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The Administration's Proposal to Make the Tax Cut Permanent

> The Center on Budget issued a full report on this subject on April 17, 2002, available at http://www.cbpp.org/2-4-02tax.htm

The President has proposed to make permanent the tax cuts enacted last year, which are scheduled to expire by the end of 2010. The House Leadership intends to push this proposal to a vote the week of April 15. The debate on this issue comes at a time when new Congressional Budget Office projections show a dramatic deterioration in the budget outlook, and only a few months after the President's Social Security Commission issued a report showing it was unable to come up with options to restore long-term Social Security solvency without drawing on large amounts of funding from the rest of the budget.

- Making the tax cut permanent by eliminating the 2010 "sunset" in last year's tax-cut law would reduce projected surpluses (or increase projected deficits) by another $397 billion over the 2003-2012 period, based on CBO estimates, thereby raising the total cost of the tax cut through 2012 to $2 trillion when the increased interest payments on the debt are included.

- The tax cut would cost the Treasury approximately *$4 trillion* in the decade after 2012, the same period when the baby boomers will begin to retire in large numbers and the cost of Social Security, Medicare, and Medicaid long-term care will rise substantially as a result. Yet it is during that same decade that the cost of a permanent tax cut would explode, as all of its revenue-losing provisions would then be fully in effect. (This $4 trillion figure includes the cost of a modest AMT fix.[1] It does *not* include the extra trillions of dollars in interest costs that the tax cut would automatically generate because the national debt would be much higher as a result of the tax cut than it otherwise would be.)

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[1] The proposal in the President's budget to make the tax cut permanent fails to address problems with the individual Alternative Minimum Tax. Two million tax filers are currently subject to the AMT. The Treasury estimates that, partly because of last year's tax law, the number of tax filers subject to the AMT will soar to 39 million — about one of every three tax filers — by 2012. Such a swollen AMT would "take back" much or all of the tax cut for many of the tax filers it would affect. Since it is inconceivable that the President or the Leadership intends this result or will allow the AMT to explode in this manner, the cost of addressing this swelling of the AMT is an "off-book liability" that must be considered part of the tax cut's long-term cost. In projecting costs over the second decade and over 75 years, this analysis includes the cost of extending an AMT relief provision of the tax cut that currently is scheduled to expire at the end of 2004. This provision leaves the increase in the number of tax filers subject to the AMT at the levels that would have been reached under the tax laws in effect prior to enactment of last year's tax cut. This analysis reflects the cost of extending the expiring AMT provision to achieve the same result, i.e., holding the increase in the number of tax filers subject to the AMT to the levels that would have been reached under prior law. This approach produces a conservative cost estimate, since it assumes policymakers still will allow the number of filers subject to the AMT to rise to more than 20 million by 2011.

- Over the next 75 years, the cost of the tax cut if made permanent would be more than twice as great as the entire shortfall projected in the Social Security Trust Fund. This estimate is based on an examination of the most recent report of the Social Security Trustees and of CBO estimates of the cost of the tax cut when it is phased in fully.

  Substantial revenues from outside Social Security are likely to be needed to ensure the solvency of the Trust Fund if deep Social Security benefit cuts are to be avoided. Permanent extension of the tax cut would render such transfers of revenues to Social Security virtually impossible unless severe cuts were made elsewhere in the budget or sizeable tax increases were enacted.

- Many do not appreciate the magnitude of the tax cut when it becomes fully effective in 2010, and therefore do not grasp the magnitude of the proposal to make those costs permanent. When it is fully effective, the tax cut will be

  — four times as large as the budget for the entire Department of Education;

  — more than three times as large as the Department of Veterans Affairs or the Department of Transportation; and

  — twenty-four times the size of the EPA.

  The tax cut is heavily skewed to those with the highest incomes. When it is fully in effect, the tax cut for the *wealthiest one percent* of all taxpayers will be

  — 1½ times the entire Department of Education budget;

  — larger than the budget of the Department of Veterans Affairs or the Department of Transportation; and

  — nearly nine times the size of the EPA budget.

- The Administration's proposal to make the tax cut permanent — and to add new tax cuts on top of it — stands in sharp contrast to President Reagan's response 20 years ago when the fiscal situation deteriorated significantly after a major tax cut was enacted. To limit the damage to the nation's long-term fiscal position, the Reagan Administration worked with Congress, behind the leadership of Senate Finance Committee chairman Bob Dole, to undo or offset a significant share of the tax cut's revenue loss. The Bush Administration and the House Leadership appear to be charting precisely the opposite course.