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June 27, 2001

How Much of the Surplus Remains After the Tax Cut?

> The full report can be viewed at http://www.centeronbudget.org/6-13-01bud.htm

On June 27, the Center on Budget and Policy Priorities revised a report, *How Much of the Surplus Remains After the Tax Cut?* The report finds that the tax cut recently signed by the President consumes virtually all of the available surplus over the next ten years, leaving no room for additional tax cuts or large defense increases unless the tax cut is scaled back or funds from the Social Security and Medicare Hospital Insurance surpluses are used for current expenses (rather than to pay down debt). The report's findings include:

- Taking into account the new tax-cut law and program initiatives in the budget plan Congress adopted in May, the remaining surplus outside the Social Security and Medicare Hospital Insurance trust funds appears to be about $500 billion between 2002 and 2011. However, this estimate rests upon several highly unrealistic assumptions. For example, the new tax-cut measure fails to extend a number of popular existing tax credits (such as the research and experimentation tax credit) that are scheduled to expire every few years but always are extended on a bipartisan basis. Extending these credits will cost $78 billion over ten years.

- Another unrealistic assumption behind the $500 billion surplus estimate is that appropriations for non-defense programs over the next decade will not exceed the appropriations level assumed for such programs in the Congressional budget plan adopted in May. This level is $45 billion below what is needed simply to keep pace with inflation and much further below what is needed to keep funding levels for these programs from declining in purchasing power on a per-person basis (i.e., to maintain funding levels for these programs, adjusted for inflation and growth in the U.S. population).

  Based on the appropriations levels for non-defense programs over the past 15 years, the minimum amount Congress is likely to provide for these programs is a level that keeps the programs from falling in purchasing power on a per-person basis. Appropriations for non-defense programs have risen faster than this over the past 15 years. If funding for these programs increased (after adjustment for inflation and population growth) in periods of deficits, it is unrealistic to assume it will be cut after adjustment for inflation and population in periods of surpluses, especially since the Administration and Members of Congress from both parties are calling for *increases* in funding for education, health research, and various other non-defense programs.

- When the budget estimates are adjusted to reflect more realistic assumptions, the surplus that remains available over the next ten years shrinks to approximately $154 billion over ten years, as the table on the next page shows. Moreover, the bulk of that surplus occurs in 2011 and is the result of the provision of the tax bill that terminates the tax cuts after 2010.

- *In fact, for the years from 2002-2010, only $14 billion remains to deal with all of the following:* the defense spending increases the Pentagon is expected to seek (which could amount to several hundred billion dollars over this period), relief from natural disasters (which have been averaging $5.6 billion a year according to the Office of Management and Budget), and other needs such as restoring long-term solvency to Social Security and Medicare, efforts to reduce child poverty, and providing funding for a prescription drug benefit beyond the level the Congressional budget plan assumes, which can support only a relatively modest prescription drug benefit that many experts believe the public will ultimately find inadequate.

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The Surplus After Making More Realistic Assumptions
(in billions of dollars)

		2002	9-year total 2002 – 2010	10-year total 2002 – 2011
Available surpluses after the tax bill and Congressional budget plan		31	287	497
Less:	Cost of extending research and experimentation tax credit and other expiring credits	0	-64	-78
	Cost of keeping non-defense appropriation even with inflation and population growth	-2	-168	-208
	Resulting increase in interest costs	0	-41	-57
Remaining available surplus (excluding Social Security and Medicare HI)		29	14	154

Note: May not add due to rounding.

- Furthermore, the new tax law contains several artificial sunsets, such as the expiration of a measure providing relief from the Alternative Minimum Tax after 2004 and the sunset of the entire tax law after 2010. Reversing these sunsets and extending all of the tax cuts would cost more than $200 billion over the next nine years, plus another $166 billion in 2011 alone.

- Congress cannot count on being bailed out of this problem by new projections of much larger surpluses. Given recent data on productivity growth and revenue collections, it is questionable whether the surplus projections will continue to grow.

- Therefore, unless Congress wishes to use funds from the Medicare Hospital Insurance or Social Security surpluses, it must hold the cost of tax cuts to no more than $1.35 trillion over 11 years, which is the amount the Congressional budget plan allotted for tax cuts and the official cost of the new tax law. This means that any *additional* tax cuts, as well as the cost of repealing the various sunsets in the new tax law (including the sunset of the entire law after 2010), need to be offset by scaling back other provisions of the law that have not yet taken effect or through other revenue-raising measures, such as closing unproductive or inefficient tax breaks. This principle — that any additional tax cuts should be paid for through offsetting revenue measures — is essentially the same as that set forth in a recent *New York Times* editorial.

- Even if Congress does hold the tax cuts to the level the budget plan allows, competing pressures for such items as a more adequate prescription drug benefit, large defense increases, and various unmet domestic and international needs likely will force Congress to use part of the Social Security and Medicare surpluses, to raise further revenues (or scale back other elements of the tax cut before they take effect), or to cut popular programs. Moreover, without additional resources, it seems unlikely that measures to restore long-term Social Security or Medicare solvency can be enacted.

The Center's report closes by noting that in 1981, Congress and a new President overreached in passing a tax cut too large for the budget realities of the time. Congress and the Administration revisited that tax cut in two of the next three years and reduced its size about 30 percent. The pattern could be repeated in the years ahead.