

POLITICAL PULSE

Plan B for Blame Game

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A tactical retreat that could be a better last-minute safety valve as the cliff approaches.

On the face of it, markets have reacted more positively than we think they should have to the dog's breakfast of fiscal cliff compromises served up by House Speaker John Boehner (R-OH) over the weekend (see ["Toxic Fudge"](#) December 17, 2012). [The emergence yesterday](#) of what Boehner is calling "Plan B" may be a rational explanation. It ups the probability of our *fudge* scenario, and it would be a relatively benign *fudge*.

- Details are unknown, but "Plan B" is essentially the tactical retreat strategy we said last week the GOP was planning (see ["How the GOP Could Survive the Cliff"](#) December 10, 2012).
- "Plan B" would be a House bill extending the Bush-era tax rates for all taxpayers with incomes below \$1 million. For those above, rates would rise -- the House would concede that point.
- Once the House enacts it, the GOP will have raised itself to an equal moral footing with the Democrats in what has become a political blame game. The Democrats will no longer be able [to say](#) the GOP is holding the so-called middle class hostage, because

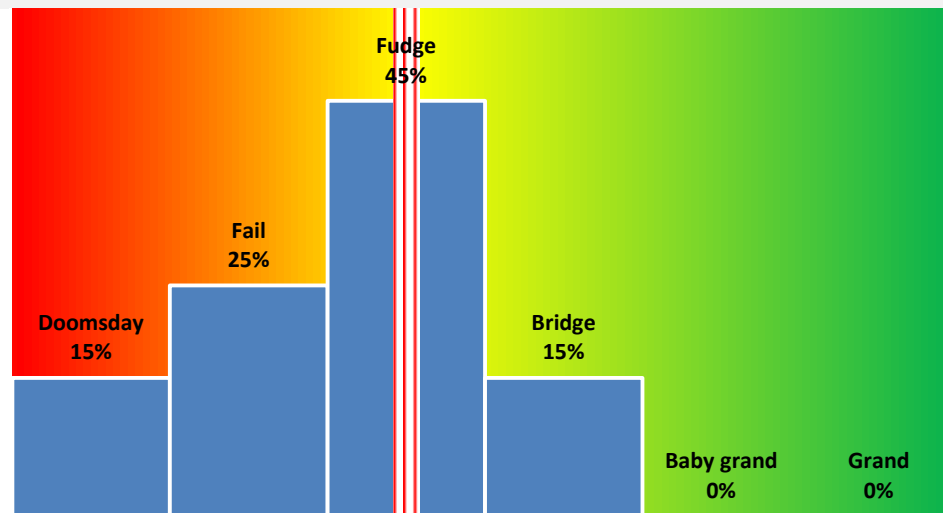
Update to strategic view

US MACRO, US STOCKS: Boehner's "Plan B" would put the GOP on equal footing with the Democrats in the blame game, and offers a new and better fudge scenario for avoiding falling off the fiscal cliff. But where's the real upside? While less damaging to growth than the excessive concessions offered over the weekend, even "Plan B" would add tax burdens to the Not So Great Expansion following the Great Recession. And it remains to be seen whether "Plan B" can even be enacted in the House, given potentially substantial conservative opposition.

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New probabilities of various fiscal cliff negotiation outcomes by year-end

■ Bad ■ Good ||| Bad/Good divide



Source: TrendMacro calculations

the GOP will have passed its own bill protecting the middle class and, against its own preferences, raising taxes on the so-called rich. "Plan B" will essentially mirror [S.3412, the July Senate tax bill](#), except it will draw the line at \$1 million instead of \$250,000.

- [Obama has said](#) he would sign S.3412 into law. Having mostly conceded the point on higher tax rates for the rich, the GOP will say that for Obama not to sign "Plan B" into law would be *him* holding the middle class hostage.
- Indeed, yesterday House Minority Leader Nancy Pelosi (D-CA) [said that](#) with "Plan B" the GOP has "delivered a victory to President Obama." So how could Obama not agree to it?
- [In heated questioning yesterday](#), White House spokesman Jay Carney did not say that Obama wouldn't sign "Plan B." He said only that it couldn't pass the Senate -- which, in the blame game, is symmetrical to saying that S.3412 couldn't pass the House.
- Yet the GOP can claim that the Senate should embrace "Plan B," as indeed should Democrats in the House -- it is, in fact, precisely the approach that Pelosi and Senator Chuck Schumer (D-NY) [have been advocating](#) for two years. This fact has already caused Democrats some embarrassment, with House Democratic Whip Steny Hoyer (D-MD) [saying yesterday](#) that Pelosi's previous support of the idea had only been a "political ploy."
- "Plan B" is all the more powerful a tool in the blame game for Boehner's having offered so many concessions over the weekend -- higher tax rates on the rich, \$1 trillion in revenue, and debt ceiling hikes. It's getting difficult for Democrats to say -- truthfully, at least -- that Boehner hasn't met Obama more than half way.

Having said all that, it's not a sure thing that "Plan B" can be passed in the House. Pelosi [says](#) Democrats won't support it, despite having called it a victory. And conservative GOP members [may see it](#) as too much of a concession -- and, effectively, a tax hike that would violate their pledge.

If it does pass the House, then it will stand with S.3412 as a second last-minute safety valve to avoid falling all the way off the cliff. So for now we are upping the probability of our *fudge* scenario to 45% -- and recognizing that it would be a relatively better fudge than the one it seemed that we were looking at Monday. However, with more *fudge* possibilities on the table and time running out, we are reducing our estimated probability of a *baby grand bargain* to zero.

Bottom line

Boehner's "Plan B" would put the GOP on equal footing with the Democrats in the blame game, and offers a new and better *fudge* scenario for avoiding falling off the fiscal cliff. But where's the real upside? While less damaging to growth than the excessive concessions offered over the weekend, even "Plan B" would add tax burdens to the Not So Great Expansion following the Great Recession. And it remains to be seen whether "Plan B" can even be enacted in the House, given potentially substantial conservative opposition. ▶

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