Congressional Smoke and Mirrors - A Phantom Stimulus
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The headlines are screaming again, this time about the Capitol Hill controversy over payroll tax cuts. And, as usual, there is more to the story than what you're reading.

First the good news. Earlier reports said that a stalemate on the tax cut would shut down the government, but before the Senate went home for the holidays, it passed a separate bill that finances the government through next September.

Better news: by all reports, Republicans and Democrats were--and are--in general agreement that there should be some kind of stimulus to the still-recovering economy, and the biggest, least-stimulated sector is consumer spending. The Republicans argued for more tax relief for the wealthiest Americans, and want to reduce pollution controls and force the President to approve the proposed Keystone XL pipeline, which would deliver oil from tar sands in Alberta, Canada to refineries in Texas. Meanwhile, the Democrats wanted a broad-based stimulus measure that would put spending money in the hands of more mainstream American consumers. And they supported environmentalist opposition to the pipeline and the pollution proposals.

Naturally, the two sides couldn't agree on a compromise, so the Senate, by an overwhelming majority, kicked the can down the road for two months by agreeing to continue the reduction in Social Security taxes from 6.2% to 4.2% until Congress could get back in session early next year.

It seems clear that the Senators expected their colleagues in the House of Representatives to follow this simple solution. But nothing is simple in this partisan political atmosphere, and the House (for now, at least) has rejected the measure.

There are several interesting complexities here that should have gotten more attention. One of them is the problems that this wrangling has created for employers, who will have to scramble at the last minute to change their payroll systems to reflect either the 6.2% rate or the 4.2% rate. Which will it be? Who knows? All anybody knows for sure is that the withholding amount will need to be correct starting January 1, and the National Payroll Reporting Consortium has already said that, as a result of the brinkmanship, there is now not enough notice to accommodate any changes that quickly.

Of course, if and when the whole issue is taken up at the end of the proposed two-month extension, companies would face exactly the same dilemma. Chalk this up to a Congress that is oblivious to the consequences of its actions on the business community--especially small businesses.

Behind the scenes, there are other dramas. One involves the very complicated way that the Social Security tax reduction is structured. Reducing the payroll tax would obviously reduce the flow of money into the Social Security trust fund, which is famously experiencing solvency troubles of its own. Neither side wanted to be seen as making the entitlement mess any worse, so the stopgap bill would have had the U.S. Treasury pick up the payments--a sideways accounting move has no real substance. The bill also prevents doctors who accept Medicare payments from receiving a 27% reduction in reimbursement payments, which would weaken the financial stability of another entitlement program, so the Treasury will pay that out of its pocket as well.

But the surprising thing here is that this is actually a revenue-neutral piece of legislation. The Treasury coffers would be replenished through a side door that nobody seems to have noticed. Title IV, entitled "Mortgage Fees and Premiums," would have raised the amount that Fannie Mae and Freddie Mac--the organizations that back a majority of home loans in the U.S.--would collect in mortgage fees after January 2012. In all, the raised mortgage fees--which would increase the cost of homeownership at a time when the housing market is staggering--would pay for the two month extension of the payroll tax cut (estimated at $20 billion) plus two months of additional jobless benefits for 2.5 million out-of-work Americans (an estimated $8.4 billion) and two months of added Medicare reimbursements to doctors (an estimated $6.6 billion).

Can we call this a stimulus, when money comes out of the pockets of home buyers and put in the pockets of payroll workers, the unemployed and doctors? Since the bill seems to be stuck in partisan wrangling, maybe the question is moot anyway.

Sources:

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