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Congress Should Not "Pay for" Stopping Taxmageddon Tax Increase

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Taxmageddon is a massive one-year $500 billion tax increase that is poised to strike the economy on January 1, 2013. It is mostly the result of tax policies that expire at the end of the year.[1]

Congress has been slow to stop Taxmageddon in part because of a common misconception that doing so would be a tax cut that adds to the deficit. On the contrary, preventing Taxmageddon would prevent a tax hike and is thus deficit neutral relative to current policy.

CBO Revenue Baseline Cause of Misconception. The misconception that stopping Taxmageddon adds to the deficit stems from a flaw in how the Congressional Budget Office (CBO) constructs the baselines Congress follows for budgetary purposes.

The baselines project what Congress will spend in future years and how much revenue it will raise in those years. The difference between the spending and revenue projections is the deficit in a given year. Congress measures its spending and tax policy changes against those baselines to determine how those policies impact the projected deficit.

The flaw is that CBO constructs the two baselines on different premises. The CBO creates its spending baseline based on current *policy*. For instance, spending on the highway program and the Children's Health Insurance Program, as well as all discretionary-spending authorization, expires at regular intervals. Since these programs constitute current policy, the CBO assumes that Congress will extend these spending programs and the spending will continue—with built-in increases for inflation.

In constructing its revenue baseline, however, the CBO takes a decidedly different approach by assuming current *law*. This means that the CBO assumes that any impending expiring tax policies, such as the Bush tax cuts and the payroll tax cut, will be revenue increases in the baseline. The CBO also assumes that new policies already enacted but delayed, such as the tax hikes in Obamacare, will increase the revenue baseline. The CBO does this even though Congress, usually after much delay, traditionally keeps expiring tax policies in place—and even though future Congresses are under no obligation to allow tax increases passed by previous Congresses, but not yet implemented, to begin.

In effect, when spending authorization expires, the CBO implicitly assumes that Congress actually intends for it to continue. Yet when tax provisions expire, the CBO assumes that Congress truly intends for them to expire.

Current Law and Current Policy Baselines Widely Divergent. The CBO's uneven treatment of spending and taxes would be a minor annoyance if tax policy remained generally stable from year to year. In such an event, the CBO's current law revenue baseline would essentially be identical to a current policy baseline. But the current law revenue baseline is now widely divergent from a current policy baseline, because the tax code is increasingly composed of tax policies that expire and some that are enacted but delayed for years. Congress's bad habit of setting temporary or expiring tax policy has led

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to Taxmageddon, because so many expiring policies have converged to end simultaneously.

For example, for fiscal year (FY) 2013, CBO current law baseline estimates that the federal government will raise $2.968 trillion in revenue.[2] This estimate includes increased revenue from the expiration of Taxmageddon policies and the beginning of several Obamacare tax increases.

A current policy baseline assumes that Congress keeps in place all the expiring tax policies that make up Taxmageddon and excludes all the tax hikes in Obamacare not yet in effect. As such, it would estimate revenue to be roughly $2.445 trillion in FY 2013. The approximately $500 billion difference between the two baselines reflects the CBO's latest estimate of the size of Taxmageddon for FY 2013 plus the projected revenue from the Obamacare tax increases.[3]

The CBO's Flawed Baseline Incorrectly Calls Stopping Taxmageddon a Tax Cut. The CBO's assumption, under its current law baseline, that revenue will rise sharply because tax cuts will expire and delayed Obamacare tax hikes will take effect leads it to wrongly imply that stopping Taxmageddon is a tax cut that adds to the deficit. The CBO scores any tax policy change that reduces estimated revenue below the $2.968 trillion current law revenue projection it anticipates for FY 2013 as a tax cut. This would include the prevention of Taxmageddon, since that figure first incorporates revenue increases from Taxmageddon policies.

Extending tax cuts or delaying new tax increases adds to the deficit under the CBO's calculations. Under budgeting rules currently in place, a policy change that increases the deficit requires Congress to "pay for" that policy or "offset" its cost. If Congress adheres to the CBO's flawed current law baseline that wrongly calls stopping Taxmageddon a tax cut, it will need to search for spending cuts and tax increases totaling about $500 billion for 2013.

Stopping Taxmageddon Prevents a Tax Hike. In contrast, a current policy baseline would not score stopping Taxmageddon as a tax cut that increases the deficit. It would continue to project revenue of $2.445 trillion once Congress prevented Taxmageddon, because it would have previously assumed that Congress was going to extend or (in the case of the Obamacare tax increases) stop the implementation of the policies that comprise Taxmageddon.

Since it is not a tax cut, and therefore does not add to the deficit, neither spending reductions nor tax increases are necessary to offset, or pay for, stopping Taxmageddon when using a more rational, current policy baseline.

As even the Obama Administration acknowledges, the current policy baseline is the right baseline for Congress to follow, because it is consistent with the spending baseline and leads to the commonsense perspective that continuing a policy in effect now for a dozen years is not a tax cut.[4] The CBO is the outlier when it comes to constructing a proper revenue baseline.

Keeping the expiring Taxmageddon policies in place, and delaying the imposition of the Obamacare tax hikes, is not a tax cut, because doing so would not lower anyone's taxes. It would stop them from rising. If Congress decided to raise taxes to pay for stopping Taxmageddon, it would create an oxymoron in which it would be raising taxes to prevent a tax increase.

The ultimate arbiters of what is and what is not a tax cut are the taxpayers themselves. Congress would be hard pressed to convince them that it cut their taxes because it declined to take more of their hard-earned money by stopping Taxmageddon. Those who make such an argument quickly end up on

1. See Curtis S. Dubay, "Taxmageddon: Massive Tax Increase Coming in 2013," Heritage Foundation *Issue Brief* No. 3558, April 4, 2012, http://www.heritage.org/research/reports/2012/04/taxmageddon-massive-tax-increase-coming-in-2013.
2. Congressional Budget Office, "Updated Budget Projections: Fiscal Years 2012 to 2022," March 2012, http://www.cbo.gov/sites/default/files/cbofiles/attachments/March2012Baseline.pdf (accessed June 4, 2012).
3. Congressional Budget Office, "Economic Effects of Reducing the Fiscal Restraint That Is Scheduled to Occur in 2013," May 2012, http://www.cbo.gov/sites/default/files/cbofiles/attachments/FiscalRestraint_0.pdf (accessed June 4, 2012). The CBO's estimate for Taxmageddon's size includes two separate figures that need to be added together to get the full size of the tax increase. Both are on page 4 of the report. First is the $399 billion subtotal for "Changes in Specified Revenue Policies." The second is the $105 billion figure for "Other Changes in Revenue and Spending." In a footnote, the CBO says the $105 billion figure "mostly reflects changes in revenue." It is not possible to determine what portion of the $105 billion are revenues and spending, so the $500 billion figure reported here is an approximation, given the information reported by the CBO.
4. J. D. Foster, "Obama Gets a Tax Issue Right—Is Congress Next?," Heritage Foundation *WebMemo* No. 2491, June 18, 2009, http://www.heritage.org/research/reports/2009/06/obama-gets-a-tax-issue-right-is-congress-next.

TABLE 1

Taxmageddon: $494 Billion Tax Increase Is Coming

These tax hikes will occur if President Obama and Congress do not act before the end of the year.

FIGURES ARE IN MILLIONS

TAX POLICIES SET TO EXPIRE ON JANUARY 1, 2013	TAX INCREASE IN 2013
Bush tax cuts	$165,750
Payroll tax cut	$124,636
Alternative Minimum Tax (AMT) patch	$118,750
Tax cuts from 2009 stimulus	$20,876
Tax extenders	$20,465
Death tax at 35 percent with $5 million exemption	$13,000
100 percent expensing for business investment	$7,695
TAX POLICIES SET TO BEGIN ON JANUARY 1, 2013	**TAX INCREASE IN 2013**
Tax hikes in Obamacare	$22,750
Total	**$493,922**

Sources: U.S. Office of Management and Budget, *Budget of the United States Government, Fiscal Year 2013* (Washington, D.C.: U.S. Government Printing Office, 2011), at http://www.whitehouse.gov/sites/default/files/omb/budget/fy2013/assets/budget.pdf (accessed March 28, 2012); Joint Committee on Taxation, "Estimated Budget Effects of the 'Tax Relief, Unemployment Insurance Reauthorization, and Jobcreation Act of 2010,'" December 10, 2012, at http://www.jct.gov/publications.html?func=startdown&id=3715 (accessed March 28, 2012).

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troubled rhetorical ground. To argue that not raising taxes is a tax cut, or is in some way a cost to the government, is to assume that money the taxpayers earned was in fact the government's first.[5]

Stop Taxmageddon Without Offsets Right Away. Taxmageddon is causing widespread uncertainty that is slowing the economy right now,[6] and, if it hits on January 1, 2013, the blow it would deliver to the already staggering economy would be severe.

Congress should not delay stopping Taxmageddon by engaging in unnecessary attempts to pay for phantom revenue losses. Congress should evaluate stopping Taxmageddon against a current policy baseline, which would clearly show that stopping Taxmageddon is not a tax cut and does not raise the deficit and that therefore Congress does not need to pay for stopping it. The sooner it realizes this and votes to stop Taxmageddon, the better.

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5. Keith Hennessey, "Government Doesn't Give Tax Cuts, It Takes More or Less Taxes," KeithHennessey.com, April 26, 2012, http://keithhennessey.com/2012/04/26/take-not-give/ (accessed June 4, 2012).
6. See Curtis S. Dubay, "Congress Needs to Act Now on Taxmageddon," The Heritage Foundation, The Foundry, http://blog.heritage.org/2012/05/04/pimco-echoes-heritage-on-taxmageddon-congress-needs-to-act-now/.