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“SMALL BUSINESS” TAX PACKAGE IN SENATE MINIMUM WAGE BILL POSES FISCAL RISKS

By Aviva Aron-Dine

On February 1, the Senate passed a minimum wage bill that includes a package of business tax cuts. The cost of these tax cuts is $8.3 billion over the ten years from 2007 to 2016. On February 16, the House of Representatives passed a much smaller package of business tax cuts, the cost of which is $1.5 billion between 2007 and 2016 (and $1.3 billion between 2007 and 2017). House Democratic leaders have explained that, while they would prefer to see Congress pass a “clean” minimum wage bill, they were willing to approve a smaller tax-cut package in order to reach agreement with the Senate.

The costs of both the House and the Senate tax packages are offset, as is required under the Pay As You Go budget rules recently reintroduced in the House. (Under PAYGO, the costs of legislation that reduces revenues or increases entitlement spending must be paid for.) Some may conclude that, because the tax cuts are paid for, they raise no concerns from the perspective of fiscal responsibility. This view is too simplistic, for two reasons.

First, PAYGO rules do not make new tax cuts free. On the contrary, by requiring that tax cuts be paid for, PAYGO should serve to highlight the fact that tax cuts have costs. The offsets used to pay for the House small business tax package, and the offsets used to pay for the Senate’s larger measure, are offsets that will become unavailable for other initiatives or for deficit reduction. Like all policies, therefore, these business tax cuts should be evaluated based on whether they are worth their cost. Especially in the case of the Senate’s larger measure, it is important to ask: are the tax cuts of greater importance to the nation than other possible uses of $8.3 billion?

Proponents of including large tax cuts in the minimum wage bill have justified them as necessary to compensate small businesses for the costs of the minimum wage increase. They have not established, however, that those costs are large or that they necessitate additional business tax relief on top of the significant tax relief already provided in the past several years. Moreover, the tax incentives included in the Senate package are not targeted solely or primarily to small businesses, and

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1 The official cost estimates of the House and Senate tax packages cover different ten-year periods because the House measure was scored several weeks later than the Senate package, after the Joint Tax Committee had shifted its estimating window.

research has cast doubt on the efficacy of some of the tax incentives included in the House and Senate measures. There consequently are concerns about the merit of these tax cuts as compared with other potential uses for the offsets.

Second, the Senate bill includes two new, temporary tax cuts, and these tax cuts pose fiscal risks. The Senate’s new provisions would allow accelerated tax write-offs for new restaurant buildings and for certain improvements to property owned by retail businesses. Both of these tax cuts are slated to expire March 31, 2008; they will be in effect for only one year. The cost of enacting the two provisions for just one year is $1.9 billion.

Because the two provisions are temporary, only the $1.9 billion cost of having them in effect for one year is offset. Supporters of the new measures, however, presumably do not intend to let them expire next March. Rather, they likely hope that the new measures will join the dozens of other tax cuts that Congress initially enacted on a temporary basis but routinely extends each time that they are scheduled to expire. (These provisions are commonly referred to as the “extenders.”)

Unfortunately, expiring tax provisions often are not reevaluated on their merits. Thus, if the new provisions are enacted, there is a serious possibility they also will be routinely renewed.

This creates two possibilities.

One is that Congress continues to abide by the PAYGO rules and offsets the cost of these provisions each time they are extended. In that case, the two measures will ultimately consume far more than $1.9 billion in offsets. Moreover, unlike the new temporary provisions, virtually all of the offsets included in the Senate bill are permanent. Thus, none of the offsets could be extended to pay for the cost of extending the bill’s new temporary tax cuts. Instead, extending those provisions would consume billions of dollars of additional offsets that could have been used for other initiatives or to reduce the deficit. In considering whether the tax cuts are worth enacting, these longer-term costs should be taken into account.

Even more worrisome from the perspective of fiscal responsibility, there is no assurance that the cost of extending the two new tax cuts in the future would, in fact, be offset. Many in Congress have consistently favored extending expiring tax provisions such as the “extenders” without offsetting the costs. In addition, many members of Congress continue to oppose applying the PAYGO rules to tax cuts, and there is no assurance that the PAYGO rules will endure over the years. At some point, Congress may allow the PAYGO rules to lapse, or may choose to waive those rules when extending expiring tax provisions because it proves difficult to secure agreement on revenue-raising measures that would serve as offsets. If that occurs, the addition of the Senate’s two new temporary tax cuts to the list of tax “extenders” would add to deficits.

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4 These offsets just suffice to cover the cost of the Senate bill’s tax cuts. That is, the Senate bill includes $8.3 billion in tax cuts and $8.3 billion in offsets.