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DESPITE THE RHETORIC, BUDGET WOULD MAKE NATION'S FISCAL PROBLEMS WORSE AND FURTHER WIDEN INEQUALITY

By Robert Greenstein

The President says he wants to promote fiscal responsibility and address growing inequality, but his budget fails on both counts. In fact, it would make both problems worse.

In a sign of the President's misguided priorities, his budget puts extremely large tax cuts for the most affluent Americans ahead of the needs of low- and middle-income families as well as future generations. Low- and middle-income Americans would be hit by budget cuts in areas from education to protection of the environment and assistance to the poor. Future generations would foot the bill for the much larger long-term deficits that the President's extravagant tax cuts would produce. The tax cuts in the budget far exceed proposed reductions in domestic programs.

Enlarging Long-Term Deficits

The President argues that his budget is fiscally responsible, trumpeting the claim that it reaches balance in 2012. But the budget would be balanced only on paper, omitting well over $100 billion in costs for that year.

Whether the budget is balanced in 2012 does not hold great significance because the big fiscal challenge is the severe long-term deficits that will emerge in the decades after 2012. Indeed, in the fine print of the budget, the Administration acknowledges that deficits will shoot up not many years after 2012. The President's budget would make these long-term deficits even larger.

Making Income Inequality More Severe

The budget would further widen the yawning gaps between the extremely wealthy and other Americans. It would essentially further enrich the most well-off at other Americans' expense.

- People with incomes of more than $1 million would get tax cuts averaging $162,000 a year (in 2012 dollars) in perpetuity, according to Tax Policy Center estimates.

- Meanwhile, states would face new fiscal incentives to push children in families with incomes as low as just over $35,000 for a family of three off the State Children's Health Insurance Program (in the one-third of the states that now cover such children) and, most likely, into the ranks of the uninsured.[1] Although nearly six million low-income children remain uninsured today, the budget fails to provide sufficient funds for the program simply to maintain current levels of coverage and represents a step backward from the goal of covering all low-income children.

- Low-income elderly people and others in low-income households struggling to pay high winter heating bills would face sharp cuts in the aid they receive through the low-income home energy assistance program.

- According to the Administration's own figures, the number of children in low-income families who receive child care assistance would be cut by 300,000 between 2006 and 2010.

- Funding for the Head Start program would be sliced $100 million below the 2007 level in the House-passed Continuing Resolution, even before adjusting for inflation, a reduction that would follow several years of essentially frozen funding.

Many low- and moderate-income children, families, and elderly individuals would be hit by several cuts at the same time. For example, the 440,000 low-income seniors — one-third of whom are over age 75 — who now receive a modest bag of foodstuffs each month (the bag costs the government about $20) to help keep them from running out of food would lose that aid; the program providing it would be terminated. These poor elderly individuals could face cuts both in food assistance and in help paying their heating bills at the same time.

The Budget and Fiscal Responsibility

The Administration presents its budget as being fiscally responsible. It trumpets the claim that the budget would be balanced in 2012. But the budget would be balanced in 2012 only on paper; the budget achieves that goal by omitting well over $100 billion in costs for that year and making optimistic assumptions about the revenue that will be collected in that year.

- The budget implicitly includes the assumption that the Alternative Minimum Tax will be allowed to explode and will affect more than 40 million households in 2012, something no one believes will happen. The budget includes the cost of AMT relief only through 2007, but omits the cost of AMT relief in the years after that. The Congressional Budget Office says that the cost of continuing this relief is $93 billion in 2012 alone, if the President's tax cuts are extended.

- The budget also rests on the shaky assumption that the deep cuts scheduled under current law in payments made to doctors for services they provide to Medicare patients will actually take effect. No one believes this will happen either. This assumption makes up to $20 billion in additional 2012 costs disappear.

- The budget also omits all costs for the Global War on Terror after 2009, which could run into the tens of billions of dollars in 2012.

[1] The budget is designed to induce states to cease covering children with family incomes above 200% of the poverty line, which will be a little above $35,000 for a family of three in 2008.

- Finally, the budget employs rosy revenue assumptions; it assumes $155 billion more in revenue in 2012 than CBO does for the same policies.

Moreover, whether the budget is balanced in 2012 is not of great significance. The big fiscal challenge policymakers face is not the state of the budget in 2012, but the severe long-term deficits that will emerge in the decades after that. (The President's budget acknowledges that "The budget is on an unsustainable path.") The policies proposed in the President's budget would make the long-term path even less sustainable.)

- Making the tax cuts permanent will add $2.3 trillion in costs over the next ten years (including the added interest payments on the debt) if AMT relief is allowed to end, CBO estimates show. Yet this figure is artificially low, because it rests on the implausible assumption that a greatly swollen AMT will cancel out a substantial share of the Administration's tax cuts.

- If AMT relief is continued so the AMT does *not* cancel out a substantial part of the tax cuts, making the President's tax cuts permanent will cost $3.5 trillion over the next ten years, based on the CBO estimates. (The Administration's budget substantially underestimates the costs of making the tax cuts permanent, primarily by assuming — without explaining it is doing so —that a vastly expanded AMT will cancel out a hefty share of the tax cuts the Administration claims are essential.)

- The long-term cost of the tax cuts, combined with the cost of the President's s defense build-up, would dwarf the long-term savings from the sizable cuts he is proposing in domestic programs. As a result, the budget would enlarge deficits in both the near term and the long term.

The Budget and Inequality

The President noted last week that "income inequality disparities is real. Its been rising for more than 25 years….And the question is whether we respond to the income inequality we see with policies that help lift people up, or tear others down."[2]

The President's comments followed the release in January of a major CBO report that found income inequality rising rapidly. Leaders such as Alan Greenspan, in one of his final Congressional appearances as Federal Reserve Chairman, have warned about growing inequality.[3]

The budget would nevertheless further increase income disparities by providing massive tax cuts for people at the pinnacle of society and weakening child care, food assistance, and other support for those at the bottom and the middle of the income scale.

- The Urban Institute-Brookings Institution Tax Policy Center reports that if the President's tax cuts are made permanent, households in the top 1 percent of the population (currently those with incomes over $400,000) will receive tax cuts averaging $67,000 a year by 2012. In today's dollars, that amount is larger than the entire income of the typical American household.

[2] ABC News transcript of President's remarks on Wall Street, January 31, 2007.

[3] Alan Greenspan before the House Financial Services Committee, July 20, 2005.

The President's Budget Would Not Increase Funding for Domestic Discretionary Programs by 1 Percent

The Administration has suggested that its budget would increase 2008 funding for domestic discretionary programs by 1 percent over 2007 levels (before accounting for inflation). As it turns out, their proposals would constitute a $1 billion cut in domestic discretionary funding.

Moreover, within the overall 2008 funding level, domestic homeland security programs would grow by roughly $3 billion (see Summary Table 4 on page 154 of the President's Budget). Thus, discretionary funding for domestic programs outside homeland security would *fall* by about $4 billion, or about 1 percent. (If inflation is taken into account, the cut in 2008 funding is even larger.)

Our figures differ from the OMB's for two reasons. First, the Center's analysis uses as the 2007 base the funding levels in the full-year appropriations bill for 2007 that the House passed last week and the Senate is about to consider, while OMB uses a more outdated 2007 base (the President's Budget was completed before work on the new appropriations bill was finished). Second, our figure excludes all defense programs, while OMB excludes Pentagon funding but fails to exclude defense funding in the Department of Energy and a few other departments.

- The tax cuts for those with incomes *of over $1 million a year* would average $162,000 a year by 2012, according to the Tax Policy Center.

- At the same time, funding for domestic discretionary programs would be cut a total of $114 billion over five years. (This cut represents the difference between the Administration's proposed funding levels and the funding levels in the full-year Continuing Resolution for 2007 that the House recently passed, as adjusted for inflation.[4]) By 2012, these programs would be cut by $34 billion.

Proposed Reductions in Domestic Discretionary Programs

The budget identifies the specific cuts it is proposing in discretionary programs *only in 2008*. Examples include the following:

- The Commodity Supplemental Food Program, which provides supplemental food packages worth a little less than $20 each month to 440,000 needy elderly people, would be terminated.

- The Low-income Home Energy Assistance Program, which helps several million poor families and elderly and disabled people afford to heat their homes in the winter, would be cut by $420 million, or 19 percent, below the expected 2007 funding level (the level in the House-passed Continuing Resolution), adjusted for inflation, and $379 million below a freeze level. This would be below the funding level for the program in every year since 2000 (after adjusting for inflation), despite the sharp increases in fuel prices in recent years and OMB's own forecast that fuel prices will be higher in 2008 than in 2007.

- Funding for child care for children in low- and moderate-income families would be frozen even as inflation causes the cost of providing child care to rise. A table in the President's budget itself shows that the number of children assisted would be cut by 300,000 over the next few years, from

[4] The baseline used here, based on the House-passed Continuing Resolution and previously enacted 2007 appropriation bills, does not include emergency supplemental funding provided for 2007.

Evidence Fails to Support Administration Claims That its Tax Cuts are Critical for the Economy

The President's new budget claims that his tax cuts should be made permanent for the sake of both the economy and the budget. This claim is belied by the evidence.

The years following the President's tax cuts have seen unexceptional economic growth and unusually *weak* revenue growth. Despite the large tax cuts enacted in 2001 and 2003, government data show that the current economic expansion is weaker than the average post-World War II economic recovery with respect to an array of critical measures, including economic growth, investment, employment, wages and salaries, and net worth. Employment growth has been slower during the current recovery than during any previous expansion since the end of World War II. Moreover, median income for non-elderly households has fallen for five straight years. In fact, the economy's overall performance has been somewhat weaker than in the recovery of the 1990s when taxes were increased.

Revenues, meanwhile, have declined slightly over the current business cycle (i.e., between the peak of the last business cycle in March 2001 and 2006), after adjusting for inflation and population growth. In previous business cycles, revenues (adjusted for inflation and population growth) have risen an average of 10 percent. The poor revenue performance in the current business cycle is a major reason why the nation's budgetary position worsened by a greater amount between 2000 and 2006 than in all but one other six-year period since World War II, going from a surplus of 2.4 percent of GDP in 2000 to a deficit of 1.9 percent of GDP in 2006. (The largest six-year deterioration occurred between 1998 and 2004 and also reflected the impact of the tax cuts, as well as other factors.)

2.3 million in 2006 to 2.0 million in 2010. Between 2000 and 2010, the drop would be 450,000 children (2.45 million were served in 2000, a number that has dropped since then due to the failure of funding to keep pace with inflation).

- Head Start funding would be cut $100 million from the anticipated 2007 level, before adjusting for inflation, which represents a reduction of more than $200 million when inflation is taken into account. Since teachers' salaries and the cost of rent and supplies generally rise with inflation, to cope with the cut, Head Start programs would need either to reduce the number of children they serve or to make changes that could diminish the quality of the program, such as reducing teachers' salaries, or cutting back on the educational, health, and other services the program provides.

- The preventive health services block grant, which helps state and local agencies undertake efforts to prevent or reduce the incidence of various health problems such as obesity and lead poisoning, would be eliminated.

- A number of low-income housing programs would face reductions. Funding for public housing would be set $377 million (or 5.9 percent) below the expected 2007 level (the level in the House-passed full-year Continuing Resolution). Supportive Housing for the Elderly and People with Disabilities would be cut by $269 million, or 28 percent, below the expected 2007 level.

The proposed cuts in domestic discretionary programs in 2009 through 2012 are left unspecified in the budget, but this budget category (i.e., domestic discretionary programs) includes numerous programs that provide basic supports and services to low- and middle-income families, such as elementary and secondary education, job training, environmental protection, veterans' health care, medical research, meals on wheels, child care, low-income home energy assistance, and dozens of others.

Data from back-up tables supplied by the Office of Management and Budget show that the President's overall funding levels for domestic discretionary programs would result in substantial reductions in a range of such public services that would grow steadily deeper over the next five years. The OMB tables provide data on the funding levels the President is proposing in each of 76 budget "subfunctions," or groupings of programs that are similar in nature. The OMB tables show, for example, that in 2012:

- Funding for elementary and secondary education would fall $2.8 billion — or 6.8 percent — below the FY 2007 funding level (approved in the recent Continuing Resolution) adjusted for inflation.

- Funding for pollution control and abatement would be cut by $1.4 billion — 15.7 percent — in 2012 as compared to the FY 2007 level adjusted for inflation.

- Funding for health care research and training — the budget category that includes the National Institutes of Health — would be cut by 8.9 percent, or $3 billion.

It should be noted that the President's budget proposes substantial increases in several international discretionary programs that are important to people in some of the world's poorest countries. These include major increases in programs to combat AIDS/HIV around the world and in the Millennium Challenge Fund.

Proposed Reductions in Mandatory Programs

The budget also proposes net cuts in mandatory programs that total $309 billion over ten years. (This excludes the cost of the President's Social Security private account proposal, as well as the outlay effects of his tax proposals.) Some $270 billion of these savings would come from Medicare and Medicaid.

Some of the proposed changes in mandatory programs, including some of the Medicare savings proposals and the proposed reforms in student financial aid that include an increase in Pell Grants,[5] merit consideration. Others, however, reflect priorities that favor the very well-off over low-income or vulnerable Americans. For example, despite the fact that 5.6 million low-income children are uninsured today, the budget fails to provide sufficient funds to the State Children's Health Insurance Program even to continue insuring the same number of children as the program insures today. In addition, many of the proposed Medicaid cuts would essentially shift costs to states, likely leading many states to cut back Medicaid eligibility or restrict health care services for the low-income beneficiaries whom the program serves. The budget also would cut the Social Services Block Grant, which provides funds to states for basic services to vulnerable low-income children, seniors, and people with disabilities, by $4.4 billion over ten years, or nearly 30 percent in nominal dollars.

[5] While the Pell Grant program is a discretionary program, the Administration is proposing that the *increases* in the program be part of a larger mandatory proposal to overhaul student financial aid programs and the Pell Grant increase is proposed in the budget as an increase in mandatory spending (offset by reductions in other mandatory spending).