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CONGRESSIONAL LEADERSHIP PUSHES FOR EXTENDING EXPIRING TAX BREAKS, BUT IGNORES EXPIRING UNEMPLOYMENT BENEFITS

House extends large corporate tax break first enacted in 2002 stimulus package, while Majority Leader says economic conditions mean unemployment extension is unnecessary

By Joel Friedman, David Kamin, and Isaac Shapiro

When Congress returns from its Thanksgiving break on the week of December 8, it will be under pressure to complete action on legislation that would extend more than a dozen tax breaks scheduled to expire at the end of the year. The House passed a tax-cut "extenders" package before the break, but the Senate did not. Despite efforts to ensure that an "extenders" package is enacted before the end of the year, Congressional leaders have shown no willingness to consider extending the temporary federal program to help the long-term unemployed, which, starting December 21, will not provide any benefits to those who newly exhaust their regular, state-funded benefits.

In addition, the House version of the tax-cut extension bill would continue a large, supposedly temporary corporate tax break that was enacted as part of the 2002 stimulus legislation. When it comes to the unemployment benefits, however, House Majority Leader Tom DeLay told *BNA Daily Labor Report* on November 19 that there is "no reason" for extending those benefits. The House approach implies that corporations need continued support amidst a still-weak economy, but that laid-off workers do not. This is despite the fact that firms might not use the tax breaks to hire new workers and that the unemployed workers who have their benefits run out will be receiving neither paychecks nor unemployment benefits.

Representative DeLay's contention that there is no basis for extending unemployment benefits is strongly contradicted by the evidence:

- In key respects, even with the recent upturn in job growth, the labor market is weaker today than when the temporary federal unemployment benefits program was established by the March 2002 stimulus legislation. The current unemployment rate is higher, and there are more unemployed workers, fewer jobs, and much more long-term unemployment. In fact, the number of individuals out of work for at least 26 weeks was more than 50 percent greater in October 2003 than in March 2002.

- If no Congressional action is taken to extend the unemployment benefits program starting December 21 between 80,000 and 90,000 unemployed workers will exhaust their regular unemployment benefits *every week* without being able to receive any federal unemployment benefits to help them make ends meet as they continue to look for work.

- The number of workers exhausting their regular unemployment benefits — and thus in need of temporary federal benefits — is much larger today than when the temporary federal program enacted in response to the downturn of the early 1990s was ended.

It should also be noted that Congressional leaders are proposing to extend various tax breaks for six months to a year, thereby maintaining the fiction that these tax breaks are temporary, when virtually all knowledgeable observers agree that these tax breaks will continue being extended each time they are about to expire and likely never will be permitted to terminate. According to the Congressional Research Service, *only one* "temporary" tax provision has been allowed to expire *in the last 25 years*.[1] As a result, the official estimate of the cost of extending these tax breaks for six months to a year substantially understates the true cost of these tax breaks over time, and hides their long-term effects on a federal budget that already faces large deficits for the foreseeable future.

Moreover, if the House corporate tax provision is included as part of the extenders package this year, that will set a precedent for this provision to be automatically considered as part of the package of "extenders" in future years. Thus, a large, supposedly temporary corporate tax break included in the 2002 stimulus package may become an ongoing feature of tax law. Under the House bill, this provision would reduce corporate taxes by $19 billion in 2004. If this corporate tax provision really is allowed to expire after one year, as the official cost estimate for the House bill assumes, most of the revenue loss in 2004 would be offset by increased revenue collections in subsequent years, and the total revenue loss from the provision would be $5 billion over the ten-year period. But if this provision instead becomes part of the list of tax measures that are routinely extended whenever they are slated to expire — a development toward which the House bill takes a large step — the provision could cost tens of billions of dollars over the coming decade.[2]

The True Cost of Extending the Expiring Tax Breaks

Congress seems intent on pushing through legislation to extend expiring tax breaks. The House of Representatives passed its tax-cut "extenders" bill, which extends 14 separate tax breaks, by voice vote with less than one hour of debate on November 20. In the Senate, Finance Committee Chairman Charles Grassley and ranking member Senator Max Baucus introduced an extenders bill. The House bill would reduce revenues by $7 billion over ten years; the Senate bill is advertised as being deficit neutral because it offsets the cost of the tax cuts with revenue-raising provisions.

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[1] Jill Barshay, "'Temporary' Tax Breaks Usually A Permanent Reality," *CQ Weekly*, November 15, 2003.

[2] This provision would allow corporations to carry back net operating losses for five years and use loss deductions against the corporate Alternative Minimum Tax. This provision essentially allows corporations to take certain deductions in the current year rather than in future years. Relative to current law, this timing shift results in a revenue losses in 2004 and revenue gains in the subsequent years (as corporations take smaller deductions in those years). If it is extended beyond 2004 and remains in effect over the full ten years, however, its cost will be much higher.

These official cost estimates are misleading, however, as they understate the likely impact on the budget. The tax cuts in these bills would be extended for short periods — typically six months in the Senate bill and one year in the House bill. It is a virtual certainty, however, that these tax breaks will be extended again and again in future years. Once extended, these tax cuts will add billions more to the deficit.

- The Senate tax-extension bill is technically revenue neutral over ten years; it includes $1.2 billion in tax cuts and $1.2 billion in revenue raisers. But its costs are front-loaded, since most of the tax cuts in the bill are extended for only six months. The revenue-raising provisions, on the other hand, would be in effect for up to the full ten years covered by the cost estimate. If all provisions — both the tax cuts and offsets — remain in effect throughout the ten-year period, as likely would be the case, the cost will be $24 billion over ten years.

- This $24 billion in revenue losses would result in $6 billion in costs in additional interest payments on the federal debt, so the total impact on the deficit would be $30 billion over ten years.

- The bill that the House has approved is more costly. As noted, if the new corporate tax provision it includes really is allowed to expire after one year, as the official cost estimate for the House bill assumes, the total revenue loss from the provision would be $5 billion over the ten-year period. But if this provision is extended in future years, it could cost tens of billions of dollars over the next decade.

Problem of Tax Extenders Will Grow Worse In Future Years

The passage of a package of tax extenders has been a Congressional ritual in recent years. This practice has always been a poor way to carry out tax policy, creating unnecessary uncertainty in the tax code and masking the true long-term cost of the tax-cut provisions. If Congress wishes to extend these provisions, it would be more appropriate to enact permanent tax changes and to offset fully the resulting costs.

It would be wise for Congress to establish such a precedent, since dealing with temporary tax provisions will become a much more substantial problem in future years. With the enactment of the 2001 tax bill, the number and cost of temporary tax provisions has exploded. Policymakers have come to rely on writing large new tax cuts into law for seemingly temporary periods in order to "game" the system and conceal the true, long-term cost of the measures in question. The Congressional Budget Office now estimates that the ten-year cost of permanently extending all of the tax provisions that are scheduled to expire before 2013 amounts to a whopping $2.1 trillion.[3]

[3] Congressional Budget Office, *The Budget and Economic Outlook: An Update,* August 2003, Table 1-6. This number includes CBO's estimate of a realistic alternative minimum tax (AMT) relief package, amounting to $548 billion, including interaction with other provisions. Current AMT relief expires at the end of 2004.

A study by William Gale and Peter Orszag of the Brookings Institution on the costs of extenders underscores how large this issue is about to become. Gale and Orszag, looking at various ten-year periods, estimated the cost of extending tax provisions that were scheduled to expire during each period. They found, for instance, that the cost in January 2001 of extending expiring tax provisions was $22 billion in the tenth year of the period. Now, however, following enactment of recent tax-cut legislation, the cost in the tenth year would be $430 billion.

Misguided priorities

> "'I see no reason, particularly with a 6.1 percent unemployment rate, to be extending unemployment compensation,' [House Majority Leader Tom] DeLay said. Currently, he added, 'every economic indicator is better than in 1993, when the Democrats ended the [federal] unemployment program.'"[4]

In March 2002, the Temporary Extended Unemployment Compensation program was established to provide additional federal benefits to those who exhaust their regular, state- funded benefits. The TEUC program is scheduled to phase down sharply at the end of the year. Starting December 21, workers who exhaust their regular unemployment benefits will not be eligible for additional weeks of benefits through the federal TEUC program[5]. The only people who will continue to receive TEUC benefits will be those who exhausted their regular benefits before December 21.

In contrast to the Congressional Leadership's last-minute push to extend expiring tax breaks, the Leadership has shown little interest in extending the federal unemployment benefits. This omission is particularly striking in the House bill, since it includes extension of a corporate tax break enacted as part of the 2002 economic stimulus package, while failing to extend the federal unemployment benefits that were established as part of the same stimulus legislation. In essence, House Leadership has indicated that it believes corporations need continued support as the economy recovers but unemployed workers do not. The facts suggest otherwise.

The labor market is weaker today than when the TEUC program was created in March 2002. As noted earlier, and as the following table indicates, even though there has been some increase in jobs in recent months unemployment indicators — and especially long-term unemployment — are higher today than in March 2002. And employment is lower.

Contrary to the House Majority Leader's claim, many economic indicators, and especially labor market indicators, are worse today than when the temporary federal benefits program of the early 1990s ended. The temporary federal benefits program of the early 1990s began to phase out sharply in February 1994; key indicators of the need for a temporary benefits program remain worse today than they were in early 1994. The earlier program ended after a sustained period of robust job creation; we have now experienced only a few months of modest

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[4] Fawn H. Johnson, "Unemployment Insurance: DeLay Sees 'No Reason' to Extend Federal UI Program Into Next Year," *Bureau of National Affairs* (BNA) *Daily Labor Report*, November 20, 2003.

[5] The one exception is in New York, where workers who exhaust their regular benefits starting on December 22 will not be eligible for TEUC aid.

Table 1

	Latest Data October 2003	Situation when TEUC was enacted March 2002
Unemployment Rate	6.0%	5.7%
Unemployment Level	8.78 million	8.22 million
Long-term Unemployed	2.02 million	1.32 million
Number of Jobs	130.132 million	130.481 million

job creation. In addition, many more unemployed workers are exhausting their regular unemployment benefits before finding work — and thus are in need of assistance from a temporary federal unemployment benefits program — than during the early 1990s.

- Before the earlier program was allowed to phase down in early 1994, the number of jobs in the economy had increased for 22 of the previous 23 months. There were 2.6 million *more* jobs than at the previous employment peak.

  By contrast, October 2003 marked just the third straight month of modest job creation, following six consecutive months of job loss. Moreover, in October 2003, there were still 2.4 million *fewer* jobs than in February 2001, the month that employment peaked before the downturn kicked in.

- The number of people in need of assistance from the TEUC program is much higher than it was than when the temporary federal benefits program of the early 1990s was ended. Over the past three months, despite modest job growth, 1.07 million workers exhausted their regular unemployment benefits. This is *41 percent higher* than the 757,000 workers who exhausted their regular unemployment benefits in the equivalent period before the federal program of the early 1990s ended.[6]

Three additional reasons to extend the program

First, the federal unemployment insurance trust fund contains ample funds to cover an extension of federal unemployment benefits. The federal unemployment insurance trust fund currently contains about $20 billion. These funds were paid into the federal unemployment insurance trust fund precisely for the purpose of providing federal unemployment benefits at times when the job market is weak. The cost of a straight extension of the TEUC program is less

[6] Even after adjusting for the growth in the size of the labor force, there were 25 percent more individuals exhausting their regular unemployment benefits over the past three months than in the equivalent months before the program of the early 1990s ended.

than $1 billion a month, so there is no risk of depleting the trust fund through another TEUC extension.

Second, it is also of note that unemployment benefits provide more stimulus to the economy than corporate tax cuts. An Economy.com study of the effects of various ways to stimulate a weak economy found that for each dollar of cost to the federal Treasury, federal unemployment insurance benefits were the single most effective policy mechanism examined. Unemployment insurance puts money in the hands of people who need it and generally will spend it quickly. Although the Economy.com study did not examine the specific corporate tax break contained in the current House extenders bill, the study found that similar corporate tax cuts were among the *least effective* methods of stimulating the economy.

Specifically, the study concluded that each dollar of new federal expenditures for unemployment compensation generated an increase in real gross domestic product (GDP) of $1.73. The study found, by contrast, that for each dollar used for a range of corporate tax breaks, real GDP would rise less than $0.35.[7] In boosting a weak economy, unemployment compensation was found to have much greater "bang for the buck." Needless to say, unemployment insurance also is much more effective in targeting help on those who most need it.

Finally, federal unemployment benefits truly are temporary. There is little question that they will expire when the economy and the job market recover sufficiently. In every past economic downturn in recent memory, temporary federal unemployment benefits have been provided when the economy was weak and then terminated when the job market recovered adequately. This contrasts sharply with the various expiring tax provisions that Congress now is extending, which are "temporary" in name only and generally are never allowed to end.

[7] "The Need For Federal Government Aid to State Government," Economy.com, February 2003. For a discussion of the report, see Andrew Lee and Joel Friedman, "Reports Finds Most Administration 'Growth' Proposals Would Be Ineffective Economic Stimulus, Center on Budget and Policy Priorities, April 8, 2003.