CENTER ON BUDGET AND POLICY PRIORITIES

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Federal Revenues Below Expectations, Casting Doubt on Affordability of New Tax Cuts; Revenues at Lowest Point in Decades as Share of GDP

Federal revenues for fiscal year 2003 are now expected to be $50 billion to $80 billion below government projections made just two months ago, according to a Congressional Budget Office report issued May 9. CBO therefore has raised its estimate for the 2003 deficit to over $300 billion. A new analysis from the Center on Budget and Policy Priorities, based on the CBO data, finds that even without any new tax cuts, federal revenues have shrunk in relation to the economy to such an extent that they will equal a smaller share of the economy this year than in any year since at least 1965.

In addition, the Center reported, the tax cuts Congress is now considering will lead taxes to fall this year to their lowest level as a share of the economy since 1959, the next-to-last year of the Eisenhower Administration.

Furthermore, the largest component of federal revenues, federal income tax collections, is on course to equal a smaller share of the economy this year than in any year since 1943, even before any new tax cuts.

"The decline in federal revenues shows the danger of enacting a large new round of tax cuts, as Congress is now considering," said Isaac Shapiro, author of the Center analysis. "In the short term, lower revenues mean a bigger deficit. The longer-term picture is even more worrisome, since the nation's revenue base is shrinking even as the retirement of the baby-boom generation is fast approaching."

Revenues Falling Even Without New Tax Cuts

If revenues fall $50 billion below CBO's March projection, they will equal 17.1 percent of the Gross Domestic Product in 2003, the lowest level since 1965. If revenues fall $80 billion below CBO's March projection, they will equal 16.8 percent of the economy, the lowest level since 1959. (Neither scenario includes the additional revenue loss from new tax cuts Congress is expected to pass this year.) In either case, 2003 will mark the third year in a row that revenues have fallen. Such a three-year revenue decline hasn't happened since 1920-1923.

Although the recent revenue decline partly reflects the economic downturn, other factors clearly are at work as well, since revenues would drop to levels well below those seen in the deeper recessions of the mid-1970s and early 1980s. A particularly critical factor is the tax cuts of 2001 and 2002, which will reduce revenues by $126 billion in 2003, based on CBO estimates. Without these tax cuts, revenues would not be headed to their lowest levels in decades.

Tax Cuts under Consideration Would Reduce Revenues Further

The tax cuts now before Congress would aggravate the situation. Revenues would fall to their lowest level as a share of the economy since 1959 under either the bill passed by the House or the less-costly Senate Finance Committee bill.

"The deterioration of the federal revenue base raises serious questions about the nation's ability to address other national priorities, from education to homeland security," added Shapiro, "as well as its ability to make good on its promises to retired Americans through the Social Security and Medicare programs. Since the federal revenue base is considerably smaller now than it was during more serious recessions, an economic recovery will not solve the problem by itself. Enacting additional ongoing tax cuts now would only make the long-term problem worse, as many mainstream economists and institutions have warned."

The Center report, *New CBO Data Show Deficit Will Be Higher Than Earlier Forecast as Revenues Fall to Their Lowest Levels in Decades, as a Share of GDP*, is available at http://www.cbpp.org/5-12-03bud.htm.

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