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Ways and Means Proposal Departs from Bipartisan Principles for Effective Stimulus And Offers Little Help to the Unemployed

The full report can be viewed at http://www.cbpp.org/10-17-01tax.htm

On October 17, the Center on Budget and Policy Priorities released an analysis of the economic stimulus legislation the House Ways and Means Committee approved on October 12. The legislation consists overwhelmingly of tax cuts — most of which are for corporations or would disproportionately benefit upper-income families — and provides scant assistance to unemployed workers. Over 95 percent of the legislation consists of tax cuts; over 85 percent of it is composed of tax cuts for corporations and businesses and upper-income people. Essentially, this legislation is a vehicle for tax cuts that have little to do with boosting the economy now or assisting unemployed workers but that have long been sought by powerful interest groups and favored by some in Congress for ideological reasons. Furthermore, because some of the corporate tax cuts in the legislation are permanent and others may be politically difficult to let expire, the package poses a threat to long-term fiscal discipline. The report's findings include:

- Only a small fraction of unemployed workers would receive added unemployment insurance benefits when their regular benefits run out or secure any assistance in maintaining their health insurance under this bill. It speeds up the transfer of $9 billion already slated to be shifted from the federal unemployment insurance trust funds to state unemployment accounts, but these funds would largely be used to build up the reserves in these accounts and would *not* be spent. The Congressional Budget Office estimates that only $3.6 billion of this $9 billion would actually be spent, and some of that would go for administrative costs rather than unemployment benefits. The additional benefits that would be provided to jobless workers would be a pittance compared to the $35 billion (in 2002 dollars) of additional weeks of federal unemployment benefits provided during the recession of the early 1990s.

  The $3 billion that the legislation would provide through the Social Services Block Grant for health coverage for unemployed workers is similarly inadequate. More comprehensive proposals to help the unemployed maintain health insurance (by providing subsidies for COBRA premiums and additional Medicaid coverage) have been estimated to cost five to eight times as much.

- The legislation includes four permanent tax cuts, including a reduction in the capital gains tax rate and repeal of the corporate Alternative Minimum Tax (AMT). This violates the principles for a sound and fiscally responsible stimulus package that the chairs and ranking minority members of the House and Senate Budget Committees issued on October 4. Those principles call for stimulus measures to be temporary, to last no more than 12 months to the extent that is practicable, and not to worsen the long-term budget outlook.

- Most of the tax cuts that are temporary nonetheless extend beyond 2002, by which time most forecasters anticipate the economy will have recovered. For instance, the bill would accelerate reductions in the 28 percent individual income tax rate that were enacted in June and scheduled to take effect in 2004 and 2006; three-quarters of the cost of this proposal would occur after 2002. Similarly, the bill's temporary corporate and business tax cuts would expire in either 24 months or 36 months. This raises a further concern: because these business tax cuts extend beyond the period when the economy is expected to require stimulus, they may come to be viewed as standard features of the tax code by the time they are scheduled to expire. As a result,

Percentage Share of the Costs in 2002 and Over Ten Years of the Provisions in the Ways and Means Package*	**2002**	**10 years**
Corporate and business tax cuts	68.6%	42.5%
Tax cuts primarily for upper-income taxpayers	14.5%	43.2%
Tax cuts primarily for low- and moderate-income taxpayers	13.3%	8.2%
Provisions for unemployed workers	3.2%	4.0%
Extension of expiring tax provisions	0.4%	2.0%
Total	100.0%	100.0%

* Excludes technical amendments and revenue effects of unemployment trust fund changes.

Congress may be more likely to continue them just as it routinely extends other expiring corporate tax provisions each year — at a very large cost. If just the provision to allow "partial expensing" of business investment were made permanent, rather than permitted to expire after three years as called for in the bill, the cost of the legislation will grow by about $250 billion over 10 years, to more than $400 billion.

- Cutting the capital gains rate is an inappropriate way to generate economic stimulus, a point that was made by both Federal Reserve Chairman Alan Greenspan and former Treasury Secretary Robert Rubin in recent Congressional briefings. The Congressional Research Service similarly found that "a capital gains tax cut appears the least likely of any permanent tax cut to stimulate the economy."

- Repealing the corporate AMT would also be ineffective as a stimulus, since it creates little incentive for firms to undertake new investments. A recent Brookings Institution analysis finds that approximately 90 percent of the tax benefits in 2002 of repealing the corporate AMT would accrue to profits on old (rather than new) investments and that this proposal consequently would be highly inefficient as a stimulus measure. Furthermore, the Ways and Means package requires the Treasury to write checks to corporations to refund certain past corporate AMT payments; the result of this would be a windfall for a number of large corporations. According to an analysis by Citizens for Tax Justice, the proposed changes to the corporate AMT would provide more than a dozen major corporations — including IBM, General Motors, and various energy companies — with tax breaks of *over $100 million each.* The total benefit to corporations from the corporate AMT provisions would be $25 billion in 2002, with the vast majority of this money being provided as tax refund checks the Treasury would write them. The amount of these corporate refund checks would exceed the total for the "rebate" checks that would be sent to over 40 million low- and moderate-income taxpayers under another provision of the bill.

- Except for the "rebate" for low- and moderate-income taxpayers, all of the other individual tax cuts would disproportionately benefit upper-income taxpayers. According to both IRS and CBO data, accelerating the reduction of the 28 percent rate to 25 percent would benefit only the top one-quarter of the income spectrum, not those in the middle, as its supporters frequently claim. The capital gains tax cut is even more skewed: CRS data show that 80 percent of the benefits would accrue to the top two percent of taxpayers (those with incomes over $200,000). Not only are higher-income families more likely to have the resources to weather an economic slowdown, but research has shown that they are more likely to save, rather than spend, a larger share of additional income. Yet to stimulate the economy, tax-cut benefits must be spent.

- Finally, accelerating the reductions in the 28 percent rate would deny policymakers the option of deferring or cancelling these rate reductions when they face tough fiscal decisions once the recession ends and the need to exert fiscal discipline returns. New estimates issued by the chairs and ranking members of the House and Senate Budget committees show that even without a stimulus package, essentially the entire non-Social Security surplus over the next ten years has disappeared and much of the Social Security surplus will likely have to be tapped as well.