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The right medicine for an ailing budget

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T oday we'll find out just how deep Oregon is in the hole when the state economist presents the latest revenue forecast. No one is -- or should be -- expecting good news.

While a revenue shortfall certainly calls for belt tightening by state agencies, a dramatic cut in state spending would be a big mistake. Leaving aside the harm that it would cause many Oregonians, particularly the most vulnerable, slashing services is the wrong medicine for what ails Oregon.

The revenue shortfall stems directly from the country's economic downturn. As demand for goods and services from both consumers and businesses has shrunk, employers have laid off workers or even shut their doors. With business activity and employment down, income tax revenue has declined.

What's needed most to turn around a recession is spending. And when consumers and businesses can't or won't spend, the only sector able to do so is the state.

But unlike the federal government, Oregon can't run a deficit. So unless it covers its shortfall with reserve funds -- tapping Oregon's reserves ought to be the first move, though they may not be adequate -- the only options are to cut spending or raise revenue.

Slashing state services inevitably reduces the flow of dollars through the economy. When the state retrenches, it cuts payments to businesses and nonprofits that provide direct services. It pares back programs such as the Oregon Health Plan that bring matching federal dollars into the Oregon economy. All this happens as demand for many public services increases because of the recession. In other words, slashing state services aggravates the problem.

To avoid deepening the recession and to help the state get past it, Oregon should confront its revenue problem with a revenue solution -- crafted in such a way as to have the least detrimental impact on in-state private sector spending.

On this, a 2001 study by two highly regarded economists -- Nobel Prize winner Joseph Stiglitz of Columbia University and Peter Orszag, now the director of the Congressional Budget Office -- points the way. It concluded that during a recession, a better option than cuts to state services is a tax increase on the wealthy, who can cover the increases by reducing their savings rather than their spending.

What might such a tax increase look like? For starters, a new 11 percent tax bracket on Oregonians with income over a half-million dollars for joint filers, or $250,000 for single filers, would raise hundreds of millions next biennium. Such a tax would apply to fewer than one out of every 100 taxpayers -- those best able to ride out the economic storm unscathed. There are other options, too.

It's appropriate that today's forecast is being presented to the House and Senate revenue committees, not the Joint Ways and Means Committee. The revenue committees write our tax laws and can explore smart revenue solutions to our revenue problem.

The suggestion of a tax increase undoubtedly will elicit howls from those who fail to acknowledge the important role that government plays in the economy. They will claim, contrary to reality, that a tax will "pull money out of the economy."

But the current economic crisis demands smart, practical solutions, not ideological sound bites. Slashing public sector spending would deal a serious body blow to the best economic actor still standing.

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