Medicaid and Deficit Reduction

A Message to Congress and the Super Committee: "Don't Just Cut Programs—Raise Revenues"

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As part of the deal to raise the debt ceiling, Congress has appointed a "super committee" of six Democrats and six Republicans to come up with a 10-year plan by Thanksgiving that will reduce the deficit by $1.2-1.5 trillion.[1] If the committee doesn't agree on a plan with at least $1.2 trillion in deficit reduction, automatic cuts will be triggered. The committee is set to begin deliberations in September. Committee members can consider anything in their deficit reduction plan: Besides spending cuts, they can propose the restructuring of existing programs (such as Medicare and Social Security) and changes that would bring in more revenue.

We have two urgent messages for members of that committee: First, Medicaid must not be cut. Second, at least half of their plan's deficit reduction must come from steps to increase revenue. This piece takes a closer look at why increasing revenue has to be a substantial part of the deficit reduction equation.

Why We Can't Reduce the Deficit with Spending Cuts Alone

To reduce the deficit, the government needs to reduce spending, bring in more revenue, or both. There are several reasons why reducing the deficit through spending cuts alone would be bad policy that would hurt individual Americans as well as the larger economy.

- **Focusing on spending cuts alone would undermine essential government programs.**

  The super committee's work represents the second phase of deficit reduction that was part of the debt ceiling deal. The first phase, which has already been approved, calls for nearly $1 trillion in spending cuts over 10 years, starting in 2013. These are significant cuts and will have serious consequences for many of the programs affected.

  Now, the super committee must seek *another* $1.2-$1.5 trillion in deficit reduction. If the super committee's plan consists entirely of spending cuts, we could be facing a walloping $2.5 trillion in cuts to federal programs. Cuts at that level would necessarily hit a wide range of important government programs, severely limiting their ability to be effective. That includes programs that are critical to the nation's economic strength and well-being, such as those that protect public health, fund medical research, keep our food and drug supply safe, and sustain our infrastructure. It would hurt child education, nutrition, and health programs—likely including Medicaid and CHIP—that help secure a brighter future for our children and our country. It would hurt programs that help us keep our fundamental commitment to the poor and the elderly.[2]

- **It would reduce economic growth and eliminate jobs at a time we can't afford it.**

  Cutting government spending while the economy is weak will weaken it further, costing jobs and threatening our recovery. After the stock market crash of 1929, federal budget cuts deepened the depression and threw millions of Americans out of work; since then, policy makers have generally recognized the contribution that federal programs make to stimulating the economy. For example, every federal Medicaid dollar that flows into states not only helps fund health care for state residents, but also stimulates business activity and generates jobs—and not just the obvious jobs of doctors, nurses, hospital workers, and so on.[3] The overall economic impact of this federal funding is actually larger than the amount of the dollars flowing into a state. The money flowing into a state generates economic activity through successive rounds of spending that drive economic growth in what's called an "economic multiplier effect." With cuts in federal Medicaid spending, that multiplier effect would be lost, placing jobs at risk and slowing business activity in every state.[4]

- **The burden of spending cuts would fall disproportionately on low-income and middle-class families.**

  It is lower-income and middle-class families who depend the most on public programs for things like health and long-term care, education, and unemployment insurance to help in tough economic times.[5] A deficit reduction plan that consists only of spending cuts, without asking the wealthiest among us to pay more, is fundamentally unfair. It places the entire burden for deficit reduction on those who have already been hardest hit during this recession.

Increasing revenue must be part of deficit reduction—and there's room to do that

Increasing revenue can include things like getting rid of corporate tax loopholes and deductions and asking the wealthiest among us to pay their share.

- **It could mean reforming our corporate tax code to make it simpler *and* increase revenue.**

  Tax provisions that let corporations avoid or substantially reduce federal income taxes cost the government billions. Corporate interest groups complain that the United States has one of the highest corporate tax rates in the world at 35 percent, but few corporations actually pay that rate.[6] From 2000 to 2005, on average, corporations in the U.S. paid 13.4 percent of their profits in taxes.[7] Corporations use tax write-offs, overseas subsidiaries, and other ways of lowering reported income in order to significantly reduce their taxes. Today, corporate taxes are extremely low by historical

U.S. standards.[8] Additionally, in the United States, both corporate tax rates paid and corporate tax receipts measured as a percent of the economy are quite low compared to other developed countries.[9]

For example, this year, GE made news for not paying any federal taxes in the U.S., despite worldwide profits of $14.2 billion.[10] In fact, over the 2008 to 2010 period, GE didn't just avoid taxes—the company actually received $4.7 billion in tax benefits on $7.7 billion in pretax U.S. profits.[11] But GE isn't alone. Other large corporations also pay very little in taxes, with many getting tax benefits.[12]

Tax provisions that let corporations avoid taxes are inefficient and cost the United States a lot of money. In a 2007 report, the Treasury Department estimated that "corporate tax preferences" will cost the government more than $1.2 trillion in lost revenue over 10 years.[13]

▪ It could mean asking the wealthiest to pay more in taxes

In recent years, there has been a dramatic rise in income inequality in the United States.[14] At the same time, the Bush era tax cuts reduced the top marginal federal income tax rate to 35 percent, which is quite low by historic standards. (That rate only applies to the portion of a person's annual income that exceeds $373,650.) In the 70 years between 1932 and 2002, when the Bush tax cuts were passed, the top marginal tax rate averaged 66.8 percent and was greater than the current 35 percent for all but five of those years. [15] The effective income tax rate—the actual percent of income paid in taxes—of the most affluent has fallen as well. In 2008, the top 400 taxpayers in the United States, with the highest adjusted gross incomes, had an effective tax rate of just 18 percent.[16]

The Bush tax cuts have cost the federal government a considerable amount in lost revenue: almost $2.5 trillion from 2001 to 2010.[17] And it gets worse. If these cuts are not allowed to expire, their revenue-reducing impact is projected to grow larger in the years ahead.[18] A balanced approach to deficit reduction would include asking the wealthiest to pay more, rather than placing the greatest burden on low-income and middle-class Americans by cutting critical programs they rely on.

▪ A balanced approach makes sense

Claims that low corporate taxes lead to more hiring and that low taxes on the most affluent stimulate the economy don't hold up. Lower tax rates don't lead companies to hire new people. Businesses invest in hiring and increasing production when there is demand for their goods and services, not because their taxes are low.[19] High unemployment, low consumer confidence, and cutbacks in household spending are stifling demand, and that keeps businesses from hiring. [20] Similarly, lower taxes for the wealthiest are a poor way to stimulate the economy:[21] With lower taxes, wealthier families tend to save more, not spend more.[22]

Using the broadest measure of tax rates, which is total federal revenues divided by the gross domestic product, taxes are at their lowest level in 60 years.[23] Assertions that there is not room to increase revenue are unfounded.

- **The public wants a balanced approach to deficit reduction**
  A balanced approach to deficit reduction—not one based solely on spending cuts—is also what the public wants. Poll results show that a majority of Americans want an approach to deficit reduction that combines spending cuts with increased revenue from businesses and higher-income Americans.[24]

Why at least 50 percent from revenue is a reasonable target for the super committee

If 50 percent of the super committee's deficit reduction comes from increasing revenue, that would make the ratio of spending cuts to revenue increases for the total deficit reduction package roughly 2:1—the total package being the nearly $1 trillion in cuts already passed and the $1.5 target for the super committee.

There is a precedent for asking that at least 50 percent of the super committee's deficit reduction come from revenue. A 2:1 ratio of cuts to revenue was the ratio proposed by President Obama in his April deficit reduction framework, it mirrors the Bowles-Simpson plan that came out of the President's Fiscal Commission, and it is the ratio contained in the proposal developed by the Senate's bipartisan "Gang of Six" in July.

Conclusion

Long-term deficit reduction is important. How we get there is important, too. How we get there says a lot about the kind of country we are and what kind of economic growth and opportunities we will have in the future. Focusing on cuts alone will short-change our future opportunities, continue to pinch the middle class, and hurt the most vulnerable among us. A balanced approach that brings in significant revenue makes sense, protects critical programs, and is what the public wants. In conversations with decision-makers, let them know that you feel the super committee should take such a balanced approach to deficit reduction.

Endnotes

[1] For a more detailed discussion of the debt ceiling agreement and the super committee, see Families USA, *Medicaid, the Budget, and Deficit Reduction: The Threats Continue* (Washington: Families USA, August 2011), available online at http://familiesusa2.org/assets/pdfs/Threats-to-Medicaid-Continue.pdf.

[2] Medicaid, other means-tested programs, and most of Medicare are exempt from automatic cuts that take effect if the super committee cannot agree to a plan for at least $1.2 trillion in deficit reduction. However, in developing its plan, the super committee can consider cuts to these programs.

[3] Kathleen Stoll and Kim Bailey, *Jobs at Risk: Federal Medicaid Cuts Would Harm State Economies* (Washington: Families USA, June 2011), available online at http://familiesusa2.org/assets/pdfs/Medicaid-Cuts-Hurt-State-Economies.pdf. The report includes state-specific data on jobs at risk at different levels of federal Medicaid spending cuts.

[4] Ibid.

[5] Donald Hernandez, *Declining Fortunes of Children in Middle-Class Families: Economic Inequality and Child Well-Being in the 21st Century* (New York: Foundation for Child Development, January 2011), available online at http://fcd-us.org/sites/default/files/2011%20Declining%20Fortunes_0.pdf.

[6] Christopher Helman, "What the Top U.S. Corporations Pay in Taxes," Forbes.com, April 1, 2010, available online at http://www.forbes.com/2010/04/01/ge-exxon-walmart-business-washington-corporate-taxes.html.

[7] U.S. Department of the Treasury, *Treasury Conference on Business Taxation and Global Competitiveness Background Paper, July 23, 2007*, available online at http://www.treasury.gov/press-center/press-releases/Documents/07230%20r.pdf. The report includes several measures to estimate the actual corporate tax burden in OECD countries. The United States was lower than average on all measures. The calculation is based on the share of corporate operating surplus the U.S. corporations pay in taxes.

[8] Jane G. Gravelle and Thomas L. Hungerford, "Corporate Tax Reform: Issues for Congress," *Congressional Research Service, Report* RL34229, updated July 24, 2008.

[9] Congressional Budget Office, *Corporate Income Tax Rates: International Comparisons* (Washington: Congressional Budget Office, 2005); U.S. Department of the Treasury, op. cit.

[10] David Kocieniewski , "G.E.'s Strategies Let It Avoid Taxes Altogether," *The New York Times*, Mar 24, 2011, p. 1.

[11] Citizens for Tax Justice, *Analysis: 12 Corporations Pay Effective Tax Rate of Negative 1.5% on $171 Billion in Profits; Reap $62.4 Billion in Tax Subsidies; Exxon Mobil, Boeing, Verizon, Others Illustrate Why Revenue-Raising Reform Is Needed*, June 1, 2011, available online at http://www.ctj.org/pdf/12corps060111.pdf.

[12] Ibid.; Chris Isidore, "Companies that pay a lower tax rate than you," *CNNMoney*, February 9, 2011, available online at http://money.cnn.com/2011/02/09/news/economy/corporate_tax_reform/index.htm.

[13] U.S. Department of the Treasury, op. cit.; Chuck Marr and Brian Highsmith, *Six Tests for Corporate Tax Reform: Reform Should Help Shrink Long-Term Deficits, Reduce Biases and Preferences in the Tax Code, and Discourage Tax Sheltering* (Washington: Center on Budget and Policy Priorities, February 2011), available online at http://www.cbpp.org/files/2-28-11tax.pdf. Lost revenue estimates are for 2008-2017.

[14] Emmanuel Saez, "Striking It Richer: The Evolution of Top Incomes in the United States (Updated with 2008 estimates)," July 17, 2010, available online at http://elsa.berkeley.edu/~saez/saez-UStopincomes-2008.pdf. This is an updated version of Dr. Saez's paper, "Striking It Richer: The Evolution of Top Incomes in the United States," *Pathways Magazine*, Stanford Center for the Study of Poverty and Inequality (Winter 2008): 6-7.

[15] The Tax Policy Center, Urban Institute and Brookings Institution, *Historical Top Tax Rate*, available online at http://www.taxpolicycenter.org/taxfacts/displayafact.cfm?Docid=213. Calculation of average top marginal tax rate by Families USA. The income at which that rate applies has changed over the years.

[16] Roberton Williams, "The Very Rich Really Are Different," *TaxVox*, the blog for the Tax Policy Center, May 12, 2011, available online at http://taxvox.taxpolicycenter.org/2011/05/12/the-very-rich-really-are-different/.

[17] Citizens for Tax Justice, *The Bush Tax Cuts Cost Two and a Half Times as Much as the House Democrats' Health Care Proposal*, September 8, 2009, available online at http://www.ctj.org/pdf/bushtaxcutsvshealthcare.pdf.

[18] Kathy Ruffing and James Horney, *Economic Downturn and Bush Policies Continue to Drive Large Projected Deficits*, (Washington: Center on Budget and Policy Priorities, May 10, 2011), available online at http://www.cbpp.org/files/5-10-11bud.pdf.

[19] Statement of Douglas Elmendorf, Director, Congressional Budget Office, *CBO Testimony: Policies for Increasing Economic Growth and Employment in the Short Term*, prepared for the Joint Economic Committee, U.S. Congress, February 23, 2010; and, Laura Tyson, "No Evidence of 'Trickle Down' Jobs," *The New York Times*, January 11, 2011, available online at http://www.nytimes.com/roomfordebate/2010/09/27/tax-cuts-the-trickle-down-argument/no-evidence-of-trickle-down-job-creation.

[20] Congressional Budget Office, *Policies for Increasing Economic Growth and Employment in 2010 and 2011*, January 2010, available online at http://www.cbo.gov/ftpdocs/108xx/doc10803/01-14-Employment.pdf.

[21] Chuck Marr, *Letting High-Income Tax Cuts Expire is Proper Response to Nation's Short- and Long-Term Challenges* (Washington: Center on Budget and Policy Priorities, July 26, 2010), available online at http://www.cbpp.org/cms/index.cfm?fa=view&id=3241.

[22] Ibid.

[23] Bruce Bartlett, "Are Taxes in the U.S. High or Low?" Economix blog of *The New York Times*, May 31, 2011, available online at http://economix.blogs.nytimes.com/2011/05/31/are-taxes-in-the-u-s-high-or-low/.

[24] CNN/ORC poll released August 10, 2011, results accessed online August 25, 2011 at http://i2.cdn.turner.com/cnn/2011/images/08/09/poll.aug10.pdf.

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