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Backgrounder
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THE RECONCILIATION BILL: EXPANDING TAX HIKES, DISAPPEARING SPENDING CUTS

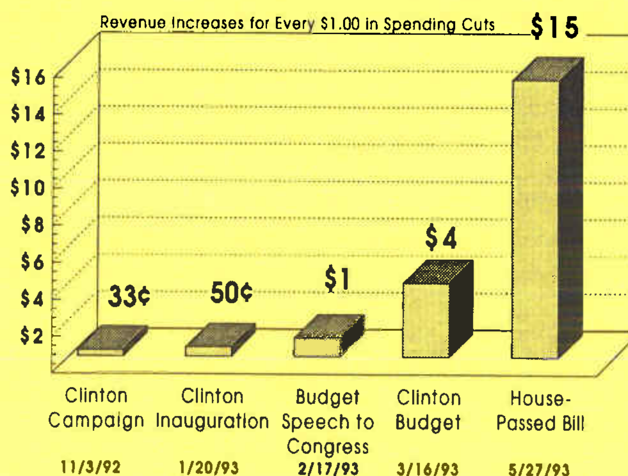
(Updating *Backgrounder Update* No. 193, "How Clinton's Budget Plan Taxes the Elderly," June 4, 1993; *Backgrounder Update* No. 192, "The House Budget Reconciliation Bill: Making a Bad Budget Even Worse," May 25, 1993; *Backgrounder* No. 942, "Why Higher Tax Rates on Income Will Slow Growth, Cost Jobs," May 25, 1993; *Backgrounder* No. 932, "Taxes, Spending, Gimmicks, and Snake Oil: Why Bill Clinton's Budget Is Bad for America," March 16, 1993.)

President Bill Clinton is asking Congress to enact the largest tax increase ever imposed upon any country in history. The White House claims that this tax increase is needed to reduce the budget deficit. Yet the Administration's own projections show that adoption of the Clinton budget actually will increase the deficit, up from $310 billion this year to $431 billion by 2003. The White House claims that higher taxes will stimulate economic growth and job creation. Yet the Administration is unable to point to any country, at any point in history, that has ever taxed its way to prosperity.

Of all the President's claims, however, the most remarkable is the assertion that the budget package is a fair and balanced approach to deficit reduction. The White House maintains that the package is evenly divided between spending cuts and revenue increases. This is a breathtaking claim, given the hard numbers in the package passed by the House. Even if the Washington definition of a spending cut is accepted—increasing spending at a slower rate than previously planned—there are almost no spending cuts that the federal government, and hence the taxpayers, can take to the bank. But there are plenty of taxes. In fact, the so-called deficit reduction legislation enacted by the House of Representatives contains $15 of tax and other revenue increases for every $1 of spending cuts.

One reason why Bill Clinton's popularity ratings have fallen to record lows may be that his budget bears little resemblance to the economic plan he promised the American people during the presidential campaign last year. Clinton promised taxpayers then that he would reverse the failed tax-and-spend policies of the Bush Administration. Curiously, Clinton's budget not only makes Bush now appear a fiscal conservative by comparison, but the Clinton budget package seems to get worse for the taxpayer with each passing day.

Clinton's Tax Increase Bait and Switch



Heritage DataChart

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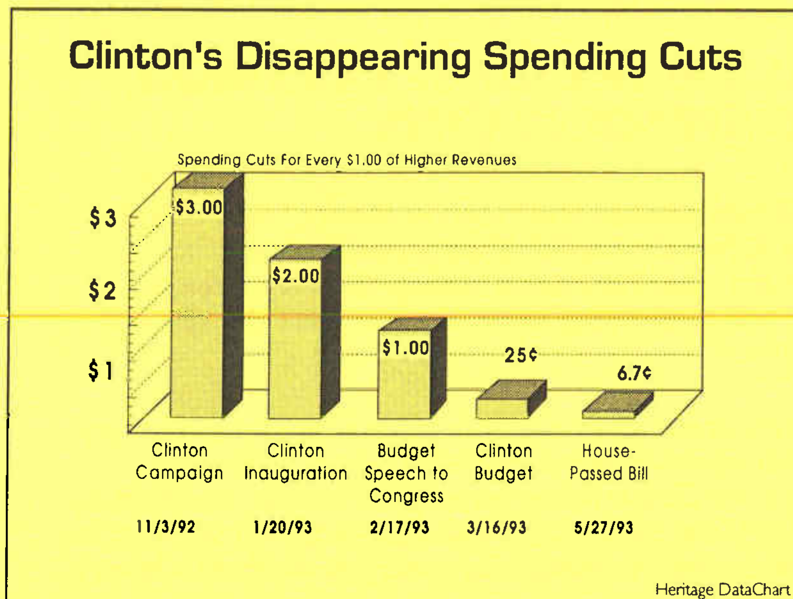
- Candidate Bill Clinton emphasized the need for spending cuts. He rightfully attacked then-President George Bush for increasing spending by more than any President since World War II . When Clinton talked about taxes, it was usually to trumpet his promised middle-class tax cut. The few times he talked about raising taxes, he promised that the only ones paying more would be those making more than $200,000 per year and foreign corporations.
- During the debate on the balanced budget amendment last year, then-House Budget Committee Chairman Leon Panetta argued against the amendment, urging Congress instead to approve legislation that would impose $3 of spending cuts for every $1 of tax increases.[1] Candidate Bill Clinton opposed the balanced budget amendment and supported the Panetta alternative.
- Once elected President, Clinton began to shift his position. Even though he had stated early in the campaign that future budget deficits were certain to be much higher than the Bush Administration estimated, he claimed that his post-election "discovery" of worsening budget projections now forced him to renege on his promise of middle-class tax cuts.
- During January confirmation hearings for Leon Panetta, Clinton's choice to head the Office of Management and Budget, Panetta stated that the Administration intended to offer a budget with $2 of spending cuts for every $1 of revenue increases.



- After Clinton was inaugurated, the ratio of spending cuts to revenue increases continued to deteriorate. Rather then $3 of spending cuts for every $1 of higher revenue, as he endorsed during the campaign, or even the $2 of spending cuts for every $1 of revenue, promised after the election, Clinton declared in his February 17 budget speech to Congress that he was going to impose $1 of taxes for every $1 of spending cuts.
- The budget that Clinton sent to Capitol Hill that day, however, did not even come close to the one to one ratio. Numerous tax increases were falsely characterized as spending cuts and many spending increases were dishonestly counted as tax cuts.[2] The effect of this accounting sleight-of-hand was to reduce artificially the reported size of the net tax increase and overstate the amount of spending cuts. In reality, the Clinton budget had nearly $4 of revenue increases for every $1 of spending cuts.
- By the time the House of Representatives had passed the so-called deficit reduction package on May 27, the ratio had become even worse. Once all the provisions are honestly accounted, there are $15 of higher revenues for every $1 of real spending cuts. To be sure, lawmakers promise that the ratio

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1 Panetta also had a version that would have relied exclusively on spending cuts. Clinton never took a no-tax-increase position, however, so it would not be fair to interpret his position as going beyond a three-to-one ratio of spending cuts to revenue increases.

2 Daniel J. Mitchell, "The House Budget Reconciliation Bill: Making a Bad Budget Even Worse," Heritage Foundation *Backgrounder Update* No. 192, May 25, 1993.

will not be as lopsided if Congress makes future cuts in the defense budget, falling back toward the four-to-one ratio of tax increases for each dollar of budget cuts. But nobody can take promised cuts to the bank. And if history is any guide, the chances of future spending cuts actually materializing are very slim.

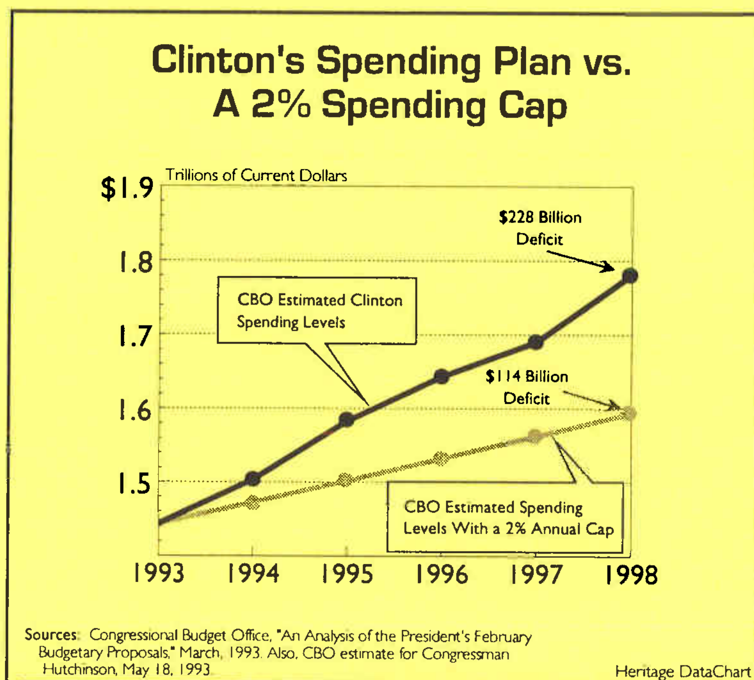
Clinton's emphasis on tax increases rather than spending cuts to reduce the deficit means that spending will continue to soar to record levels. According to the Congressional Budget Office's (CBO) analysis of the Clinton plan, total federal spending will grow $338 billion over the next five years, from $1.443 trillion in fiscal 1993 to $1.781 trillion in fiscal 1998.[3]

Yet none of the new taxes in the budget are necessary to reduce the deficit. Nor are massive cuts in government spending needed. While genuine spending cuts are economically desirable, all that is required to make serious inroads to the deficit is moderation in the annual growth of federal spending.

According to CBO, total federal outlays are expected to grow over the next five years at an average annual rate of 4.3 percent per year—or 63 percent faster than the inflation rate. But according to recent calculations performed by CBO at the request of Congressman Tim Hutchinson, the Arkansas Republican, if the growth of all federal outlays was held to 2 percent annually, just slightly below the average rate of inflation, some $633 billion could be saved over the next five years—enough to cut the deficit to $114 billion without any increase in taxes.

These savings represent nearly one-third more deficit reduction for the period than even the most generous assessment of the deficit reduction plan now being considered in Congress. As is seen in the chart below, if all of these savings were plowed back into deficit reduction, the deficit could be lowered to $114 billion by 1998, just 1.5 percent of gross domestic product (GDP), the lowest level since 1974.

By contrast, if the Clinton plan works as advertised, it will reduce the fiscal 1998 deficit to $228 billion—or to roughly 3 percent of GDP. This assumes, incidentally, that the record tax hike will have no negative impact on the economy and that Congress will not use the revenue for more spending. In other words, the largest tax increase in history would lower the $359 billion deficit projected for fiscal 1998 by only 33 percent, whereas the modest 2 percent cap on all federal spending would lower that same projected deficit by 68 percent.



Sources: Congressional Budget Office, "An Analysis of the President's February Budgetary Proposals," March, 1993. Also, CBO estimate for Congressman Hutchinson, May 18, 1993.

The recent move on the part of some Senate Democrats to replace a small portion of the Clinton package's new taxes with additional spending cuts misses the point: No new taxes are needed to lower the deficit. In March 1993, CBO estimated that tax revenues to the federal government will increase by $338 billion over the next five years without any change in current tax rates.

CBO's revenue estimate also assumes only modest economic growth over the five-year period. But based on the experi-

3 Congressional Budget Office, *An Analysis of the President's February Budgetary Proposal*, March 1993 (This calculation excludes the failed Clinton Economic Stimulus Package). The Administration admits that spending will rise by $322 billion by 1998.

ence of the 1990 budget agreement, which included a five-year net tax increase of $137 billion, another tax hike will surely dampen the economy. This will lead to lower, not higher, tax revenues and higher, not lower, deficits. In July 1990, three months before the budget agreement was signed into law, CBO estimated that tax revenues to the government would increase by $373 billion during fiscal years 1990 to 1995. But after three years of sluggish economic growth, due in large part to the added tax burden imposed by the 1990 agreement, federal tax revenues have fallen dramatically short of projections. CBO's current revenue estimates for the period covered by the 1990 budget agreement are a cumulative $534 billion below the pre-agreement estimates. Combined with the putative $137 billion tax hike, this represents a total revenue shortfall of $671 billion.

What this experience suggests is that restraining spending is the surest way of lowering the deficit. This need not require "draconian" cuts. All it requires is that the growth of total federal spending be held to the reasonable rate of 2 percent per year. Those lawmakers now supporting a record tax increase should be prepared to explain to American families why a huge tax increase, forcing severe belt-tightening by every household, is preferable to modest belt-tightening by the federal government.

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Data for the charts on pages 1 and 2 of this study were taken from the following sources: Office of Senator Phil Gramm; Confirmation Hearing for Leon Panetta, Director Designate for the Office of Management and Budget, Senate Government Affairs Committee, January 11, 1993; Address by the President to the Joint Session of Congress, February 17, 1993; "Taxes, Spending, Gimmicks, and Snake Oil: Why Bill Clinton's Budget is Bad for America," Heritage Foundation *Backgrounder* No. 932, March 16, 1993; "The House Budget Reconciliation Bill: Making a Bad Budget Even Worse," Heritage Foundation *Backgrounder Update* No. 192, May 25, 1993.