How Should the Surplus be Used?

James Horney
Isaac Shapiro
Robert Greenstein

CENTER ON BUDGET AND POLICY PRIORITIES

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Authors

James Horney, Isaac Shapiro, Robert Greenstein

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Center on Budget and Policy Priorities
820 First Street, N.E., Suite 510
Washington, DC 20002
(202) 408-1080

E-mail:center@cbpp.org
Web: www.centeronbudget.org

Table of Contents

I. Introduction and Overview

The debate in Washington over what use to make of the budget surplus has been problematic in two respects. First, as previous Center analyses have explained, much of the debate has been based on unrealistic assumptions about how much of the surplus is available for tax cuts and program expansions. The Congressional Budget Office projects that non-Social Security surpluses will total nearly $2.2 trillion over the next 10 years under current policies if discretionary spending is maintained at its current level, adjusted for inflation. This figure is frequently taken at face value as the amount available for tax and program initiatives. As a Center report issued in July explains, however, the surplus available for initiatives is considerably smaller than that and is in the vicinity of $700 billion over 10 years. (See the text box at the end of this section for an explanation of this estimate.)

The focus of this report is on the second troubling aspect of the current debate over the use of the budget surplus — the fact that policymakers and the public need to engage in a debate and assessment of the full range of national priorities before enacting measures that would consume the surplus, but so far, such a debate has not occurred. Instead, Congress has charged ahead with efforts to advance tax cuts that would use all of the surplus that is realistically available. The tax cuts that the House, the Senate, or both chambers have approved this year would absorb $951 billion over 10 years (including the increased costs for interest payments on the debt the tax cuts would engender). Moreover, the costs of these tax cuts would nearly double in the second decade of this century, even though that is the time when the baby boom generation will begin to retire in large numbers and the costs of programs for the elderly will necessarily rise.

Adding to these concerns, the tax cuts would be inordinately skewed toward higher-income households. An analysis of the tax cuts that the House, the Senate, or both chambers approved before the August recess, prepared for the Center on Budget and Policy Priorities by

Citizens for Tax Justice (using a tax model similar to that which the Treasury Department employs), found that:[1]

- The five percent of taxpayers (i.e., taxpaying units) with the highest incomes would receive half of these tax cuts. The other 95 percent of taxpayers would share the other half of the tax cuts. The six million taxpayers with the highest incomes would receive as much in tax cuts as the other 121 million taxpayers combined.

- The average tax cut for the top five percent of taxpayers would be $6,408, while the average tax cut for the 20 percent of taxpayers in the middle of the income spectrum would be $193.

What Congress has not fully considered are other potential uses of the surplus, including tax reductions that would be more targeted on low- and middle-income families and individuals and policies that would shrink the number of Americans without health insurance, boost selected investments in future economic growth, and seek to moderate poverty and assist those with low and moderate incomes.

The Structure of this Report

The next section of this report provides a discussion of a range of potential uses of the surplus that merit consideration and is drawn from Chapter III of the Center's July analysis, *How Much of the Enlarged Surplus is Available for Tax and Program Initiatives?*

The principal new component of this report is its third chapter where we weigh tax cuts passed by the Congress against alternative tax and program proposals. Although some policymakers and pundits appear to think there are more than enough funds for a wide array of initiatives and that difficult trade-offs can be avoided, this is not the case. Priority-setting is needed. The size of tax and spending initiatives matters; tradeoffs are inevitable. Providing several hundred billion dollars in tax reductions for higher-income individuals means fewer resources will be available for other purposes that may represent national priorities (or for reducing the national debt). Accordingly, the final part of this report compares some of the tax proposals that Congress has advanced to other types of proposals with similar costs — including both program initiatives and tax cuts —and illustrates some of the choices that policymakers and the nation face.

These examples, which are based on the costs of the tax-cut and spending provisions when fully phased in, are intended to demonstrate how resources used for various Congressional

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[1] See Robert Greenstein, James Horney, and Iris Lav, "Tax Cuts That the House or Senate Has Approved Would Consume All of the Realistically Available Surpluses," Center on Budget and Policy Priorities, July 28, 2000.

How Large is the Available Surplus?

The frequently cited Congressional Budget Office figure that the surplus outside of Social Security is projected to total $2.2 trillion over the next 10 years is reduced substantially when four factors are taken into account. First, there is overwhelming bipartisan consensus in Congress and the executive branch that the annual surpluses in the Medicare Hospital Insurance trust fund should be set to the side, along with the Social Security surpluses, and should not be used for tax or program initiatives. This reduces the surplus available for tax and program initiatives by $360 billion.

Second, due to baseline projection rules, the $2.2 trillion surplus projection assumes that an array of highly popular tax credits that are regularly extended for a few years at a time on a bipartisan basis will instead be allowed to expire, that farm price support payments to farmers will be sharply reduced below current levels despite the strong bipartisan support they command, and that the Alternative Minimum Tax will reach into the middle class in coming years and subject millions of middle-class families to substantially greater tax complexity and increased tax bills. It is extremely unlikely that any of these events will occur. When the more realistic assumption is made that current policy will continue in these areas (i.e., that the tax credits will be extended, payments to farmers will be maintained, etc.), the available surplus shrinks by another $230 billion.

Third, the $2.2 trillion surplus projection assumes that spending for non-defense discretionary programs (i.e., non-entitlement programs) will be cut in purchasing power per person over the next 10 years despite budget surpluses, even though spending for these programs increased amidst budget deficits during the 1990s. Simply assuming that expenditures for discretionary programs remain at their current level per person in inflation-adjusted terms — an assumption that budget experts like Robert Reischauer believe *understates* the likely course of discretionary spending — reduces the available surplus by nearly another $400 billion.

Finally, at least $500 billion of the projected surplus is likely to be needed as part of measures to restore long-term solvency to Social Security and Medicare, since few, if any, policymakers in either party will countenance closing the long-term financing gaps in these programs entirely through benefit cuts or payroll tax increases. The result is a surplus of about $700 billion over 10 years that is available for tax cuts and program initiatives.

Some other budget experts have estimated that available surpluses are likely to be even smaller. For instance, assuming that the discretionary spending will keep pace with the economy and that the surpluses in the federal civilian and military retirement trust funds should be off limits just like Social Security and Medicare HI, Alan Auerbach and William Gale conclude that available surpluses under current policies would be only about $350 billion over the next ten years — before subtracting amounts that will be needed to facilitate Social Security and Medicare reform.

Note: For more information, see Jim Horney and Robert Greenstein, *How Much of the Enlarged Surplus is Available for Tax and Program Initiatives?*, Center on Budget and Policy Priorities, July 7, 2000 and James Horney, "How Much of the New CBO Surplus is Available for Tax and Program Initiatives?," Center on Budget and Policy Priorities, July 18, 2000. Also see Alan J. Auerbach and William G. Gale, Perspectives on the Budget Surplus, July 17, 2000 (http://www.brookings.org/views/papers/gale/20000717.htm).

tax cuts could be redirected to meet other national priorities. The Center is not suggesting that all of the alternatives outlined here be enacted this year or at the levels set forth in these comparisons. Rather, the purpose of this exercise is to underscore the necessity of engaging in a national debate on the full range of public priorities and uses of the available surplus.

The third chapter describes how:

- For the cost of repealing the estate tax, funds could be made available for a Medicare prescription drug benefit, while also providing more targeted estate tax relief focused on family-owned businesses and farms. Rather than spending $50 billion a year on repealing estate taxes for the nation's wealthiest individuals, comparable resources could help address a major deficiency in our nation's health care system for the elderly.

- Instead of spending $29 billion on the Congressional marriage penalty bill, which disproportionately benefits higher income taxpayers (many of whom incur no marriage penalty), funds could be spent on more targeted provisions for marriage-penalty relief in addition to several tax proposals focused on low and middle-income families. These proposals could include an expansion of the Earned Income Tax Credit (EITC) and the Dependent Care Tax Credit for lower income working families, as well as a proposal to support retirement savings accounts (RSAs) for low- and middle-income workers.

- Senate-passed legislation spends about $13 billion a year to create a new health insurance tax deduction that would likely do little to reduce the ranks of the uninsured; for a somewhat smaller amount of money, Congress could pass legislation proposed by a bipartisan group of legislators that could substantially expand health care coverage to low- and moderate-income children and their working parents through the State Children's Health Insurance Program (SCHIP) and make several other smaller improvements in health care coverage.

- Rather than devoting $25 billion on House-passed tax cuts affecting pensions and Social Security benefits that strongly favor higher-income households and could result in reduced pension coverage for some lower- and moderate-income workers, a comparable package of tax and program initiatives could be enacted that would provide tax relief to larger numbers of elderly people, increase retirement savings among low- and middle-income families, and reduce elderly poverty.

II. National Needs and Priorities

The emergence of large non-Social Security surpluses is a very recent phenomenon. Neither lawmakers nor the public have yet gone through a process of weighing the most appropriate uses of the surpluses and establishing priorities. Before rushing to enact large tax cuts or other measures that will consume the available surpluses, policymakers should consider a range of uses of the projected surpluses and weigh these uses against each other. In this process they should especially consider whether the highest national priority is to provide tax cuts that go disproportionately to high-income taxpayers who have benefitted the most from the booming economy or to provide assistance to those whose economic well-being has not substantially improved.

In our view, uses that qualify as national priorities and should be given serious consideration include the following, not all of which can be fully funded from the surplus amounts that are realistically available.

Extending Health Insurance to the Uninsured

In 1998, approximately 44 million Americans — 18.4 percent of the non-elderly population (nearly all of the elderly are covered by Medicare) — were uninsured. That is up from about 15 percent who lacked insurance a decade earlier. Roughly 85 percent of those currently uninsured are members of a family with a working adult.

The lack of coverage is particularly acute among poor working parents. Nearly half of working parents with incomes below the poverty line — 48 percent — were uninsured in 1998. More than one-third (34 percent) of working parents below twice the poverty line ($34,100 for a family of four) lacked insurance. In addition, about one of every four low-income children (children in families with incomes below twice the poverty line) is uninsured.

Adapting the Medicare Benefit Package to Changing Conditions

While Medicare has been successful in ensuring that the nation's elderly have access to high quality medical care, the benefits Medicare provides are not keeping pace with developments in medicine and health care financing in recent decades. Many Medicare beneficiaries are finding it increasingly difficult to obtain adequate health care without paying too much out of their own pockets.

The most obvious, and politically salient, shortcoming is the lack of an adequate prescription drug benefit. Modern medicine is increasingly reliant on drug therapies, which provide improved health outcomes and reduce the need for expensive, unpleasant, and potentially dangerous surgical and other invasive procedures. But the Medicare benefit package has not been adapted to changing circumstances, and Medicare beneficiaries have much less generous prescription drug benefits than most employer-based private health insurance plans provide. Because many of the new drugs are expensive, this can impose hardship on many Medicare beneficiaries and is eroding the success of Medicare in keeping the elderly from having to sacrifice adequate food and housing to pay for health care.

In addition, Medicare does not adequately protect the elderly against catastrophic health care costs. Patients with extended hospital stays or very large doctors' bills can end up with crippling expenses if they have not been able to afford Medigap insurance, which can be costly. Medicare also does not provide protection against the cost of long-term care, except for limited stays in skilled nursing facilities.

Providing Funds for Investments in the Future

Part of the projected surpluses could be used to fund investments that can produce long-term economic benefits, such as carefully selected investments in education, training, research, and infrastructure. Carefully targeted public investments in such areas can help to increase the productivity of the American workforce over the long term.

A higher rate of growth in productivity would result in greater overall growth in the U.S. economy. In the decades ahead, achieving a higher rate of productivity growth is particularly important; without strong productivity growth, the very-slow growth of the U.S. work force that is projected for coming decades (due to the aging of the U.S. population and assuming no dramatic change in allowing in young immigrant workers) threatens to hold economic growth to anemic levels. (The economic growth rate is largely the sum of the rate of growth in the labor force and the rate of productivity growth.)

Carefully chosen investments have the potential to help boost productivity over the long term.

- Education and job training (including both pre-school education and improved financial assistance to enable more low-income youth to receive higher education) can help better prepare American workers to develop and use new technologies and new means of production. That can enable workers to be more productive, enabling them to fare better in the global economy.

- Research and development can help keep the U.S. economy competitive and may produce breakthroughs that boost the economy and improve living standards.

- Targeted improvements in the nation's infrastructure can promote productivity and economic growth through more efficient transportation and communications.

Investments in environmental protection and cleanup also can pay long-term dividends, as such efforts can help protect natural resources needed to foster better health and more productive workers and also can provide future generations the opportunity to enjoy America's natural wonders.

Assisting Working Poor Families and Reducing Poverty at Home and Abroad

A significant number of Americans have not shared much in the fruits of prosperity (see box below on income disparities). Although the booming economy has pushed the poverty rate below the levels reached during the recession of the early 1990s, the overall poverty rate remained higher in 1998 (the latest year for which data are available) than in any of the 1970s. Moreover, the poverty rate for children remains higher in the United States than in most other western industrialized nations, with nearly one in every five U.S. children being poor and more than one in every three black and Hispanic children living in poverty.[2] In addition, while the number of children who are poor was lower in 1998 than in earlier years of the 1990s, those children who remained poor were, on average, poorer; the average poor child fell farther below the poverty line in 1998 than in any year since at least 1978 (comparable data are available only back to 1979).[3] Finally, the poverty rate for elderly women living alone in the United States, at 18.5 percent in 1998, is nearly as high as the poverty rate for children.[4]

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[2] See *Low Unemployment, Rising Wages Fuel Poverty Decline*, Center on Budget and Policy Priorities, October 1, 1999.

[3] Kathryn Porter and Wendell Primus, *Changes Since 1995 in the Safety Net's Impact on Child Poverty*, Center on Budget and Policy Priorities, December 1999.

[4] The figures cited here are the official poverty rates. Under an alternative measure of poverty that counts non-cash benefits such as food stamps and housing subsidies, subtracts income and payroll taxes, and adds Earned Income Tax Credit payments, the poverty rate for children was 14.3 percent in 1998, while the poverty rate for elderly women living alone was 15 percent. Among elderly widows, the official poverty rate was 16.8 percent in

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Disparities in Incomes

In recent years, income disparities in the United States have reached their widest point in at least a quarter century and probably since the end of World War II. Data the Congressional Budget Office has compiled, which are based on both IRS data from actual tax returns and Census data and are widely regarded as the best data available on income trends, show that income disparities widened markedly between 1977 and 1995 (the last year for which these data are available). During this period, the average after-tax income of the bottom fifth of the population fell 14 percent, after adjusting for inflation, and the average after-tax income of the middle fifth of households was stagnant. But the average after-tax income of the top fifth of households rose 27 percent, while the average after-tax income of the top one percent soared, climbing 87 percent.

The Internal Revenue service recently issued data on changes in adjusted gross incomes and federal income taxes from 1995 to 1997. These data show that the sharp increase in income disparities continued in these years. From 1995 to 1997, average AGI minus federal income taxes climbed 31 percent, after adjusting for inflation, for the top one percent of tax filers, a remarkable increase for a two-year period. By contrast, this measure of income rose an average of only three percent for the bottom 90 percent of filers. Preliminary IRS data for 1998 show another surge in capital gains income in that year, indicating that disparities widened further in 1998. (These data also show that 72 percent of the capital gains income in 1998 went to tax filers with incomes exceeding $200,000, the top 1.7 percent of filers.)

A projection of income trends for 1999 that the Congressional Budget Office issued several years ago, based on data for 1995, estimated that the top 20 percent of households would receive slightly more than half of the national after-tax income in 1999, with the remaining 80 percent of the population sharing the other half of the income. CBO also projected that the share of national income going to the middle class would be lower in 1999 than at any time since CBO began collecting these data in 1977 and that the top one percent of the population would receive as much after-tax income in 1999 as the bottom 38 percent combined. In other words, the 2.7 million Americans with the largest incomes would receive as much after-tax income as the 100 million Americans with the lowest incomes. The new IRS data for 1996 and 1997 (and the preliminary data for 1998) — which were not available to CBO when it developed its projections for 1999 — indicate that income disparities in 1999 are likely to have been even greater than CBO had projected.

The problems of working poor families merit particular attention. The majority of poor people in the United States live in households in which someone works. The number of full-time year-round workers with incomes below the poverty line *increased* by nearly half a million in 1998.[5]

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[4] (...continued)
1998, and the rate under the alternative poverty measure was 14.2 percent.

[5] The Conference Board, *Does a Rising Tide Lift All Boats? America's Full-time Working Poor Reap Limited*
(continued...)

On the international front, 1.2 billion people in developing countries survive on less than $1 a day and live in conditions of extreme poverty and destitution. Many areas of the world also are marked by a striking shortage of medical care. The United States has 245 medical doctors for every 100,000 people. By contrast, the South Asia region has 44 doctors for every 100,000 people, and Sub-Saharan Africa has 16. Modest, well-designed increases in U.S. economic aid for poor nations could result in significant improvements in living standards for their people.

Initiatives in these areas would be desirable. The Blair government in the United Kingdom recently established a national policy goal of cutting child poverty in half in 10 years. The United States has no goal in this area. Initiatives warranting consideration, which are spelled out here in more detail than the other priorities described in this paper because of the Center's particular focus, include the following:

- *Expanding the earned-income tax credit (EITC) to increase the rewards of work for low-income families.* The EITC helps to reduce taxes, supplement wages, and make work more attractive than welfare. Recent research indicates it has a strong effect in increasing employment among single female parents and that the EITC lifts more children out of poverty than any other program or category of program.[6] The EITC can be strengthened so that it is even more effective in promoting work and reducing poverty.

- *Reforming the unemployment insurance (UI) system.* The UI system provides inadequate protection for low-wage workers. Unemployment insurance reform is needed to prevent welfare reform from leading to considerable hardship in the next recession, when many low-income parents who lose their jobs may not be able to receive either unemployment insurance (due to the problems in the UI system) or public assistance (due to time limits). A blue-ribbon, Congressionally chartered commission on the UI program chaired by Janet Norwood, the respected former Commissioner of the Bureau of Labor Statistics, reported in the mid-1990s that the UI system was failing to perform adequately for many low-wage workers; the commission recommended a series of improvements to address these shortcomings. These improvements have never been acted upon, in substantial part for budgetary reasons. With emerging budget surpluses, these reforms warrant serious consideration. Some of these reforms are included in a new UI reform package that is beginning to attract bipartisan support; the package was

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[5] (...continued)
Gains in the New Economy, June 14, 2000

[6] Robert Greenstein, *Should EITC Benefits Be Enlarged for Families with Three or More Children*, Center on Budget and Policy Priorities, March 21, 2000.

drawn up by a broad-based group of representatives of business, labor, and state government that has met over the past year to fashion the package.[7]

- *Improving child care assistance for low-income working families.* Expansion of Head Start and other child care programs — along with expanding the Dependent Care Tax Credit and making it refundable so it assists low-income working families that have out-of-pocket child care costs, as well as middle- and upper-income families — should be considered.

- *Reforming the child support system so more child support is collected and reaches the children for whom it is intended.* Needed reforms in this area include financial incentives to encourage states to discontinue procedures under which 100 percent of the child support paid by the non-custodial parents of children who receive public assistance is retained by the state and does not reach the children. This practice discourages the payment of child support and deepens child poverty.

- *Providing housing vouchers to more low-income families, particularly working poor families.* Despite a strong economy, the shortage of affordable housing has continued to grow. Census data show that the number of low-income households with "worst case housing needs" — households that spend more than half of their income on housing or live in severely substandard housing — reached a record-high 5.4 million households in 1997. A majority of these "worst-case-housing-needs" households are low-income working households.[8] More housing vouchers (and other forms of housing assistance) could help address these problems. Recent research suggests that vouchers also can be helpful in increasing employment and earnings among low-income parents, in conjunction with well-run welfare reform programs.[9]

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7 Interstate Conference of Employment Security Agencies, *Joint Comprehensive Unemployment Insurance-Employment Service Reform Proposal*, June 27, 2000 (see http://www.icesa.org/articles/template.cfm?results_art_filename=uidoc2.htm)

8 In fact, low-income working households constitute 70 percent of all worst-case-housing-needs households that are not elderly or disabled households. These data are from U. S. Department of Housing and Urban Development, *Rental Housing Assistance — The Worsening Crisis: A Report to Congress on Worse Case Housing Needs*, March 2000. A working household is defined in this study as one that receives more than half of its income from earnings.

9 Center on Budget and Policy Priorities, *Research Evidence Suggests That Housing Subsidies Can Help Long-term Welfare Recipients Find and Retain Jobs*, June 27, 2000, and Barbara Sard and Jeff Lubell, *The Value of Housing Subsidies to Welfare Reform Efforts*, Center on Budget and Policy Priorities, February 2000. See also, Cynthia Miller, *Explaining MFIP's Impacts by Housing Status*, Unpublished Paper, Manpower Demonstration Research Corporation, 1998.

- *Improving food stamp assistance, especially for working poor families with children.* Food stamp participation has declined by more than 10 million people — nearly 40 percent — since 1994, a much larger decline than can be explained by the improvement in the economy and the food stamp eligibility restrictions included in the 1996 welfare law. Census data show that in 1995, there were 88 children receiving food stamps for every 100 children below the poverty line. By 1998, there were 72 children receiving food stamps for every 100 children below the poverty line. There are growing concerns that poor families that leave welfare for work, or never go on welfare in the first place, are missing out on food stamp benefits for which they qualify (and often on Medicaid coverage as well). A recent Urban Institute study found that only 42 percent of families that left welfare but had incomes below the food stamp eligibility limits continued to receive food stamps. In this post-welfare reform era, the food stamp program should serve low-income working families with children more effectively.

- *Improving assistance to the elderly poor.* Although poverty rates for the elderly as a group have declined dramatically over the past 40 years, poverty remains high among elderly widows and other elderly women living alone. One factor contributing to the problems in this area is that key parts of the benefit structure in the Supplemental Security Income program, a program created under President Nixon that is the nation's basic cash assistance program for the elderly and disabled poor, have not been adjusted for inflation in more than a quarter century. As a result, the level of income that many poor elderly and disabled people receive from a combination of SSI and modest Social Security checks has been declining in purchasing power for years. Given emerging budget surpluses, adjustments are warranted to make up, at least in part, for the effects of inflation on the SSI benefit structure so these elderly and disabled individuals can receive benefits that are closer in purchasing power to the benefits President Nixon and Congress established in the early 1970s and so that the poverty of several million elderly and disabled poor people, many of whom are poor women living alone, can be somewhat alleviated. Substantial additional progress could be made in this area through revisions in the Social Security benefit structure, which should be considered in conjunction with Social Security solvency legislation.

- *Boosting saving among low- and moderate-income working families.* Proposals to enable low- and moderate-income families to build assets through savings accounts into which the government provides matching contributions hold promise and are developing bipartisan support. Such initiatives are particularly significant for low- and moderate-income working families that have little or no savings for retirement and cannot participate in employer-sponsored pension plans.

- *Improving assistance for poor legal immigrant children, parents, and elderly and disabled people who remain subject to unduly harsh restrictions on eligibility for various means-tested programs.* Although some of the severe restrictions the welfare law contained in this area were eased by legislation enacted in 1997 and 1998, other harsh restrictions remain in effect. For example, legal immigrant parents who entered the United States before the 1996 welfare law was signed and who are working for poverty wages are barred from receiving food stamps. (Their children may be eligible.) In addition, poor legal immigrant children and pregnant women, as well as individuals who have become disabled after entering the United States, are barred from Medicaid and the Child Health Insurance Program for at least five years if they entered the country after August 22, 1996, the date the welfare law was signed.

- *Boosting U.S. foreign economic aid devoted to helping people in the world's poorest nations.* According to estimates from the World Bank, there are 1.2 billion people in developing countries living on less than $1 a day. Nevertheless, as a percentage of government spending, U.S. economic aid to other nations is on track soon to reach its lowest level in half a century.[10] The U.S. aid level continues to drop even though our nation already spends a much smaller share of its resources on such aid than any other industrialized nation. The United States should strengthen funding of carefully targeted anti-poverty efforts in the world's poor countries, particularly in the areas of health, education, and combating hunger. In addition, we should fully fund U.S. debt relief commitments, including the commitments that President Clinton made in conjunction with the other six leading industrialized nations to fund the Heavily Indebted Poor Country (HIPC) initiative to provide debt relief to the world's poorest nations.

Tax Cuts and Tax Reform

Tax cuts are likely to consume a significant share of the potentially available surpluses. Wisely chosen tax cuts could constitute an appropriate and beneficial use of a portion of the surpluses. But tax cuts should meet several criteria:

- They should be limited in size so they do not consume so much of the surpluses that insufficient funds remain to help ensure the long-term solvency of Medicare and Social Security, modernize the Medicare benefit package, moderate poverty rates and reduce the ranks of the uninsured, and fund investments in education, research, and other initiatives that can produce long-term benefits.

- The benefits of a tax cut package should be distributed equitably. Using the budget surplus to fund tax cuts primarily for high-income individuals, the group that has benefitted the most from the economic boom, would not be appropriate.

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[10] See Isaac Shapiro, *Trends in U.S. Development Aid and the Current Budget Debate,* Center on Budget and Policy Priorities, April 2000.

Any tax-cut package should include provisions that help those who are struggling to make ends meet, such as improvements in the earned income tax credit and the dependent care tax credit, including making the dependent care credit refundable so low- and moderate-income working families are not denied access to the child care subsidies that this credit provides to families at higher income levels.

- Major tax cuts should be considered in connection with tax reform that makes the tax code simpler, fairer, and more supportive of economic growth. Such a plan would generally combine lower tax rates with a broader tax base, rather than carving out still more exceptions to reward certain groups and certain types of endeavors. One interesting reform approach that has recently been proposed would revamp and integrate the EITC, the personal exemption for children, and the child tax credit to reduce substantially both marginal tax rates and marriage penalties among low-, moderate-, and middle-income working families.[11]

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[11] Robert Cherry and Max B. Sawicky, *Giving Tax Credit Where Credit Is Due: A 'Universal Unified Child Credit' that Expands the EITC and Cuts Taxes for Working Families,* Economic Policy Institute, 2000, and David T. Ellwood and Jeffrey B. Liebman, "The Middle Class Parent Penalty: Child Benefits in the U.S. Tax Code," forthcoming.

III. Weighing the Alternatives

As noted in Chapter I, the cost of the tax cuts that the House, the Senate, or both chambers of Congress have passed this year exceeds the amount of the non-Social Security surplus that is realistically available. The total cost of all policy options outlined in Chapter II of this report also exceeds the amount of the available surplus. In tapping the surplus, choices will have to be made.

In this chapter, we examine some of the tax-cut legislation that Congress has approved this year and compare the cost of the tax-cut bills to other potential uses of those funds. We consider what other priorities could be funded for the same cost as some of the tax cuts.

In making these comparisons, we use the costs of the tax-cut proposals when those proposals are phased in fully. This is necessary because a number of the tax-cut proposals would either be phased in slowly or are "backloaded" in some other fashion, with the result that their costs are kept deceptively low in the early years. In all but one instance, the fully phased-in cost of legislation is represented by the cost projections of the Joint Committee on Taxation (Congress' official scorekeeper for tax legislation) for fiscal year 2010, the last year for which such projections are available. Because the revenue effects of legislation repealing the estate tax will not be felt fully until several years after 2010 (see footnote 13 on page 17), CBO's estimate of the anticipated estate tax collections in 2010 is used to represent the fully phased-in cost of that legislation.

These examples are meant to be illustrative of how the resources that Congress is on track to using for various tax cuts might be employed on other alternatives. We should be clear that we are not suggesting that all of the alternatives outlined here should be enacted this year or ultimately should be enacted at the levels set forth in these examples. Doing so would entail incurring costs larger than the available surpluses. Rather, the purpose of these examples is to demonstrate the folly of rushing headlong to enact large tax cuts without first having a debate over the range of uses of the surplus and to suggest that the alternatives presented here be considered as part of such a debate.

The extent to which such options can safely be adopted will become clearer in the years ahead. The surpluses may prove larger than is currently projected, allowing for more initiatives to be enacted. Or the surpluses may be smaller, allowing for a smaller number of initiatives. Policymakers and the public may wish to engage in a debate on priorities that can lead to development of a prioritized agenda of tax and program initiatives, only some of which are pursued right way. In future years, as the amount of the surplus that is available becomes more certain, more elements of the agenda can be advanced if resources permit.

This chapter looks at four sets of tax cuts that Congress has approved and at alternative policies that would cost about the same amount of money as those tax cuts:

- *Repeal of the estate tax versus a Medicare prescription drug benefit and more targeted estate tax relief*. The House and Senate have both voted to eliminate the estate tax, which would ultimately reduce government revenues by $45 billion to $50 billion a year. Only the largest two percent of estates would be affected; all other estates are already exempt from taxation. For the same level of resources, substantial funds could be made available to help pay for a Medicare prescription drug benefit while also providing more-targeted estate tax relief focused on family-owned businesses and farms among others.

- *So-called "marriage penalty"elimination versus better targeted marriage penalty relief and other help for low- and moderate-income working families.* Congress has passed, and the President has vetoed, a "marriage-penalty relief" bill that would cost $29 billion in 2010. The labeling of this legislation as a marriage penalty bill is something of a misnomer, since much of the relief from the bill would go to families that face no marriage penalties under current tax law and receive marriage tax bonuses instead. Moreover, the bill tilts its relief heavily toward more-affluent couples. An alternative tax package could include about $9 billion of marriage-penalty relief in the vetoed bill that is targeted on lower- and middle-class families. That would leave room for $20 billion of additional assistance through the tax system that would be focused on low- and middle-income households, including expansions of the child and dependent care tax credit, the Earned Income Tax credit, and other measures.

- *Health insurance tax deductions versus expanded health insurance coverage for low- and moderate-income working families that are currently uninsured.* The Senate has approved legislation that would use $13.4 billion a year by 2010 to create a tax deduction for the costs of health insurance premiums incurred by taxpayers who purchase basic insurance individually or who purchase long-term care insurance. Such deductions would do little or nothing to reduce the ranks of the uninsured; the vast majority of the uninsured either owe no federal income tax or are in the 15-percent tax bracket. A deduction would reduce the high cost of insurance for such households either not at all or by only 15 percent, which is much too little in most cases to make insurance affordable. For a somewhat smaller amount of resources, Congress could pass legislation proposed by a bipartisan group of legislators and the Administration that could substantially reduce the number of uninsured parents and children by expanding and reforming the State Children's Health Insurance Program. This proposal would enable large numbers of low- and moderate-income working families to secure coverage on a family basis. Several related Administration proposals would accord states new options to reach and insure more low- and moderate-income children.

- *Tax cuts for high-income Social Security beneficiaries and workers with pension programs versus tax cuts for low- and moderate-income Social Security beneficiaries, assistance to low- and moderate-income working families who are struggling to save for retirement, and help for the lowest-income elderly.* Tax cuts moving through Congress that affect pensions and Social Security benefits carry a total cost of more than $25 billion in fiscal year 2010. These tax cuts strongly favor higher-income households and could result in reduced pension coverage for some rank-and-file workers.[12] For the same level of resources, a package of savings incentives, tax cuts, and program initiatives could be provided that would substantially increase retirement savings among low- and middle-income families, reduce elderly poverty significantly, and provide tax cuts to a larger number of elderly people than the Social Security-related tax cuts that Congress is considering. Moreover, those who would receive these tax cuts would be moderate- and middle-income elderly people, rather than the affluent elderly individuals whom the Congressional proposal would favor.

A more detailed discussion of the Congressional tax cuts and alternative policies follows:

1. Elimination of the Estate Tax versus a Targeted Estate Tax Cut and Partial Funding for Prescription Drugs

Congress has passed legislation (H.R. 8) that would repeal the federal estate tax over the next 10 years. The President has vetoed it. When fully in effect, the annual revenue loss from this legislation would be about $45 billion to $50 billion.[13]

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[12] See Peter R. Orszag, Iris Lav, and Robert Greenstein, "Proposed Pension Changes Would Overwhelmingly Benefit Corporate Executives and Owners," Center on Budget and Policy Priorities, July 2000; and Robert Greenstein "Proposal Regarding Taxation of Social Security Would Benefit Higher-Income Beneficiaries While Requiring $14 Trillion in General-Revenue Transfers Over 75 Years," Center on Budget and Policy Priorities, July 17, 2000.

[13] The full effect of H.R. 8 on revenues would not be realized until several years after fiscal year 2010. Estate

(continued...)

Although proponents of repeal argue that the legislation is needed to allow individuals to pass their farms and small business on to their children or other family members, the overwhelming bulk of the benefits of H.R. 8 would go to wealthy Americans who do not own or operate a small family business or farm. Only about two percent of the estates of all people who die — currently about 50,000 estates a year — are subject to any estate tax under current law. To be subject to the tax, an estate must currently exceed $675,000, an amount that is scheduled to rise under current law to $1 million by 2006. Since each member of a married couple is entitled to the basic exemption, by 2006, a couple will be able to exempt an estate worth up to $2 million from any estate taxes. Moreover, the bulk of taxes are paid on very large estates. Half of all estate taxes are paid on estates with assets exceeding $5 million; only one of every 1,000 people who die leaves an estate that large. More than 90 percent of estate taxes are paid on the estates of people whose annual incomes exceeded $190,000 around the time of their death.

Furthermore, few people leave a taxable estate that includes a small family business or farm. Just six of every 10,000 people who die leave a taxable estate in which a family business or farm forms the majority of the estate. In addition, current law already includes sizable special estate tax breaks for family businesses and farms.

Alternative Policies

The problems the estate tax poses for a very small number of small farmers and small business owners could be dealt with at a fraction of the cost of repealing the tax. An alternative to repeal, offered in the House of Representatives by Representative Charles Rangel, would exempt the first $2 million of a family-owned farm or business for an individual and $4 million for a couple, without requiring any estate planning. The Rangel amendment also would increase the basic estate-tax exemption to $1.2 million ($2.4 million for a couple) starting in 2006. In addition, the Rangel amendment would reduce all estate tax rates by one-fifth (the top rate would decline from 55 percent to 44 percent). These changes would cost about $14 billion a year by 2010. The Rangel amendment also contained a change in the estate tax that would offset about $10 billion of the amendment's annual cost by converting to a deduction the current federal estate tax credit for estate taxes paid to states.

If this offset is not included (it would cause states to lose significant revenues), the Rangel amendment would carry a price tag of $14 billion, a very-substantial amount but less than one third of what full repeal would cost. (There is a question whether even as much as $14 billion should be devoted to estate tax reductions; smaller estate tax cuts can be designed that would be sound policy. But it is unclear whether such smaller tax cuts in this area are viable in the current

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[13] (...continued)
taxes usually are not paid until several years after the decedent's death. As a result, some estate taxes would be paid in 2010; these would be taxes due on the estates of individuals who died *before* 2010. The $45 billion-to-$50 billion cost cited here is an estimate of what the cost of estate tax repeal would be in 2010 if the revenue effects of the legislation were fully realized in that year (i.e., if no estate tax was collected).

political climate.) The $30 billion to $35 billion saved could cover the cost of other policy changes that would provide benefits for a far greater number of older Americans, most of whom are less wealthy and have not benefitted from the surging economy and stock market to the same degree as those who would be helped by estate-tax repeal.

For example, there is widespread agreement that Medicare must do more to help cover the cost of prescription drugs for the elderly. Medicare currently funds prescription drug costs only for the minority of beneficiaries enrolled in a Medicare HMO that provides a prescription drug benefit. National expenditures for prescription drugs, which reached $91 billion in 1998, are growing faster than expenditures for other health care items.

The elderly are disproportionately affected by this growth in costs. Not only do they have higher average drug costs than the rest of the population, but almost one-third of Medicare beneficiaries — 31 percent — had *no* drug coverage whatsoever in 1996 (the latest year for which good data are available). Beneficiaries who have low incomes, are 85 and over, or live in rural areas are particularly likely to lack coverage.

A variety of Medicare prescription drug plans are under consideration. The President proposed a plan in his February 2000 budget and expanded it in July. The House has passed a much more limited plan introduced by Representative Bill Thomas. Plans have been introduced in the Senate by Senators John Breaux and Bill Frist and by Senators Bob Graham, Richard Bryan, and Chuck Robb.

According to the Congressional Budget Office, the plan the President proposed would cost about $60 billion in 2010 (taking into account the offsetting effects of premiums that beneficiaries would pay). The plan would make prescription drug coverage available to all Medicare beneficiaries (with premiums covering about half of the basic program costs), cover the full costs of such coverage for low-income beneficiaries, and cover the full costs of all expenditures above $5,000 ($4,000 out-of-pocket) for any individual.

The $30 billion or more saved from passing the modified version described above of the Rangel estate tax amendment rather than H.R. 8 would cover about half of the cost of the President's prescription drug proposal in 2010.

- Instead of providing benefits in 2010 to the heirs of about 60,000 affluent individuals who will die with estates large enough to be subject to federal estate taxes, that $30 billion could help provide prescription drug coverage for nearly 50 million Medicare beneficiaries.

- The benefits would be focused on those who need help the most — elderly people who have low or modest incomes but are not poor enough to qualify for Medicaid and seniors with extremely high prescription drug expenses.

- By removing the potential for elderly people to have their assets consumed by extremely high out-of-pocket expenditures for prescription drugs, a Medicare prescription drug benefit would do far more to protect the estates, not to mention the health, of the average elderly couple than would repeal of the estate tax, which would affect the estates only of a small fraction of elderly people.

If the $30 billion saved from adopting a more-targeted approach to estate tax reductions were not devoted to helping finance a Medicare prescription drug benefit, it could be used to help pay for long-term care for the elderly. There is growing recognition that the government needs to provide some long-term care assistance to help middle-income elderly who do not qualify for Medicaid but are hard-pressed to pay for extended stays in nursing homes out of their own pockets. (Medicaid currently pays for nursing home care only for the very poor. Medicare provides only limited coverage of nursing home stays related to *short-term* medical needs.)

It is estimated that by 2010, out-of-pocket expenses for long-term care could be about $50 billion.[14] While specific plans to alleviate the burden of long-term care for the non-affluent elderly are not as advanced as plans to deal with prescription drug costs for the elderly, $30 billion a year could help reduce the likelihood that an elderly individual will be impoverished by the high costs of long-term care. Here, also, such an approach would do far more to protect the estates of the bulk of elderly individuals than would estate tax repeal.

2. The Congressional "Marriage Penalty" Bill versus Targeted Marriage Penalty Relief and other Middle- and Low-Income Tax Relief

In late July, Congress passed a bill labeled the "Marriage Tax Relief Reconciliation Act of 2000" that President Clinton subsequently vetoed. The "marriage tax relief" provisions of the bill would cost $28.8 billion in 2010.[15] These provisions are not aimed only at married families that are subject to higher taxes because they are married; approximately half of the resulting tax reductions would actually go to families that currently receive marriage *bonuses*. More importantly, the tax reductions are tilted toward couples with higher incomes. Over half of the bill's benefits when it is fully in effect would go to taxpayers with incomes over $100,000, and 79 percent of the benefits would go to taxpayers with incomes exceeding $75,000, the highest-income 22 percent of taxpayers.

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[14] Congressional Budget Office Memorandum, *Projections of Expenditures for Long-Term Care Services for the Elderly*, March 1999. CBO estimates that out-of-pocket costs could be as much as $38.4 billion in 2010, stated in 2000 dollars. That would be about $50 billion in 2010 current dollars.

[15] This figure does not include the cost of a provision of the bill that relates to the alternative minimum tax and affects both married and single taxpayers; that provision is not specifically designed to relieve marriage penalties. Some form of alternative minimum tax (AMT) relief is needed. The estimates of the realistically available non-Social Security surplus mentioned earlier in this paper assume that such relief will be provided.

The skewed effects of the bill reflect its single largest component, a provision that would increase the income level at which the 15 percent tax bracket ends and the 28 percent begins for married couples, many of whom now receive marriage bonuses. In 2010, this provision would cost $19.9 billion, or more than two-thirds the cost of the marriage provisions in the bill. The provision only affects taxpayers in brackets higher than the current 15 percent bracket; these are the top quarter of all taxpayers and the top third of married taxpayers.

Alternative Policies

A possible alternative tax package would drop the provision extending the 15-percent tax bracket. The package would include the two remaining provisions of the vetoed bill. One of these provisions raises the standard deduction for married couples to twice the level for single taxpayers. This provision, at a cost of $7.6 billion in 2010, is particularly well-targeted on married couples in the middle of the income distribution. The second provision would increase the Earned Income Tax Credit for certain low- and moderate-income married couples with children. The potential marriage penalty for such families can be especially large, and public policy should give some priority to encouraging marriage among low-income parents. We propose a somewhat-larger expansion in this area than that in the Congressional bill (to eliminate a greater share of marriage penalties for these families), but the provision's cost would still come in at under $2.5 billion in 2010.[16]

	Vetoed bill	Alternative
	(2010 cost, in billions)	
Expand 15% tax bracket	$20	$ 0
Increase standard deduction for married couples	8	8
Increase where EITC begins to phase out	1	2
Other tax credits for working families with children	0	8
Boost savings among low- and middle-income families	0	10
Total	29	28

The only "marriage-tax relief" provision that would be dropped from the vetoed bill is the one that benefits the top third of married taxpayers exclusively. Since the package would expand the bill's EITC provision, the alternative package would provide, by the standards of the bill, slightly more "marriage-tax relief" than the original bill to the low- and middle-income married couples that comprise the bottom two-thirds of such taxpayers.

[16] The vetoed bill called for an increase of $2,000 in the level at which the EITC begins to phase down for married couples filing a joint return. The Senate version of the bill had proposed a $2,500 increase. We propose a $3,500 increase in the level at which the EITC begins to phase down for such couples. This is the same amount by which Senator Phil Gramm proposed to increase this level in 1998.

Because the alternative package does not include the proposal extending the 15-percent tax bracket (but modestly increases the EITC proposal), $18.7 billion is freed up for other tax proposals. The alternative package would spend a bit less than half of this on two proposals to help low- and middle-income families with children. One is a further expansion in the EITC that has been introduced on a bipartisan basis by Senators Rockefeller, Jeffords, and Breaux. Although the EITC lifts more children out of poverty than any other program, the official poverty rate remains a stunning 29 percent for children in families with more than two children and 23 percent when the EITC and various non-cash benefits are counted. In both cases, this is more than double the poverty rate among children in smaller families. The EITC proposal would expand the EITC for families with three or more children and thereby both reduce poverty and encourage work among such families. It also would simplify the EITC and phase it out at a modestly lower rate to reduce marginal tax rates. The second proposal is the President's proposal for expanding the Dependent Care Tax Credit for low- and middle-income families with child care costs.

The remainder of the alternative package would be used to establish a program to support private retirement savings accounts (RSAs) by low- and middle-income workers. The President's budget includes a proposal that would establish RSAs through the tax system and provide matching contributions to those accounts for taxpayers with taxable incomes up to $80,000 for a couple ($40,000 for a single individual). The large majority of taxpayers have incomes below these levels. The matching contribution would be as high as 100 percent for the lowest-income taxpayers (plus an additional match of up to 100 percent on the first $100 contributed to an account) and would phase out for higher-income taxpayers. The RSA proposal would cost $10 billion in 2010.

The RSA proposal would boost savings and retirement income among those who, by and large, have not been in the position to put much aside for the future. The bottom 80 percent of the population has only 17 percent of the nation's net worth, the bottom 40 percent just five percent.

Altogether, the alternative package would cost about $28 billion, most of which would go to the bottom three-fourths of taxpayers. In contrast, only $8.9 billion of the Congressional bill went to the two provisions — the standard deduction and EITC phase-out expansions — targeted on this group. For the same amount of resources, the alternative package would provide about three times as much aid to the bottom three-fourths of taxpayers as the Congressional bill would.

3. Health Tax Deductions versus FamilyCare and Increased Child Access to Health Insurance

Bankruptcy legislation the Senate approved earlier this year includes two new deductions related to health care costs that would cost $13.4 billion in 2010. The largest new deduction would apply to health insurance premiums paid by individuals who purchase their own insurance or whose employers subsidize less than 50 percent of the cost of the health insurance premium.

- The provision would likely do little to make health insurance affordable for most of the nation's uninsured, 93 percent of whom either owe no federal income taxes or are in the 15 percent bracket and thus would at most receive a subsidy of 15 cents for every dollar spent on health insurance. Such a subsidy is unlikely to enable many of them to purchase health insurance.

- A health insurance deduction is worth more than twice as much to affluent individuals in the 31 percent, 36 percent, and 39.6 percent brackets than to moderate- and middle-income families in the 15 percent bracket. Many of these higher-income taxpayers who would benefit already purchase insurance as individuals.

- Because the deduction would provide a far deeper percentage subsidy for purchasing health insurance to higher-paid business owners and executives than to lower-wage earners, it could encourage some small business owners to drop group coverage (or not to institute it in the first place) and to rely on the deduction for their own coverage. To the extent this occurs, the ranks of the uninsured and underinsured among low- and moderate-wage workers could increase.

The second, smaller provision would allow a new deduction for the premiums paid to purchase long-term care insurance. While there are problems related to access to long-term care that need to be addressed, this deduction is not an appropriate approach. It, too, would subsidize at most 15 percent of these insurance costs for the three-quarters of taxpayers who are in the 15-percent tax bracket or do not owe income tax; this is not sufficient to help moderate- and middle-income taxpayers purchase relatively expensive long-term care insurance. Moreover, the provision would provide a much-larger subsidy to those with higher incomes, although the cost of long-term care presents less of a problem for that group.

Alternative Policies

Proposals such as the FamilyCare plan that was included in legislation recently introduced in both the House and the Senate (and drew support from a majority of Senators in a recent vote[17]) and also is part of the Administration's budget could expand health care coverage substantially for low-income working parents. The FamilyCare legislation would provide additional funds to states under the State Children's Health Insurance Program and allow states to use these funds to extend coverage to the parents of children being insured under Medicaid and SCHIP. Both poor and near-poor families could benefit, with the approach expected to provide

[17] The FamilyCare proposal secured 51 votes, receiving some bipartisan support, when offered in the Senate. For procedural reasons, however, the proposal needed 60 of the possible 100 votes to pass.

insurance ultimately to about five million more people a year, including additional children brought in with their parents. The FamilyCare Act also contains several smaller provisions that would give states new incentives and options for increasing coverage to children, such as permitting states to use schools and certain other entities to help determine Medicaid eligibility. Other steps could be taken to extend coverage to individuals not currently eligible for either Medicaid or state health insurance programs, such as low-income adults who are not elderly, disabled, or raising children.

The cost of the FamilyCare proposal would be a little less than $9 billion in 2010, leaving another $4 billion to $5 billion available from the funds that would otherwise be consumed by the Congressional health tax deductions. A variety of modest health initiatives could use these funds in a constructive manner. For example, in 1998 Congress established a working group to examine how to improve the health insurance coverage of children in single-parent families either through coverage available to one of their parents or government-funded coverage. This working group recently released recommendations that would improve coordination between the child support program and child health insurance programs and carry a modest cost. In another example, legislation has been introduced to give states the option to provide Medicaid and SCHIP coverage to pregnant women and children who are legal immigrants and entered the United States after August 22, 1996, the date the welfare law was signed. Currently, states are prohibited from extending Medicaid or SCHIP coverage to these women and children during their first five years in the United States. The legislation according states the option to cover these women and children would cost about $250 million in 2010.

4. Competing Approaches to Assisting the Elderly

The House of Representatives has passed two bills related to pensions and the tax treatment of Social Security benefits. The tax cuts provided in these two bills, which would cost an estimated $25.5 billion in 2010, would overwhelmingly benefit higher-income taxpayers.

H.R. 4843, passed by the House on July 19, would confer an array of pension tax preferences on highly paid individuals despite the fact that they are the individuals who already have the most generous pensions. Provisions of current law that place upper limits on the tax-favored contributions that may be made to pension plans on behalf of highly paid individuals would be relaxed. So would the limits on the amount of pension payments that high-income individuals may receive when they retire. Citizens for Tax Justice estimates that 77 percent of the tax reductions provided by the bill — $8.7 billion in 2010 — would accrue to the 20 percent of Americans with the highest incomes. This House bill also includes a number of provisions that would create incentives for some employers to *reduce* pension coverage for low- and moderate-income workers, such as provisions that would weaken rules that prevent employers from skewing too great a proportion of pension contributions to executives at the expense of ordinary employees.

H.R. 4865, passed by the House on July 27, would repeal a provision of law enacted in 1993 that requires Social Security benefits paid to higher-income beneficiaries to be treated for tax purposes in essentially the same manner as private pension payments.[18] H.R. 4865 would reduce the amount of Social Security benefits that are subject to the federal income tax for beneficiaries whose income exceeds $34,000 ($44,000 for a couple), at a cost of $16.8 billion in 2010. The tax cuts provided would go only to the one-fifth of Social Security beneficiaries with the highest incomes. Many of those who would benefit from the change have significant wealth. Data from the Survey of Consumer Finances, conducted by the Federal Reserve, shows the group whose taxes would be reduced by this provision has average net worth of more than $1 million. Their median net worth is $420,000.[19] Anyone living on the average Social Security benefit, or anything close to it, would not be affected by this legislation.

Furthermore, the revenues from the current partial taxation of Social Security benefits are deposited in the Medicare Hospital Insurance Trust Fund. To offset this loss of revenues to the trust fund, H.R. 4865 calls for transfers in perpetuity from general revenues to the trust fund. Such transfers would total $13.7 trillion (in current dollars) over the 75-year period used to measure long-term Medicare solvency.[20] These transfers would not extend the solvency of the Medicare Trust Fund a single day.

Alternative Policies

For less than the $25 billion cost of the tax cuts, alternative policies could be pursued that would provide much broader benefits aimed at retirees whose needs are greater than the higher-income taxpayers who would be the principal beneficiaries of H.R. 4843 and H.R. 4865. Possible alternative policies include:

- The President's proposal to support private retirement savings accounts (RSAs) by low- and middle-income workers, which would cost about $10 billion in 2010. (This proposal is also included as part of an alternative package to the "Marriage Penalty" bill.) An RSA proposal would increase savings and retirement income for taxpayers who have the hardest time putting money aside and will have more modest retirement incomes. The House-passed pension legislation, by contrast, would primarily provide benefits for those individuals who already are able to put

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[18] The Senate also voted to repeal this provision on July 13 in an amendment to the estate tax bill, but that and other amendments were subsequently removed from the bill so the Senate and House estate tax bills would be identical.

[19] Analysis of the data from the Survey of Consumer Finances shows that in 1997, the latest year for which these data are available, Social Security beneficiaries subject to the tax provision that the House bill would repeal had an average net worth of $1,066,000. Their median net worth was $420,000. The average financial assets of this group of beneficiaries were $607,000. Their median financial assets were $187,000.

[20] In constant dollars, the transfers would total $2.4 trillion.

away substantial savings and can expect to have much-higher-than-average retirement incomes and would risk causing some employers to provide less in pension contributions for ordinary workers.

- Increase the size of the additional standard deduction in the federal income tax for individuals who are age 65 and over or blind. Doubling the deduction from the current $1,100 ($1,700 for couples) to $2,200 ($3,400 for couples) would cost about $4 billion in 2010. This would benefit more than 15 million elderly taxpayers — a larger number than would benefit from the Social Security taxation provision the House passed — with most of the benefits going to middle-income elderly people who would not get any benefit from the House bill.

- Make benefit adjustments in the Supplemental Security Income program, the federal program created under President Nixon that provides cash assistance to elderly and disabled individuals and couples who remain poor despite Social Security. The goal here would be to recapture the ground lost to inflation in the past quarter century by the lack of inflation adjustments in a key aspect of SSI that is used to determine benefits for low-income retired workers (disproportionately women) who receive modest Social Security checks that leave them well below the poverty line. Addressing this shortcoming in the SSI program also would extend Medicaid coverage to some elderly and disabled people whose incomes are too high to qualify for it today but who live below the poverty line. The total cost would be $6 billion in 2010.

- This would leave about $5 billion in 2010. That could be used to cover the costs of various other program improvements or tax reductions that would provide benefits more focused on elderly individuals with the greatest needs than are the benefits in the tax bills the House or Senate has passed.

Other Policies

Other policies obviously could be considered for inclusion in these packages in place of some of the policies suggested above. Chapter II of this report outlines a number of other policies that warrant consideration in debates over uses of the surpluses.

For example, in the case of policies to assist working families and reduce poverty, various policymakers from both parties have introduced proposals over the past year that would institute some of the policy initiatives that are discussed in Chapter II but are not part of the four alternative packages described above. These proposals include: legislation the House Ways and Means Committee recently approved on a bipartisan basis to strengthen the child support system; bipartisan legislation to reduce hunger by strengthening the food stamp program (the Hunger Relief Act); an unemployment insurance reform proposal recently developed and proposed jointly by representatives of business, labor, and state government; a proposal in the Administration's budget to provide 120,000 new housing vouchers in fiscal year 2001; legislation to remove some of the restrictions the welfare law placed on the ability of poor legal immigrant families and elderly and disabled people to receive certain means-tested benefits; and proposals to expand Head Start, boost funding for child care programs, and restore funding for the Social Services Block Grant to the levels specified in the 1996 welfare law. (The program has been cut below those levels.)

These and other policies examined in this paper merit discussion. Our nation's current fiscal strength presents an unusual opportunity to address national priorities; careful consideration of the full range of national needs and alternative policies to meet these needs will help ensure that the nation takes full advantage of this opportunity.