article/2012/11/15/markets-global-id>

USL1E8MFAY120121115 (“U.S. stocks have struggled to hold onto gains. . . as investors fret the economy could slip into recession if no deal is reached to avoid the “fiscal cliff.”).

33 Morcroft, *supra* note 28; *see also* Jason Scott, *U.S. Fiscal Cliff Threatens World Economy, Australia’s Swan Says*, BLOOMBERG (Nov. 11 2012), <http://washpost.bloomberg.com> (stating fiscal cliff impact has already begun and, “could stretch far beyond the U.S” effecting the global economy).

34 Morcroft, *supra* note 28.

35 Scott, *supra* note 33.

36 Jennifer Carinci, *Economic Shock from Fiscal Cliff Will Last Over a Decade: U.S. Manufacturers*, YAHOO! FINANCE (Nov. 2, 2012), <http://finance.yahoo.com/blogs/breakout/economic-shock-fiscal-cliff-last-over-decade-warns-181646611.html>.

37 *Id.*

38 Watson, *supra* note 3; *see also* Steve Schaefer, *Has the Fiscal Cliff Brought Out the Stock Market Vigilantes?*, FORBES (Nov. 15, 2012), <http://www.forbes.com/sites/steveschaefer/2012/11/15/has-the-fiscal-cliff-brought-out-the-stock-market-vigilantes>.

39 Watson, *supra* note 3.

40 *Id.* *See also* Richard Wolf, *The Fiscal Cliff: Will Obama, Congress Cut Budget Deal*, USA TODAY (Nov. 14, 2013), <http://www.usatoday.com/story/news/politics/2012/11/13/fiscal-cliff-will-obama-congress-cut-a-budget-deal/1703601>.

41 Ben Rooney, *Stocks Fall 1% on Mideast Flare-Up, Fiscal Cliff*, CNN MONEY (Nov. 14, 2012), <http://money.cnn.com/2012/11/14/investing/stocks-markets/index.html>.

42 Watson, *supra* note 3.

43 Watson, *supra* note 3; Andrews, *supra* note 14.

44 Franklin, *supra* note 1.

45 *Id.*