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Ways and Means Democratic Staff

The Thomas Tax Cuts Are Too Large, Dig the Deficit Holes Deeper, and are Bad for the Economy

As the following table shows, the new House Republican $550 billion tax-cut plan is another step on the way to an ever larger tax-cut total. These tax cuts, in turn, are part of a Republican Congressional budget that increases and extends budget deficits, even with the Social Security trust fund surpluses are counted in. That budget drives up long-term debt by $1.5 trillion.[1]

What this budget does have is another round of tax cuts tilted to the affluent and deficits that will become a future tax on the rest of us and our children. Under this budget, the Federal government will have to borrow another $1.5 trillion over the next ten years. The budget, of which these tax cuts are a part, does not even pretend to come into balance until 2012. In 2012, the resulting debt load will be about $50,000 per American household.[2]

The Social Security trust fund surpluses will be mis-used in every year, for at least eleven years, to mask even larger deficits in the rest of the budget.

This relentless push for tax cuts – and the use of gimmicks like early “sunsets” that set the stage for more tax cuts in the future — will “starve government” of funding, both directly and indirectly by driving up interest costs ($293 billion in net interest in 2013). Never mind the vulnerable people who will be hurt. Never mind the retiring baby boomers who are counting on Social Security and Medicare. All this gets in the way of the anti-government ideological agenda.

Just to pay the amount of interest costs that will be added, over ten years, under the President’s budget,[3] it would be necessary to zero out all of unemployment compensation, plus some more, or one or more programs like Supplemental Security Income ($400 billion), the refundable Earned Income and Child Tax Credits ($357 billion), Food Stamps ($274 billion), Family Support ($259 billion), Student Loans - State Children's Health Insurance - and - Veterans' Pensions ($149 billion).

The Administration projects budget deficits as far as the eye can see, yet House Republicans relentlessly pursue $1.2 trillion in tax cuts. With the collateral increase in interest costs, the total is $1.6 trillion.

	2003 - 2013
Amount of so-called economic-growth tax package:	**$550 billion**
Amount beyond the "economic growth" package: This can include • accelerate, expand and extend pension/retirement tax benefits ($100 billion or more) • extending other tax cuts that expire at the end of 2010, • permanent extension of the R&E credit ($68 billion), • health insurance credit ($89 billion), • above-the-line deduction for long-term care insurance and an added personal exemption for long-term care-givers ($32 billion) • above-the-line deduction for charity ($13 billion).	**$675 billion**
Tax cuts:	**$1.225 trillion**
Added interest costs:	**$335 billion**
Total	**$1.560 trillion**

Sources: Congressional Budget Resolution, JCT estimates for President's proposals and CBO debt-service factors.

Ways & Means Democratic Staff, 5/2/03

Long-term budget deficits hurt the economy

Long-term deficits are bad for future economic and job growth. That is what Bob Rubin, former Senator Rudman, former Federal Reserve Chairman Paul Volcker and Fed Chairman Alan Greenspan have said.[4] Persistent budget deficits hurt economic growth over the long term because they soak up scare private savings that should be used instead for capital formation.

> In February, Fed Chairman Alan Greenspan testified, "*We must be sure that the Federal Government does not impinge on the private sector's capability of creating goods and services and expanding the standard of living of the American people. And that requires that it not drain the savings resources of the private sector, which it does when it's running a deficit*."

This budget and the House Republican tax cuts have it backwards — almost nothing to deal with real distress that will soon be out there from expiration of unemployment benefit's and state cuts in Medicaid, but over the longer-term another round of big tax cuts for the affluent, who get rewarded for doing nothing except collecting the dividends and capital gains they will have anyway.

What sense does it make for a country that has a $436 billion trade deficit and depends on $474 billion in borrowing from abroad to adopt a budget that will try to borrow another $1.5 trillion over the next ten years? This is like having one more cocktail before hitting the road. It's too big a risk, especially when you are driving an entire economy around.

Let's not fall for the same failed story again

Claims are not credible: The claim that another round of tax cuts for the affluent will help the economy is not credible. The President and House Republicans always call for more tax cuts. It's tax cuts, winter-fall-summer-spring --- economy weak or strong. The President called for tax cuts during his 2000 campaign when the economy was strong. He called tax cuts early in 2001 when budget surpluses were projected and before it was known that the economy becoming weak. However, he also called for tax cuts in 2002. Now, in 2003, the surpluses are gone. The bill is coming due for the tax cuts already enacted, and budget deficits are now projected. Yet the call stays the same: more tax cuts, mostly for the affluent.

When President Bush submitted his first budget, early in 2001, he said that surpluses would be so large that he could have a $1.6 trillion tax cut, yet "preserve" the Social Security surpluses for Social Security and retire as much Federal debt as was practical. His budget did not call for any increase in the statutory debt ceiling.

Just six months after the tax cut was enacted, Treasury Secretary O'Neill asked for a $750 billion increase in the statutory debt ceiling.

Then the real picture kept emerging. Rather than budget surpluses and lower debt, we got budget deficits and higher debt. The unified budget was in deficit by $158 billion in 2002. The non-Social-Security budget was in deficit by $317 billion. The 2003 unified budget will be in deficit by $345 billion, according the Administration's own figures. 2.6 million private sector jobs have been lost since the end of 2000.

Republicans blame the war and the 2002 economic recession and they say that there have been large deficits in the past. <u>But Leaders look ahead and fix mistakes. They don't perpetuate mistakes</u>.

The President's own budget now shows that there will be <u>future</u> unified budget deficits under "current polices," and that deficits will get bigger when the baby-boomers retire. <u>Yet</u> the President requests <u>another</u> round of $1.6 trillion in tax cuts and $1.1 trillion in spending increases, for a total of $2.7 trillion in actions that <u>increase</u> deficits and debt. This is the opposite of leadership. <u>This is a failure to act to move the budget and the economy in the right direction</u>.

"<u>Jobs</u>": Most recently, the President has equated tax cuts with "jobs." He has demanded first-round of tax cuts at least as large as $550 billion, and House Republicans want to deliver. If economics is that simple, why not eliminate all taxes? If economics were that simple, families could get ahead by spending twice their income every year.

<u>The debt situation</u>: is a badge of a failed Republican spend-more and cut-taxes policy. Republicans insist on another round of large multi-year tax cuts, but they don't really cut spending. Since President Bush began submitting budgets, domestic discretionary budget authority has been going up much more rapidly than inflation: 9.7% per year for three years,[5] and, of course, Republicans are very much in favor of higher military spending.

The Senate now has before it a $984 billion debt-ceiling increase bill, an all time record.   First quarter Treasury borrowing was a record this year and this quarter is likely to be a record as well.   This year's budget deficit is head upwards well past $340 billion.

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<u>Economic growth</u>:

Republican growth claims are not credible.

- The non-partisan Congressional Budget Office (CBO), now headed by a Republican appointee, has already found that the President's budget, at best, has little positive effect on economic growth, if any.

  CBO wrote, "*the proposals, on net, would probably increase labor supply but decrease investment and the stock of capital. Largely because of these two opposing forces, the net effect on economic output could be either positive or negative. ... Regardless, the net effect on output through long-term changes to the supply side of the economy ... would probably be small.*."

  The new CBO Director testified that "*in our view, on balance, the conventional estimate is a very good indicator of the budgetary outlook even after including the macroeconomic effects*." This means that the tax cuts and spending increases in the President's budget don't come close to "paying for themselves" by expanding the economy.

- Others agree with CBO.

  More than 400 professional economists, including ten Nobel Laureates, had this reaction to the President's plan: "Regardless of how one views the specifics of the Bush plan, there is wide agreement that its purpose is a permanent change in the tax structure and not the creation of jobs and growth in the near-term."

  The Committee for Economic Development, an organization of distinguished corporate leaders and educators argued in March, "Deficits ***do*** matter. ... We cannot afford economic policy decisions today that further raise deficits tomorrow."

> The bipartisan Concord Coalition said in April, "It is illogical to begin the journey back toward balanced budgets by enacting a tax cut that will only make the long-term outlook worse. Furthermore, the proposed tax cuts are not useful for short-term fiscal stimulus, since only a small portion would take effect this year."
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> The established Wall Street firm of Goldman Sachs wrote to its clients, "The long-term budget outlook is much worse than official government projections, with annual deficits apt to cumulate to more than $4 trillion over the next ten years ... .Unfortunately, the sharp deterioration in the budget outlook does have negative economic consequences."
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> According to a *Wall Street Journal* report, "International Monetary Fund research director Kenneth Rogoff said, 'Suppose for a moment we were talking about a developing country that had a gaping [trade] deficit year after year as far as the eye can see, budget ink spinning from black into red, open-ended security costs, and an exchange rate that has been inflated by capital inflows. With all that, I think it's fair to say we'd be pretty concerned.'"

<u>There they go again – cutting the capital gains tax rate to 15 %</u>:

In 1998, CBO studied the 15% capital gains rate in response to a request from Ways and Means Committee Chairman Archer. CBO wrote, "*The net effect of the proposal is likely to be small*." CBO pointed out that the economic growth effects would <u>not</u> come close to generating enough feedback to offset the revenue loss estimated using normal procedures. Furthermore, CBO pointed out that if the tax cut is not paid for, which is surely the case now, then the adverse effect of budget deficits will retard GDP growth, rather than increase it. CBO also explained why unlocking capital gains does not, in and of itself, create new saving, or result in the more efficient use of tangible capital, despite the apparent belief of many in this proposition. Unlocking will essentially result in the <u>rearrangement</u> of portfolios, rather than new net saving.

<u>Stock market magic</u>: can the tail wag the dog.

Republicans claim that the economy can be boosted by dividend and capital gain tax cuts that are supposed to pump up the stock market. This is backwards. It is a self-served banquet for the affluent. Famous investor Warren Buffett recently told Senators that getting rid of the tax on dividends would reduce his federal tax bill by $300 million a year, and Mr. Buffett said that would mean he would pay proportionately less in taxes than his secretary. Mr. Buffet would get this tax break for doing nothing differently than he does already. House Republicans are forging ahead to give Mr. Buffett most of that tax – for doing nothing.

If House Republicans would focus on improving the economy, the stock market would take care of itself. It is backward to try to lever up the huge economy with the stock market.

The Republican capital gains and dividends tax cut is going to be done with borrowed money. It makes no sense to pretend that the government can create real wealth and prosperity by borrowing large sums of money. The dividend tax cuts may make some stocks look more valuable to some people, but there is also a big corresponding debt on the ledger that the Administration ignores in its economic analysis.
Even if a dividends tax cut would improve the stock market, why are "conservatives" in favor of government intervention to prop up the stock market? Is this "neo-conservatism," according to which the rest of America pays to help the people who own the most stock when the stock market goes down, but there is no "profit sharing" for the rest of America when the stock market goes up?

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1. This is the increase in debt held-by-the-public in the budget resolution from the end of 2003 to the end of 2013.

2. This is the 2013 projected Federal debt held-by-the-public in the budget resolution, $5.4 trillion, divided by the number of households.

3. $530 billion is the amount of net interest costs added by the President's budget.

4. According to Sam Nunn, Peter G. Peterson, Robert E. Rubin, Warren B. Rudman, Paul A. Volcker, and Bob Kerrey, in Wednesday's New York Times, "*Given the rapidly deteriorating long-term fiscal outlook, neither proposal* [House or Senate budget] *is fiscally responsible. It is illogical to begin the journey back toward balanced budgets by enacting a tax cut that will only make the long-term outlook worse. Furthermore, the proposed tax cuts are not useful for short-term fiscal stimulus, since only a small portion would take effect this year. Nor would they spur long-term economic growth. In fact, tax cuts financed by perpetual deficits will eventually slow the economy.*"

5. For the three years from 2000 through 2003, domestic budget authority (including obligation limits for transportation) has risen at an average of 9.7% per year. This does not include any domestic funding included in the April war supplemental. (Source: CBO)