

PAY FOR TAX CUTS WITH SPENDING CUTS, NOT PINK SLIPS

After months of political squabbling over how to jump start the United States economy, both Democrat and Republican members of the Senate seem in agreement on two things: something must be done to lighten the crushing tax burden on middle-income American families, and action must be taken to reduce the bias in the tax code against savings, investment, and job creation. The Senate this week will debate a tax bill that takes a small step toward alleviating the tax burden on some Americans, but does so by raising taxes on other Americans and without giving a much-needed boost to the sagging economy. The bill would cut taxes on average working families by increasing taxes on those Americans who invest and create jobs. It is a tax break for the middle class that would be paid for with pink slips.

The wiser approach would be to finance a tax cut for struggling families and tax incentives for investment by placing real controls on surging federal spending. At a time when government spending is at an all-time high and rising rapidly, no tax cut plan truly can be declared "fair" or sensible if it resorts to tax increases rather than reining in the rampant growth in federal domestic spending.

Lawmakers this week will have the opportunity to make this choice when the Senate takes up the tax bill sponsored by Senator Lloyd Bentsen, the Texas Democrat. The major elements of Bentsen's bill, which as yet has no bill number, include:

- X A \$300 per child tax credit which is phased out for families earning between \$50,000 and \$70,000;**
- X The restoration and expansion of fully-deductible individual retirement accounts (IRAs);**
- X A temporary 10 percent investment tax allowance, which expires at the end of 1992; and**
- X A "progressive capital gains relief" package, which includes a two-year holding period for assets as a condition of relief and a 50 percent exclusion from taxation for gains from venture capital investments.**

According to Congress's Joint Committee on Taxation, the Bentsen tax package will mean a loss of revenue to the Treasury of an estimated \$57 billion over the next five years. To make up for this revenue loss, so that the overall package can meet Congress's "deficit neutral" budget requirement, the bill raises \$57 billion in new revenues by creating a fourth income tax bracket for single taxpayers with incomes above \$150,000 per year and for families with incomes above \$175,000 per year, by imposing a 10 percent tax surcharge on millionaires, and by other measures aimed at upper-income Americans.

Ignoring Tax and Spending Burden. Lawmakers who cheer the "fairness" of this proposal seem content to keep in place the \$165 billion in higher taxes approved in the 1990 budget agreement, a tax burden that has deepened and lengthened the recession. And they do nothing to deal with the dramatic increase in domestic spending.

These lawmakers ignore the fact that the budget agreement not only meant a tax increase that has sabotaged the economy, but also that it launched the largest domestic spending spree in U.S. history. As a result of the budget agreement, domestic spending in inflation-adjusted terms in fiscal 1993 will be \$169 billion higher than Ronald Reagan's last budget in fiscal 1989. That is a 25 percent rise. This boost in inflation-adjusted domestic spending

is 70 percent greater than the \$99 billion (or 17 percent) total increase that occurred in twelve years under Jimmy Carter and Ronald Reagan.

The Bentsen plan does nothing to bring this spending under control. It does not trim a single dollar of the pork, fraud, and wasteful spending that taxpayers generally associate with Washington's fiscal irresponsibility. Most taxpayers no doubt will be puzzled to hear that in a \$1.5 trillion budget, absorbing one-quarter of the nation's output, there is no wasteful spending that could have been eliminated and the savings returned to taxpayers.

Tightening Belts. Congress easily could save the \$57 billion to finance the tax relief in the Bentsen plan by imposing a three-year freeze on the budgets of domestic discretionary programs and then allowing these programs to grow at only the inflation rate in the fourth and fifth years. No programs would have to be eliminated under that scenario, but program administrators would have to tighten their belts—as most American families now are having to do.

Alternatively, if Congress chose to freeze the budgets of domestic discretionary programs at their current levels for five years, it could save nearly \$80 billion. This is enough savings to finance the tax cuts the economy needs and still lower the deficit by \$20 billion. In the same vein, Congress could save nearly \$65 billion over the next five years just by lowering the projected growth rate of civilian agency overhead costs (excluding the postal service) by 10 percent each year.

Another way lawmakers truly could get serious about eliminating government waste, and raise the \$57 billion for the tax relief in the Bentsen plan, would be to take ten specific measures. They could:

- 1) **Save over \$10 billion in the next five years by canceling the proposed space station.**
- 2) **Save over \$9 billion by eliminating the Department of Agriculture's Conservation Reserve Program, which pays farmers not to plant crops.**
- 3) **Save \$700 million by closing or selling the National Helium Reserve program.**
- 4) **Save over \$10 billion by lowering the subsidies paid to wealthy agribusinesses.**
- 5) **Save \$1.2 billion by eliminating the honey, wool, and mohair subsidy programs.**
- 6) **Save \$5.2 billion by eliminating unnecessary highway "demonstration" projects.**
- 7) **Save \$2 billion by cutting the travel costs of the federal bureaucracy.**
- 8) **Save nearly \$12 billion by holding the increases of federal personnel costs at the inflation rate and increasing the productivity of bureaucrats, a measure suggested by the General Accounting Office.**
- 9) **Save \$5.7 billion by eliminating school lunch and other nutrition subsidies to middle and upper-income families.**
- 10) **Save \$1.2 billion by eliminating the Economic Development Administration, which for many years has been a source of pork barrel funds for members of Congress.**

The Bentsen plan does none of these things. All it does is give a tax cut to one group of Americans while raising taxes on other Americans who are the main source of investment funds for the U.S. economy. It simply raises taxes on Peter to pay Paul. Unfortunately, one result of taxing Peter in a recession is that he is likely to respond by giving Paul a pink slip.

Scott A. Hodge
Grover M. Hermann Fellow in Federal Budgetary Affairs

For further information:

Scott A. Hodge, ed., *A Prosperity Plan for America—Fiscal 1993* (Washington, D.C.: The Heritage Foundation, 1992).