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Administration's New Stimulus offer Largely Cosmetic Changes

> The full report can be viewed at http://www.cbpp.org/12-13-01tax.htm

On December 13, the Center on Budget and Policy Priorities released an analysis of the $100 million stimulus package Treasury Secretary O'Neill presented on December 11. This offer by the Administration, which follows discussions with members of the Senate's Centrist Coalition, reflects largely cosmetic changes from previous offers. It relies on large multi-year tax cuts for business and higher-income taxpayers, while providing relatively modest benefits for the unemployed. In addition, the plan continues to omit one of the most effective and badly needed types of stimulus measures — fiscal relief to states to ease the need for states to cut programs or raise taxes to cope with the growing deficits created by the economic downturn. The report's findings include:

- The National Governors Association estimates that state budget deficits in this fiscal year could rise to $50 billion, a significantly greater shortfall than states encountered in the worst year of the recession in the early 1990s. The Administration plan not only rejects fiscal relief for the states, but the Congressional Research Service estimates that the plan would cause states to lose an additional $5.4 billion of tax revenue in 2002. This would force even larger state budget cuts or tax increases in the months ahead, which would counteract a substantial share of the stimulus efforts taken at the federal level.

- The largest component of the Administration's package is accelerating implementation of one of the income tax rate reductions enacted in June — the reduction in the 27 percent tax rate to 25 percent. This would cost $54 billion over ten years. According to the Congressional Budget Office, only the top one-quarter of taxpayers would benefit from this proposal.

  This tilt toward upper-income taxpayers diminishes the proposal's effectiveness as short-term economic stimulus. Research has shown that those with higher incomes are more likely to save (and not spend) an additional dollar in income than low- and moderate-income families. In addition, Joint Committee on Taxation estimates show that more than three-quarters of the cost of accelerating this rate cut would be incurred after fiscal year 2002 — that is, when the economy is expected already to be in recovery.

- Amidst mounting evidence of the severity of the unemployment caused by the recession, the Administration now accepts the need for additional weeks of unemployment insurance benefits in all states. But this proposal continues to exclude several significant provisions in the Senate Finance Committee bill that would make more laid-off workers (especially low-income workers) eligible for benefits and provide for a modest increase in unemployment benefit levels.

- The Administration proposes to give a tax credit to unemployed workers to help them pay for health insurance premiums. Many unemployed workers with low or modest incomes, however, would be unable to afford insurance even with the credit. Many others would be ineligible for the credit since under the Administration's proposal, only unemployed workers eligible for unemployment insurance may receive the credit and, as just noted, the proposal excludes two key Finance Committee provisions to broaden unemployment insurance coverage.

  Furthermore, the credit is designed for unemployed workers not eligible for COBRA coverage to use the credit to purchase insurance in the individual health insurance market. That market is unregulated and lacks the advantages of group insurance purchased through employers or provided through public programs such as Medicaid. For instance, many plans sold on the individual market impose high deductibles and offer only limited benefits. Furthermore, premiums in the individual market can vary based on risk factors such as age and medical history, and people can be denied coverage altogether. Older and sicker workers generally cannot obtain health insurance in the individual market or can obtain it only at prohibitive cost.

  The Administration would also increase funding for the National Emergency Grants program. This program is designed to address the need for job training and related services in individual localities where events that have caused significant job losses have occurred. The program is not designed to respond to problems created in most or all states as a result of a national recession or to provide health insurance for unemployed workers who lack it.

  Of particular concern, the program has no experience in purchasing health insurance or providing health care coverage. States would likely need a number of months to develop eligibility rules and procedures for what would effectively be a new health insurance program, to determine the nature and scope of the insurance coverage to be offered, to contract with health insurers and plans, and to train and hire new staff. By the time health insurance coverage could be provided to workers through NEGs, the recession could be over. Meanwhile, the program that can provide coverage expeditiously — Medicaid — would likely be subject to larger cutbacks at the state level than would otherwise be the case as a result of tax provisions of the Administration's package that would cause state revenue losses and make state budget shortfalls larger.

- The Administration plan retains most of the multi-year business tax cuts in the House-passed stimulus package. It makes no specific proposal regarding the corporate AMT, stating that this matter is "to be determined later." One of the proposals the Administration reportedly is considering as an alternative to repeal is the permanent elimination of key components of the minimum tax. If these components of the minimum tax are jettisoned, the continuation of the corporate AMT will be largely symbolic, as the tax will largely be gutted.

The Center's report notes that the Administration's new offer is reportedly the product of discussions with the bipartisan Centrist Coalition, led by Senators John Breaux and Olympia Snowe. The Centrist Coalition issued a stimulus package on November 14 that was flawed in a number of respects, particularly with regard to its proposals to assist unemployed workers and the impact it would have on state budgets. It is therefore not surprising that the "compromise" reached between the White House and the Centrist Coalition continues to reflect flaws found in each of their original proposals.

In addition, by relying on multi-year tax cuts, the Administration's plan incurs significant costs after 2002 that offer no near-term stimulus, since these policies would be in effect when the economy is expected to be in a recovery. While of limited effectiveness as stimulus, these proposals — which provide benefits primarily to higher-income taxpayers and profitable businesses — would nonetheless place more pressure on the budget in the years after 2002. As a result, these proposals would worsen an already deteriorating budget outlook. This seems ill-advised, particularly in the light of the recent acknowledgment by the Administration's Budget Director that the budget will be in deficit for the next several years.