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THE SENATE REPUBLICAN BUDGET: WHY TAX CUTS MUST BE INCLUDED

(Updating *Rolling Back Government: A Budget Plan to Rebuild America*, May 1995.)

Senate Budget Committee Chairman Pete Domenici (R-NM) has proposed a budget that, if enacted, would result in a balanced budget for the first time in more than thirty years. While this effort should be applauded, particularly when compared with the ruinous fiscal policy of the past six years, the proposal needs to be strengthened by incorporating tax relief to spur growth and provide relief to families. The American people deserve to get back some of the savings reaped by the long overdue elimination and scaling back of dozens of inefficient, ineffective federal programs. The budget debate is about who controls spending. As the federal government relinquishes its control over spending decisions, Congress must allow families to retain more of their earnings to make those spending decisions themselves.

The absence of any tax relief in the Budget chairman's plan, particularly the \$500-per-child tax credit, is a dramatic and puzzling reversal by Senator Domenici. During last year's budget debate on the Senate floor, Senator Domenici vigorously supported a \$500-per-child tax credit because, he said, it would "help middle-class American families who are struggling to raise their families....[The credit] grants what we perceive to be needed and, we know, welcome relief to families of 52 million American children."¹ According to Senator Domenici, the credit would provide a typical family of four with an additional \$80 every month.²

The need for tax relief has not changed in the last year. Family incomes have been declining ever since 1989, thanks in large part to the tax increases imposed on Americans in 1990 and 1993. Moreover, the economy's performance during the current recovery lags well behind the historical average, largely because of an excessive tax burden. The modest tax relief included in the House budget proposal comes nowhere close to undoing the damage caused by those two record tax increases, but it is still a good step toward creating a tax code that rewards work, savings, investment, and entrepreneurship.

The House budget proposal demonstrates that it is possible to balance the budget while providing long-overdue tax relief to American families.

The House Budget Committee plan provides for more than \$1 trillion in savings over seven years, compared to current projections, and proposes to allow Americans to keep a little more than \$360 billion in tax relief over this same time period while reducing the deficit to zero by 2002. Chart 1 presents state estimates of the level of tax relief provided by just two of the key elements of the House tax relief proposal—the

1 *Congressional Record*, March 23, 1994, p. S3478.

2 *Ibid.*

\$500-per-child tax credit and a reduction in the capital gains tax. And in the House Budget Committee plan, projected tax collections will still rise by \$460 billion, climbing from \$1.355 billion this year to \$1.815 billion in 2002.

The Senate budget proposal can and should do the same by slowing the rate of spending growth and including additional spending reductions.

An important difference between the plans is how fast each would allow spending to grow. By limiting average annual spending growth to about 2.5 percent, House Republicans are able to provide all the tax cuts promised in the Contract with America and put an end to government borrowing in just seven years. The Senate Budget Committee's effort, by contrast, allows spending to grow by an average of 3.0 percent each year. This weaker degree of control over spending is blocking tax cuts in the Senate.

In addition, Americans should not have to bear a heavy tax burden to finance a wide array of government programs that do not work. Chart 2 provides just a few examples of the types of additional reductions in programs that could be included in the Senate budget plan. The examples shown would achieve an additional \$150.4 billion in savings to permit tax relief.

The Senate budget plan should include tax relief because both tax and spending reductions are needed to move control of spending out of Washington and into the hands of ordinary Americans. The Senate budget can include relief if the Senate slows spending growth only a little more sharply than Senator Domenici proposes. But tax relief is important for another reason. Policymakers have failed in previous efforts to balance the budget precisely because they have not linked spending reforms to tax cuts.

A package designed to balance the budget solely by limiting spending growth, such as the one pushed by Senate Republicans in 1985, will meet strong resistance from interest groups and could flounder. "Deficit reduction" packages involving tax increases have even worse results. They usually are approved, but without exception are followed by higher rather than lower deficits.

Hence, tax cuts have to be an integral part of the budget strategy to make the package more politically feasible. No matter how necessary and desirable they are, spending reforms will attract fierce opposition from interest groups. The average citizen, meanwhile, may support deficit reduction in principle, but is not likely to become politically active in support of spending control. The tax cuts in the Contract will give millions of voters a direct stake in passing the budget.

The only example of a successful spending control policy was Ronald Reagan's economic growth package in 1981. Thanks in large part to the popularity of across-the-board tax rate reductions, the American people pressured Congress to approve a limited set of spending reforms. With one major change—making sure the amount saved by spending reforms is sufficient to lead to a balanced budget—lawmakers should follow this model of success.

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Chart 1

The House Budget: Total Tax Relief from a \$500-per-Child Tax Credit and a Reduction in the Capital Gains Tax Rate

(millions of Dollars)	7-Year Total Tax Relief From \$500 per Child Tax Credit	7-Year Total Tax Relief From Reduction in Capital Gains Tax Rate	7-Year Total Tax Relief
United States	\$161,600.0	\$62,300.0	\$223,900.0
Alabama	\$2,592.6	\$600.4	\$3,193.0
Alaska	\$418.3	\$108.9	\$527.2
Arizona	\$2,307.5	\$824.2	\$3,131.7
Arkansas	\$1,624.8	\$340.1	\$1,964.9
California	\$20,533.2	\$10,244.3	\$30,777.5
Colorado	\$2,285.9	\$1,034.0	\$3,319.9
Connecticut	\$2,242.9	\$1,085.7	\$3,328.6
Delaware	\$533.1	\$156.8	\$689.9
District of Columbia	\$251.7	\$260.2	\$511.8
Florida	\$6,921.7	\$5,177.4	\$12,099.1
Georgia	\$3,800.0	\$1,356.8	\$5,156.8
Hawaii	\$915.4	\$422.3	\$1,337.6
Idaho	\$818.1	\$291.7	\$1,109.8
Illinois	\$7,752.9	\$3,391.4	\$11,144.3
Indiana	\$3,443.0	\$803.2	\$4,246.2
Iowa	\$1,987.0	\$556.9	\$2,543.8
Kansas	\$2,018.2	\$533.8	\$2,552.0
Kentucky	\$2,008.8	\$538.1	\$2,546.8
Louisiana	\$2,692.4	\$454.5	\$3,147.0
Maine	\$691.9	\$227.6	\$919.5
Maryland	\$3,218.3	\$1,193.2	\$4,411.4
Massachusetts	\$3,441.7	\$1,766.5	\$5,208.2
Michigan	\$5,786.1	\$1,532.1	\$7,318.2
Minnesota	\$2,934.0	\$1,067.6	\$4,001.6
Mississippi	\$1,674.8	\$268.2	\$1,943.0
Missouri	\$3,040.5	\$953.0	\$3,993.5
Montana	\$613.5	\$225.3	\$838.8
Nebraska	\$1,325.7	\$370.0	\$1,695.7
Nevada	\$768.5	\$677.7	\$1,446.2
New Hampshire	\$763.6	\$387.5	\$1,151.1
New Jersey	\$4,719.5	\$1,774.3	\$6,493.8
New Mexico	\$997.5	\$242.2	\$1,239.7
New York	\$11,080.9	\$5,281.4	\$16,362.4
North Carolina	\$4,212.4	\$1,233.9	\$5,446.4
North Dakota	\$454.9	\$145.6	\$600.5
Ohio	\$7,414.2	\$1,758.4	\$9,172.5
Oklahoma	\$1,998.3	\$413.8	\$2,412.1
Oregon	\$1,883.2	\$904.6	\$2,787.8
Pennsylvania	\$7,770.9	\$2,220.3	\$9,991.2
Rhode Island	\$494.2	\$253.5	\$747.7
South Carolina	\$2,411.0	\$540.2	\$2,951.2
South Dakota	\$490.7	\$208.0	\$698.7
Tennessee	\$2,571.8	\$961.6	\$3,533.3
Texas	\$11,245.0	\$3,598.5	\$14,843.5
Utah	\$1,467.4	\$297.2	\$1,764.5
Vermont	\$359.7	\$143.4	\$503.1
Virginia	\$3,986.6	\$1,460.7	\$5,447.3
Washington	\$3,537.4	\$2,029.9	\$5,567.3
West Virginia	\$1,074.4	\$153.2	\$1,227.6
Wisconsin	\$3,643.9	\$1,125.5	\$4,769.4
Wyoming	\$380.2	\$167.1	\$547.3

Note: The figures presented here represent the tax relief provided by HRI 215 as passed by the House of Representatives and included in the House Budget Committee's "Chairman's Mark." The Heritage Foundation budget plan assumes even larger tax relief.

Sources: Joint Committee on Taxation; U.S. Bureau of the Census; and the Internal Revenue Service.

How the Senate Budget Committee's Plan Could be Strengthened to Permit Tax Cuts

From the Senate Budget Plan

From the Heritage Plan

Function 150 - International Assistance

Consolidating and reducing programs of AID by \$2.7 billion and reducing aid to Europe by \$1.7 billion.

Close down the Agency for International Development and reduce bilateral assistance by 50%.

Function 270 - Energy

Continuing to provide a total of \$21 billion over the next five years for Federal energy research and development efforts.

Terminate all Federal energy related research and development programs.

Function 300 - Natural Resources and Environment

Reducing NOAA funding by 5 percent over 5 years.

Reduce spending for NOAA by 50 percent over 3 years

Function 350 - Agriculture

Reducing agricultural research by only 10 percent and making undefined reforms to the income subsidy and price support programs through the 1995 farm bill.

Phase out all farm income subsidy and price support programs and end all export promotion programs. Reduce agricultural Research by 50 percent.

Function 450 - Community and Regional Development

Consolidating several programs into a rural development block grant and reducing outlays by only \$.7 billion.

Eliminate all Department of Agriculture rural development grants and loan guarantee programs.

Function 500 - Education, Training, Employment, & Social Services

Reducing funding for National Endowments for the Arts and Humanities by only 50 percent.

Eliminate federal funding for the National Endowments of the Arts and Humanities.

Function 920 - Allowances - Cross Agency Reforms

Establishing a non-partisan commission to make recommendations on the CPI.

Readjust the flawed cost-of-living calculations employed by the federal government.

Total 5 Year Savings: \$19.4 billion

\$169.8 billion

Note: These examples are from the Heritage Foundation's budget, "Rolling Back Government: A Budget Plan to Rebuild America.," and from the Senate Budget Committee's "FY 1996 Balanced Budget Resolution: Chairman's Mark."