CENTER ON BUDGET AND POLICY PRIORITIES

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HOW MUCH WOULD THE BUSH TAX CUT COST?

The full report can be viewed at http://www.cbpp.org/2-6-01tax.htm

On February 6, the Center on Budget and Policy Priorities issued an analysis, "Cost of the Bush Tax Cut Rises; Making Rate Cuts Retroactive Adds $400 Billion." The report concludes that the tax cut plan proposed by the Administration could cost as much as $2.5 trillion over a ten year period. The report makes the following points:

- **Total Ten-year Costs Rise From $1.3 Trillion to $2.1 Trillion:** The Bush tax cut, when properly measured, costs $2.1 trillion over the ten-year period 2002-2011, rather than the $1.3 trillion figure used in the campaign and the $1.6 trillion figure used by the Bush Administration and commonly cited by the press.[1] The $2.1 trillion figure takes into account both the extra federal interest costs automatically generated by the tax cut and the inevitable costs of fixing the Alternative Minimum Tax (AMT).

- **The Alternative Minimum Tax (AMT):** The AMT was established to prevent wealthy taxpayers from engaging in so much tax shelter activity that they owe little or no income tax. Some 1.3 million taxpayers were subject to the AMT last year. Due to a flaw in the AMT's design, however, it will encroach heavily upon the middle class in the coming year if Congress does not act to prevent that from occurring, causing 15 million taxpayers to be subject to the AMT by 2010. Virtually all observers agree policymakers will act to prevent that from taking place. This anticipated action to remedy the flaw in the AMT law will increase the cost of the Bush tax plan by $200 billion over 10 years. The estimate that the Bush plan will cost $1.6 trillion over ten years is actually an estimate that the plan will cost $1.8 trillion, but $200 billion of these costs will be cancelled out by the effects of a swollen AMT.

- **Additional Interest Costs of $400 Billion:** CBO's new budget projections assume that no tax cuts or spending increases will be enacted over the next decade and therefore that the debt will fall rapidly. As a result, the costs of interest on the debt — a component of federal spending — also will fall rapidly. If a ten-year, $1.6 trillion tax cut is enacted, however, surpluses will be smaller and the debt larger than CBO projects, and interest costs will be almost $400 billion higher than CBO assumed when developing its estimate of the surplus.

- **Accelerating the Tax Cut Could Increase Costs to $2.5 Trillion:** When President Bush announced his tax package on February 8, he expressed support for accelerating a portion of his tax cuts to the beginning of 2001. He did not specify which aspects of the plan should be accelerated, but offered to work with Congress to achieve this goal. If the rate cuts in his plan, which are not scheduled to become fully effective until 2006, are placed in full effect retroactive to January 1, 2001, and these added costs are not offset by scaling back other parts of the plan, the ten-year cost of the plan rises another $400 billion, to $2.5 trillion.

The total costs of the proposed ten-year tax cut thus includes $1.6 trillion in revenue losses over the period 2002-2011, another $200 billion in revenue losses caused by the changes that inevitably will be made to the AMT so that it will not encroach heavily upon the middle class, and an additional $400 billion in interest costs. The total (with rounding) is $2.1 trillion over ten years. The total rises to $2.5 trillion if the proposed rate cuts are made effective immediately rather than being phased in gradually through 2006 and these added costs are not offset by scaling back other parts of the plan.

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[1] The figure of $1.3 trillion covered the *nine* years from 2002 through 2010, whereas the figure of $1.6 trillion covers the full ten-year period 2002-2011.