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# AVAILABLE BUDGET SURPLUS IS SMALLER THAN MANY REALIZE

## Concord Coalition and Brookings Experts Join in Releasing New Center Analysis

On January 4, the Center on Budget and Policy Priorities issued an analysis of the likely dimensions of projected budget surpluses and whether those surpluses are sufficient to accommodate a large tax cut. Joining the Center at the National Press Club in releasing this report were Robert Bixby, executive director of The Concord Coalition, and William Gale, a senior fellow at the Brookings Institution. Bixby and Gale largely concurred in the report's findings.

The analysis examines three issues: the likely size of the non-Social Security surplus under new projections that the Congressional Budget Office will issue shortly; how much of that surplus amount actually will be available for tax cuts and program initiatives; and how the size of the available non-Social Security surplus compares with the size of the tax cut President-elect Bush has proposed.

The analysis states that CBO is likely to place the size of the non-Social Security surplus at $2.5 trillion to $3.0 trillion over 10 years, modestly higher than the $2.4 trillion estimate the White House recently issued. The report also explains, however, that as previous analyses issued by the Center, Brookings, and the Concord Coalition have noted, there is a substantial difference between CBO's estimate of the size of the non-Social Security surplus and the amount actually available for tax cuts and program expansions.

In making its surplus estimates, CBO must follow certain rules that require it to assume that various tax increases and program reductions that neither party favors — and that are extremely unlikely to take place — will go into effect. For example, the CBO forecast mechanically assumes that about 20 popular tax credits that always are extended for two years at a time and enjoy strongly bipartisan support will be allowed to expire in the next year or two, with taxes on the individuals and businesses who use those credits being raised as a consequence. In addition, the CBO projection includes the surplus in the Medicare Hospital Insurance trust fund, which large bipartisan majorities in both chambers of Congress voted last year to set aside and not use for tax cuts or program increases.

The Center's report estimates that when the Medicare component of the surplus is set to the side and the more prudent and realistic assumption is made that the tax increases and program reductions reflected in the CBO projection will not occur (and that current tax and program policy in these areas will remain in effect instead), the size of the available surplus is reduced by at least

$1 trillion. Thus, about $1.5 trillion to $2.0 trillion is available over the next 10 years, rather than $2.5 trillion to $3.0 trillion.

At the press conference both Bixby and Gale stated that even the Center's estimates overstate the size of the available surplus because those estimates assume levels of discretionary spending that, while more realistic than those in the CBO projections, are still unrealistically low. The Center's estimate of the surplus assumes that discretionary spending will keep pace with inflation and population growth over the next 10 years but decline as a share of the economy (i.e., of the Gross Domestic Product). Since budget surpluses began to emerge three years ago, discretionary spending has kept pace with GDP. If discretionary spending is assumed to remain constant as a share of GDP, the size of the available surplus is $600 billion smaller.

The Center's analysis cautions that given Congress' oft-stated desire to devote all of the Social Security and Medicare surpluses to debt reduction, it would not be prudent for the 107th Congress to commit to tax cuts and program increases *all* of the surplus that is realistically available, for at least three reasons.

- The estimates of the surplus are only projections and may not fully materialize. If the economy grows just a little less rapidly than CBO forecasts or health care costs rise faster than projected, the actual surpluses will be substantially smaller. Bixby of the Concord Coalition noted that under recent CBO projections, two-thirds of the projected surpluses do not show up until the second five years, the period when the projections are the most uncertain.

- Even if CBO's economic forecast proves precisely correct and the full $1.5 trillion to $2.0 trillion in potentially available surpluses materializes, action by the 107th Congress and the President now to commit all of that surplus for the next decade will leave no resources to meet needs that inevitably will arise in the remaining eight years of the 10-year period. It is inconceivable that no new military, international, or domestic problems that require resources will arise over that period. Adding to this concern, both the CBO projection and the Center's estimate of the available surplus do not account for funds that will be needed over the coming decade to address problems that arise from natural disasters (e.g., hurricanes, floods, and tornados).

- At least $500 billion from the non-Social Security surplus is ultimately likely to be needed as part of reform proposals to restore long-term solvency to Social Security and Medicare, regardless of whether Social Security is partially converted to private accounts, because the magnitude of the Social Security and Medicare benefit reductions or payroll tax increases that otherwise would be required will almost certainly make solvency packages impossible to pass.

## The Size of The Bush Tax Cut

Finally, the Center's analysis explains that the tax cut that President-elect Bush has proposed would consume a little more than $2 trillion of the surpluses over the next 10 years. The $1.3 trillion figure often used for the cost of the Bush tax cut was generated last spring by the Joint Committee on Taxation and covered the period from 2001 through 2010. Because the cost of the tax cut would be zero in 2001, this essentially was a nine-year estimate. Now the 10-year budget period has shifted to 2002-2011 (the same period the new surplus projections cover), which means that the tax cut's cost in 2011 — which is about $240 billion — must be added.

In addition, the old $1.3 trillion figure is based on the assumption that a significant portion of the tax cut will be taken back from middle-class taxpayers, because Congress and the Administration will allow the Alternative Minimum Tax to raise the taxes that millions of middle-class families otherwise would owe, canceling out a portion of the Bush tax cut. No knowledgeable observer, however, expects policymakers to allow the AMT to encroach upon the middle class in this fashion; a resolution of this problem in the AMT, which is widely expected, will add about $200 billion to the cost of the tax cut, according to Joint Tax Committee estimates. Finally, the $1.3 trillion figure does not include the additional interest payments that will have to be paid on the national debt if a large share of the surplus is used for a tax cut rather than for paying down debt. Under CBO's formula for calculating interest costs, the additional interest payments amount to about $400 billion.

As a result, the Bush tax cut would consume approximately $2.1 trillion of the projected surpluses. The speakers at the press conference noted this exceeds the size of the realistically available surplus, even before one takes into account additional Bush proposals for such items as prescription drugs and health insurance, additional expenditures or tax cuts that Congress may favor, and the likely need to preserve some of the non-Social Security surplus for legislation to restore long-term Social Security and Medicare solvency.