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GOING FOR BROKE

The Fiscal Implications of the Dole Tax Plan

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Republican presidential candidate Bob Dole has proposed a \$548 billion tax cut as the centerpiece of his presidential campaign. At the same time, he insists that he will follow through on his party's commitment to balance the budget by the year 2002. What are the fiscal implications of the Dole tax plan in light of this commitment and the candidate's other commitments with regard to spending?

To date, the Dole campaign has provided few specifics about the areas it would target for cuts. It has, however, said it will not cut Social Security, and it will make no cuts in the military budget or in Medicare beyond the amounts included in the Republican congressional resolution of 1995. Placing these areas (plus interest payments on the debt) off limits leaves only domestic discretionary spending and non-Social Security, non-Medicare entitlement spending as the possible targets of his cuts. The cuts that will be required in these areas will be of such magnitude as to have a devastating impact on basic government services.

Dole's plan for paying for tax cuts

The Dole plan listed four spending cuts, in addition to the substantial cuts already included in the Republican congressional resolution, to offset the revenue lost from the tax cut. They total \$183 billion:

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| • 10% cut in nondefense administrative costs | \$90 billion |
| • Energy Department | 32 billion |
| • Commerce Department | 15 billion |
| • 1% reduction in other spending programs | 46 billion |

The plan also anticipates increased revenues: \$34 billion from auctioning off portions of the radio and television spectrum (many analysts consider this figure optimistic, but it is accepted here for pur-

poses of analysis); \$157 billion more in tax revenue over six years than is anticipated by the latest Congressional Budget Office estimates (\$10,072 billion in the Dole plan compared to \$9,915 billion from CBO); and \$147 billion from an “income growth effect” induced by the tax cut.

For purposes of this analysis, it is assumed that CBO’s revenue projections are correct; this was the position of the Republican Congress in last year’s budget impasse, and these projections have since been accepted by President Clinton as well. This analysis also assumes, based on the evidence of the 1980s, that the income growth effect will be zero. At that time, much larger tax cuts failed to stimulate a positive supply-side response in labor supply, saving, or investment. Thus, there seems little reason to believe that the smaller tax cuts in the Dole plan would have any effect in stimulating growth.

Combining the \$183 billion from the cuts above with the \$34 billion from spectrum sales produces \$217 billion toward paying for the \$548 billion tax cut.

Apportioning the specific cuts

How will the \$217 billion in cuts be apportioned? Since the Dole spending cuts are not clearly specified, some speculation is necessary in assigning them to specific categories. Following the analysis of the Center on Budget and Policy Priorities (1996), this analysis assumes that the 10% cut in nondefense administrative costs will come out of nondefense discretionary-not entitlement-spending. The 1.0% reduction in other spending programs is assumed to come out of nondefense discretionary programs and entitlement programs that have not been specifically excluded in the candidate’s statements.

The four categories of cuts listed above imply reductions in nondefense *discretionary* spending of \$154 billion (i.e., the \$90 billion from the 10% cut, the \$47 billion from Energy and Commerce, and \$17 billion from the 1% reduction in “other spending programs.”), or 71% of the \$217 billion in savings and extra revenue laid out in the plan. In 2002, these “additional actions” referred to in the Dole plan account for \$59 billion in savings. If the cuts for discretionary spending follow the same path, they will account for \$42 billion, meaning that the already low level of domestic discretionary spending for 2002 in the congressional budget resolution-\$245 billion-will have to fall to \$203 billion.

Apportioning the shortfall

Incorporating CBO’s revenue projections and assuming a zero growth dividend will require an additional \$73 billion in cuts in 2002. Apportioning this shortfall equally among all the areas not explicitly protected by Dole (expected to total about \$500 billion in 2002, after the cuts discussed above are included) means an additional \$30 billion in cuts for domestic discretionary spending, lowering the 2002 level of spending to \$173 billion.

The impact on nondefense discretionary spending and entitlements

Nondefense discretionary spending in 1996 was \$272 billion. Adjusting for inflation, approximately \$325 billion would be needed in 2002 to provide the same level of services as are provided at present. This means that *domestic discretionary spending will have to be cut 47% if the country follows the Dole plan*. It is worth noting that the 1996 levels were already reduced by \$6 billion (2.0%) from the amount projected for 1996 by the previous Congress.

The Dole plan also includes all of the proposed Republican cuts in entitlements, plus an extra 16% cut (consisting of the 1% cut explicitly included in the program and the further 15% reduction that would be needed to cover the shortfall in revenues described above) in programs other than Medicare and Social Security.

The nondefense discretionary category comprises the kinds of governmental activities that directly affect the health, safety, and well-being of typical families. Spending on highways, education, meat inspection, airline safety, aid to cities, the weather service, NASA, the CIA, the FBI, even prisons, to name just a few programs, would have to be cut nearly in half to pay for the tax cuts promised in the Dole plan. It seems unlikely that the economic concerns the candidate purports to address through his tax cut will be assuaged by cutting in half the ability of the federal government to promote the general well-being of its citizens.

References:

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