



# Misplaced Priorities: Cutting Services to Finance Tax Breaks

November 29, 2005

## Overview

A budget document reflects priorities, and whether it is your family budget or the federal budget, you get what you pay for. Being a sound fiscal steward means making wise choices: setting a financial course that invests in a better future for our children, anticipating potential risks like long-term illness or job loss, and taking care of critical needs as they arise to reduce harms and keep costs low. That is good leadership, whether in our homes or in our nation's capitol.

Many Americans today are struggling to find affordable health care, pay for college, support their families, and put food on the table. Unfortunately, Congress is using the budget process to play games with America's finances. It is rolling back vital services that protect the middle class, and dismantling the social safety net that has protected all Americans for generations. The budget reconciliation package currently under consideration in Congress contains billions in cuts to health care for low-income families, student loans, child support enforcement, food stamps, and many other areas.

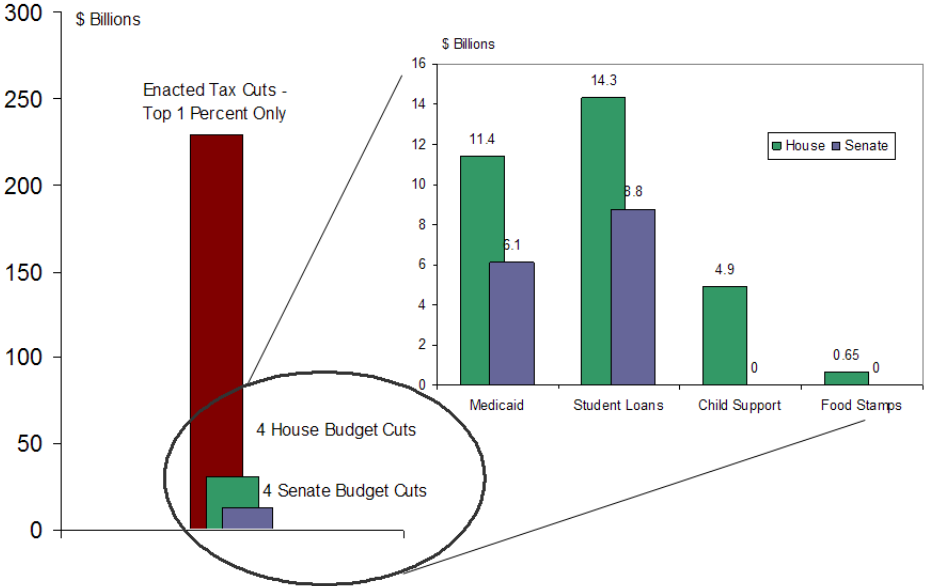
Why? In order to offer permanent tax cuts for those least in need. Reversing just one-seventh of the tax cuts for the top 1 percent of taxpayers—those making more than \$300,000 a year—would be enough to avoid these costly cuts cited below.

Yes, a budget document reflects priorities—sadly, Congress is not looking out for mainstream families. It is time for a budget that reflects America’s real priorities. We must do better.

The Congressional budgets, among other cuts, include:

- Medicaid - new costs for more than 7 million poor and near-poor Americans, including 3.5 million children; an estimated 70,000 would lose coverage completely; low-income Americans just above the poverty line will be subject to substantial co-pays and charges;
- Student Loans - \$8 billion in new charges to students and their families: an average student borrower with \$17,500 in loans would pay an estimated \$5,800 in additional interest payments;
- Child Support - cuts would lead to \$24 billion in uncollected child support payments over the next decade; other changes would create large unfunded mandates for child care, leaving states with billions less to pay for education and health care;
- Food Stamps - an estimated 225,000 people would lose food stamps, most of them in working families.

Figure 1: Already Enacted Tax Cuts for Top 1 Percent: 7 Times Larger Than Budget Cuts Targeting Working Poor and Students (5-year costs, 2001-2004 tax changes)





## Misplaced Priorities: Cutting Services to Finance Tax Breaks

By John S. Irons and Bracken Hendricks<sup>1</sup>

A budget document reflects your priorities, and whether it is your family budget or the federal budget, you get what you pay for. Being a sound fiscal steward means making wise choices: setting a financial course that invests in a better future for our children, anticipating potential risks like long-term illness or job loss, and taking care of critical needs as they arise to reduce harms and keep costs low. That is good leadership, whether in our homes or in our nation's capital.

Many Americans today are struggling to find affordable health care, pay for college, support their families, and put food on the table. Unfortunately, Congress is using the budget process to play games with America's finances. It is advancing a radical ideological agenda of privatization, rolling back vital services that protect the middle class, and dismantling the social safety net that has protected all Americans for generations. The budget reconciliation package currently under consideration in Congress contains billions in cuts to health care for low-income families, student loans, child support enforcement, and food stamps. The budget includes cuts to many other areas as well.

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Why? In order to offer permanent tax cuts for those least in need. Reversing just one-seventh of the tax cuts for the top 1 percent of taxpayers—those making more than \$300,000 a year—would be enough to avoid the costly cuts cited below.

At a moment in our nation's history when thousands of workers are losing their jobs, healthcare costs are skyrocketing and retirement security is disappearing as pensions vanish, and even as new threats emerge in food safety, the global environment, and international terror, conservatives are slashing the very services that can keep our country strong through times of economic trouble.

Conservatives in Congress may try to frame these cutbacks as a response to the costs of Hurricane Katrina or fighting an intractable war, but follow the numbers and it is clear who pays and who benefits. They are choosing permanent tax cuts that benefit millionaires at the expense of good government and vital services that make our country stronger, safer, and more prosperous. Yes, a budget document reflects priorities—sadly, Congress is not looking out for mainstream families. It is time for a budget that reflects America's real priorities. We must do better.

## **Follow the Numbers: Who Pays?**

### **Medicaid**

The Medicaid program provides health insurance to low-income families, people with disabilities and individuals who need long-term care. The House budget cuts federal funding for this program by \$11.4 billion over the next five years,

and will affect millions of Medicaid enrollees.<sup>2</sup> These cuts will enable states to require people with Medicaid coverage to pay more for their health care through increased premiums and co-payments, and to reduce the Medicaid benefit package, therefore requiring families to pay for more services on their own.

The Congressional Budget Office (CBO) estimates that the cost sharing provisions will push new financial burdens onto more than 7 million people—half of them children—by 2010, while the new premium requirements will leave 70,000 current enrollees without coverage by 2010. In addition, 2.5 million enrollees—again, half of them children—will receive skinnier benefit packages.<sup>3</sup> The combination of these provisions will mean that people who have coverage today will end up delaying treatment and foregoing preventive care - resulting in increased costs on the rest of society.<sup>4</sup>

## **Student Loans**

Both the House and Senate's budgets reduce funding for Student Loans, hitting middle-class families with \$8 billion in new costs as they send their kids to school. The House version cuts \$14.3 billion over five years from higher education programs, most of which is achieved by reducing payments to lenders and implementing other changes to student loans, while the Senate version increases

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<sup>2</sup>CBO cost estimate, "Reconciliation Recommendations of the House Committee on Energy and Commerce," available at <http://www.cbo.gov/ftpdocs/68xx/doc6829/ECrecon.pdf>. Estimates of the cuts do not include Katrina-related provisions.

<sup>3</sup>CBO cost estimate, "Additional Information on CBO's Estimate for the Medicaid Provisions in H.R. 4241, the Deficit Reduction Act of 2005," available at <http://www.cbo.gov/ftpdocs/68xx/doc6849/BartonLtr1.pdf>

<sup>4</sup>Ibid.

the interest rates that borrowers must pay.<sup>5</sup> Both versions would mean significant additional costs for borrowers—the CBO estimated that these cuts would cause \$8 billion in new charges to students and their families.

According to estimates from the State Public Interest Research Groups' Higher Education Project, an average student borrower with \$17,500 in loans could pay an estimated \$5,800 in interest payments.<sup>6</sup>

### **Child Support Enforcement and Child Care**

The House's budget plan cuts \$4.9 billion over five years from child support enforcement—a cost born by single parents and their kids through lower—generally uncollected—child support payments. CBO estimates that these cuts would result in families receiving \$7.9 billion less in child support payments over the next five years, and \$24 billion over the next 10 years.

Another change in the House's budget would oblige states to require more low-income Americans receiving cash assistance to participate in work programs, and hence would require states to provide child care subsidies for these new workers. The budget, however, does not provide the funding necessary to states to provide the additional child-care costs. To provide this assistance, therefore, states would have to displace others currently receiving help with child care costs—specifically low-income working families who do not receive TANF cash assistance. The Center on Budget and Policy Priorities estimates that in the

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<sup>5</sup>CBO cost estimate, "Reconciliation Recommendations of the House Committee on Education and the Workforce," available at <http://www.cbo.gov/ftpdocs/68xx/doc6827/EdWrecon.pdf>.

<sup>6</sup>See State PIRGs "Stop the Raid on Student Aid," available at <http://www.studentaidaction.com/aid.asp?id=1157>.

end 330,000 children in low-income working families would lose their help with child care costs.

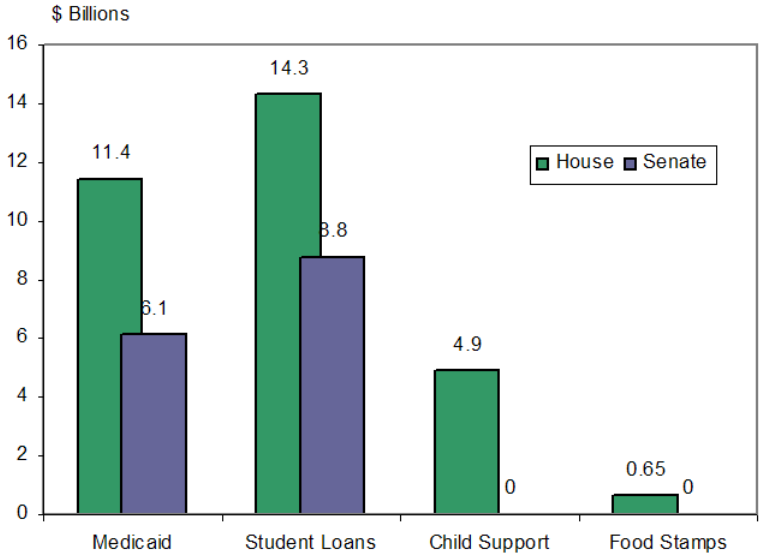
## **Food Stamps**

The food stamp program provides vouchers to low-income Americans to purchase much needed food, and is a core safety net program that provides aid in time of most need to millions. The House's budget cuts over \$647 million over five years from the food stamp program, hurting the poor and hungry. These cuts would mean approximately 225,000 people would lose food stamps, according to estimates from the CBO.<sup>7</sup>

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<sup>7</sup>See CBO cost estimates at <http://www.cbo.gov/ftpdocs/68xx/doc6885/HousePassedRecon.pdf> for final net reductions. For number of people impacted, see CBO cost estimate, "Agriculture Reconciliation Act of 2005," available at <http://www.cbo.gov/ftpdocs/68xx/doc6830/HseAgRecon.pdf>. The final version of the bill contained slight changes to the policy analyzed by the CBO; however, the changes are unlikely to have a sizeable impact on the number of people affected.

Figure 2: Cuts to Selected Federal Programs, 2006 Budget Reconciliation Bills  
(5-year costs)



## Who Benefits? - Tax Changes

The Bush tax changes of the last several years have cost hundreds of billions and the benefits have overwhelmingly gone to upper-income individuals. Permanently extending these provisions would cost at least \$1.5 trillion over the next 10 years and \$188 billion over the next five—clearly swamping the \$35-50 billion five-year spending cuts.<sup>8</sup>

### Already Enacted Cuts

Tax changes from the last four years have cost over \$200 billion per year, and a large share—23 percent—benefits the top 1 percent of taxpayers. Over five years, just the share of cuts going to the top 1 percent is approximately \$230 billion. Reversing just one-fifth of the tax cuts for the top 1 percent would be enough to avoid these costly budget cuts.<sup>9</sup>

### Upper-Income Tax Breaks

There are two tax changes that benefit high-income individuals that are scheduled to begin to take effect in 2006. The repeal of the phase-out of the personal exemptions and the limitation on itemized deductions that benefit only upper income individuals (PEP/Pease) have not yet taken effect, yet will cost \$27.9

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<sup>8</sup>Most of the costs of extending the Bush tax changes come after the five-year window since most provisions expire in 2010. Congressional Budget Office, “Budget Options,” February 2005. Extending a temporary fix to the AMT and adding interest costs would bring the 10-year cost to about \$3 trillion including interest costs (see W. Gale and P. Orszag, “Key Points on Making the Bush Tax Cuts Permanent,” Brookings, January 21, 2004, available at <http://www.brookings.edu/views/op-ed/gale/20040121taxcuts.htm>.)

<sup>9</sup>Five-year costs and distribution is derived from single year estimates from the Tax Policy Center, Table T05-0062.

billion over the next five years.<sup>10</sup>

Ninety-seven percent of these benefits will go to those making over \$200,000 a year, and over half will go to those making more than \$1 million.<sup>11</sup>

Total or partial reversal of the marginal rates reductions would also raise significant revenue. Raising the rates on the top two tax brackets by 1 percent would bring in an estimated \$17.3 billion over five years. And returning all rates and brackets to 2002 levels would raise \$155 billion over five years.<sup>12</sup>

## **Capital Gains and Dividends**

Extending capital gains and dividends tax cuts would cost an estimated \$20.5 billion over five years. About 45 percent of these benefits would go to those making more than \$1 million, and 72 percent would go those making more than \$200,000.<sup>13</sup> Recent changes have further shifted the burden of the tax code from income from wealth onto income from work.

## **2006 Reconciliation Tax Changes**

The House and Senate are also pursuing tax changes as well as the budget cuts. The Senate has already passed a tax bill that costs \$60 billion over five years, while the House is looking at a \$56 billion measure.

Under the Senate's measure, those making more than \$1 million a year would receive on average a \$10,000 break, while those in the middle would see a \$47

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<sup>10</sup>Tax Policy Center, Table T04-0173.

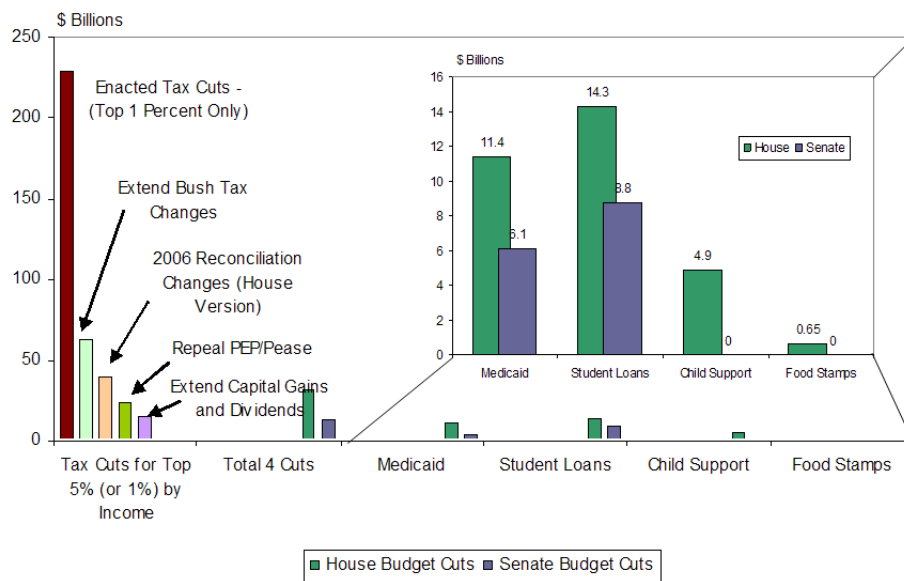
<sup>11</sup>Tax Policy Center, Table T05-0023.

<sup>12</sup>Congressional Budget Office, "Budget Options," February 2005.

<sup>13</sup>Tax Policy Center, Tables T05-0291,2.

cut. Under the House's measure, those making more than \$1 million a year would receive on average a \$50,000 break, while those in the middle would see a \$55 cut.<sup>14</sup>

Figure 3: Tax Costs for Top 1 and 5 Percent of Income, and Selected Cuts to Federal Programs, 2006 Budget Reconciliation Bills (5-year costs)



<sup>14</sup>Tax Policy Center, Tables T05-0293 through T-05-0296.