UPDATE

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THE HOUSE BUDGET RECONCILIATION BILL: MAKING A BAD BUDGET EVEN WORSE

(Updating *Backgrounder* No. 932, "Taxes, Spending, Gimmicks, and Snake Oil: Why Bill Clinton's Budget Is Bad For America," March 16, 1993, and *Backgrounder* No. 942, "Why Higher Tax Rates on Income Will Slow Growth, Cost Jobs," May 25, 1993.)

The House of Representatives is scheduled this week to vote on the budget reconciliation bill, a measure which purports to reduce future federal budget deficits by a total of $336.8 billion over the next five years. The Clinton Administration and House Democratic leadership claim that the legislation represents a balanced use of spending cuts and tax increases to reduce federal borrowing. But in reality the package consists almost entirely of higher taxes. More than $301 billion, or 89.5 percent of the total, comes from increased revenue. The legislation would impose the largest tax increase in American history.

Even using the Washington definition of a budget cut—increasing spending at a slower rate than previously planned—the bill contains almost no spending cuts. Less than six percent of the package, or barely $20 billion ($4 billion per year), takes the form of reductions in the rate of growth of rapidly expanding federal entitlement programs. The remaining $15.4 billion of alleged savings, accounting for 4.6 percent of the total savings, comes from provisions that can best be described as budget gimmicks. The ratio of tax increases to spending cuts: 15 to 1

TAXES AND DISGUISED TAXES

On a party-line vote, the House Ways and Means Committee approved almost all of the tax increases proposed by the White House. The only noteworthy change was the decision to forego the Administration's convoluted Investment Tax Credit and instead raise the top corporate income tax rate from 34 percent to "only" 35 percent. The package contains all the other economically destructive increases in tax rates on income and wealth creation proposed by the White House. The legislation also would impose a huge and controversial new tax on energy.

Architects of the House "deficit reduction" bill have attempted to hide the size of the tax increase. But the claim that the legislation raises "just" $246 billion over the next five years is accomplished only by using creative accounting to portray some spending increases as tax cuts and to characterize many revenue increases as spending cuts.

Spending Hikes Dressed as Tax Cuts. The Democrat-controlled Joint Committee on Taxation, for instance, admits that three provisions that are counted as tax cuts are really spending increases. The three provisions are:

✓ **$1.252 billion of higher Social Security and Medicare spending for educational assistance is counted as a tax cut;**

✓ **$25.678 billion of higher welfare spending is counted as a tax cut;**

✓ **$2.105 billion of higher spending for immunization is counted as a tax cut.**

Note: Nothing written here is to be construed as necessarily reflecting the views of The Heritage Foundation or as an attempt to aid or hinder the passage of any bill before Congress.

By counting these spending increases as tax cuts, lawmakers can pretend that the tax increase is smaller than it really is since the dollar value of this new spending is subtracted from the dollar value of all the tax increases. As a result, the reported size of the net tax increase in the budget reconciliation bill is dishonestly reduced.

Tax Hikes Dressed as Spending Cuts. The number of spending increases masquerading as tax cuts is dwarfed, however, by the number of tax increases and revenue-raising provisions that are counted as spending cuts. By counting these tax increases as spending cuts, Congress artificially inflates the reported amount of spending cuts in the budget reconciliation bill. Among these provisions:

- ✓ **$2.420 billion from higher import "user fees";**
- ✓ **$8.078 billion from increasing the monthly Part B Medicare tax;**
- ✓ **$2.089 billion from increasing the federal unemployment tax in 1997 and 1998;**
- ✓ **$.214 billion from aircraft registration taxes;**
- ✓ **$.345 billion from patent and trademark "user fees";**
- ✓ **$1.169 billion from Nuclear Regulatory Commission "user fees."**

All told, the legislation actually raises nearly $55 billion more in revenues over the next five years than supporters admit. Not all of the higher revenues, it should be noted, are tax increases. Auctioning off portions of the electromagnetic spectrum, for instance, will raise an estimated $7.2 billion. And a tiny fraction of the user fees are genuine efforts to charge beneficiaries the cost of government-provided services. These steps are desirable, but they are not, by any stretch of the imagination, spending cuts.

More Budget Gimmicks. The bill also is noteworthy for its use of blatant smoke-and-mirrors tactics. For instance, the legislation claims savings of $8.810 billion from ending lump-sum payments for federal retirees. This provision, however, simply shifts spending into future years. Similarly, the provision claiming to save $2.339 billion in military retirement costs is achieved by a delay in cost-of-living adjustments, thus doing nothing to alter the long-run growth of spending. And proponents claim the bill will save $4.270 billion by nationalizing the guaranteed student loan program. Yet the Congressional Research Service points out that, "Direct lending [the Clinton alternative] actually could increase budget outlays and reduce national income if it were unable to duplicate administrative efficiencies achieved by private lenders." One need only compare the Postal Service with Federal Express to consider whether this provision is likely to save taxpayers money.

MORE SPENDING AND HIGHER DEFICITS

Proponents of the budget reconciliation bill assert that the legislation is a much-needed step to bring deficit spending under control. Yet according to the White House's own estimates, adoption of the Clinton budget will result in $322 billion of higher spending by 1998. If history is any guide, spending actually will climb much faster than this since Congress, in the expectation that more revenue will be forthcoming, will increase spending even more. Tax increases in 1982, 1984, 1987, and 1990, for instance, were all enacted with the promise that the deficit would fall. But in every case, the deficit rose the following year.

The Administration effectively concedes that the tax increase will be swallowed by new spending. According to estimates prepared by the Office of Management and Budget (OMB), adoption of the Administration's budget will cause the deficit to climb to $431 billion by 2003. But even this estimate is based upon the remarkable assumption that the record tax increase will not harm the economy and shrink the tax base. The Administration's $431 billion deficit estimate also assumes that the budget gimmicks will generate real savings and that Congress will not increase spending in the future, two rather dubious assumptions.

PHONEY IMPROVEMENTS TO THE PACKAGE

Even though the White House's own figures show that the Administration's budget will cause the deficit to rise, not fall, the President is telling taxpayers that he will place all new tax revenue in a "trust fund" to ensure that the money goes for deficit reduction. This is a charade, however, because it would not impose any roadblocks to new spending. Clinton's own Deputy OMB Director, Alice Rivlin admits, "I don't think it affects anything."

The 15 to 1 ratio of tax increases to spending cuts in the budget reconciliation bill has caused considerable discomfort to many lawmakers. For instance, Representative Charles Stenholm, the Texas Democrat, is insisting that the savings in the legislation be enforced by a sequester mechanism that would automatically cut spending and raise taxes. This approach is misguided, however, because the package has no savings to enforce. Nor is it reasonable to punish taxpayers, as Stenholm would do, by including an automatic tax increase provision in the sequester.

Other frustrated members of Congress are exploring proposals to eliminate the energy tax and instead impose a cap on entitlement programs. While a small step in the right direction, such a step would still leave the ratio of tax increases to spending cuts at an unacceptable level. Worse still, this approach would do nothing about the most economically destructive portion of the budget reconciliation bill—the higher tax rates on income.

CONCLUSION

Large tax increases are not the solution to deficit spending. Herbert Hoover, Lyndon Johnson, Jimmy Carter, and George Bush all imposed large tax increases and in every case the economy turned sour, jobs were destroyed, and the deficit rose. Higher tax penalties on productive economic activity are not compatible with a growing economy. The record tax increase in the budget reconciliation bill is a certain recipe for economic stagnation.

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