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RECENT LEGISLATIVE ACTIVITY

Beth A. Diebold

The Budget Battle on Capitol Hill: Can America Really Have "All of the Above?"

"The Democrats have phrased the question as: 'tax cuts vs. social security;' 'tax cuts or Medicare;' 'tax cuts or domestic spending' or 'tax cuts versus debt reduction.' But the right answer is not 'this vs. that;' or 'this or that' —the correct answer is 'all of the above!'"¹

U.S. Senator Peter Domenici, R-N.M.

"...[T]o use the old Yiddish proverb: 'You can't dance at two weddings at the same time.'"²

U.S. Senator Paul Wellstone, D-MN

I. Introduction

The battle began in July of this year, when the Congressional Budget Office ("CBO"), a nonpartisan group which studies the potential effects of Congressional budget proposals, released a report forecasting a budget surplus of as much as \$3 trillion over the next ten years, including a surplus of \$161 billion predicted for the year 2000.³ The CBO report stated that approximately two-thirds (2/3) of the surplus expected over the next decade would come from Social Security funds. For instance, \$147 billion of the year 2000 surplus was expected to come from Social Security, with the remaining \$14 billion generated from other sources of revenue.⁴ Until the release of the CBO report, both the White House and Congress, although in agreement on little else, agreed on the importance of setting aside Social Security income and focusing heavily on Medicare spending and deficit reduction. However, the unexpected windfall caused many to envision a myriad of other possibilities for distributing the funds.

The question of what to do with the surplus instantly became a hot topic of debate on Capitol Hill. Although both Congress and the

White House continued to concede the importance of ear-marking Social Security receipts, a controversy arose regarding the amount necessary to set aside.⁵ A White House proposal called for increased spending for a variety of public-assistance programs such as Medicare and education, while both Congressional Houses set out to craft their individual plans.

In late July, the House developed and passed a largely Republican-influenced tax-relief proposal known as "The Financial Freedom Act of 1999."⁶ One of the many provisions included in the House bill was a phased-in 10% across-the-board tax-cut intended to utilize the surplus in a way that would "give back to the taxpayers" and decrease the amount of money set aside for certain governmental social programs.⁷ It took the Senate an additional week to approve its "Taxpayer Refund Act of 1999," a similar, yet much less aggressive tax-cut initiative.⁸

In late July, the Joint Committee on Taxation, made up of members of the Senate Finance Committee and the House Ways and Means Committee, released a conference report outlining the general provisions included in the final piece of legislation.⁹ The heated debate that ensued between strongly-divided parties caused one Senator to remark, "[I] have never seen this body as polarized, as personalized, and as partisan as it is at this moment."¹⁰ The bill also created friction between the Senate and the White House. Throughout the summer, President Clinton repeatedly stated his intent to veto the bill, arguing that such a sharp tax cut was "wrong for America" and "bad for the economy."¹¹ The final version of the bill, sent to the President in September, was promptly rejected.

Ultimately, little benefit may come of the projected surplus funds due to the political gridlock that has developed between Democrat and Republican strategists. Congress was not able to reach a final decision prior to fiscal year 2000, which commenced October 1, 1999. As of this writing, Congress has resolved to keep Federal agencies functioning for at least three weeks into the new fiscal year in an attempt to resolve current budget differences with the White House.¹² The budget complications are so pervasive, however, that according to Rep. David Obey (R-Wis.) Congress could remain in session "past Thanksgiving, past Christmas" before the situation is cleared up.¹³

What exactly are the provisions in the Taxpayer Refund Act of 1999 that have caused a rift among the country's legislators? Is such strong partisan opposition to the bill justified? This article will examine some of the primary features of the proposed legislation,

outlining both supporting and opposing arguments. The article will then present the American public's response to the budget proposals and the legislative grid-lock that has ensued. Ultimately, the existing contention among the members of Congress and the White House appears to reflect partisan interests much more than it does the interests of the American public.

II. Selected Provisions of The Taxpayer Refund Act of 1999

According to Senate Finance Committee Chairman William Roth (R-Del.), in his remarks to the Senate regarding the joint conference report, the Taxpayer Refund Act ("TRA") is designed for the primary purpose of refunding excess taxes to the American people:

The fundamental question before Congress . . . is quite simple: Is it right for Washington to take from the taxpayer more money than is necessary to run the Government? [W]e believe [the] Government is not automatically entitled to the surplus that is, in large part due to the hard work . . . of the American people. Individuals . . . are due a refund, and that is exactly what we do with this legislation.¹⁴

One of the initial proposals of the TRA is the marginal income tax rate decrease of one percentage point per income bracket.¹⁵ For example, the lowest tax-bracket, currently 15%, would be decreased to 14%. The highest current tax bracket, 39.6%, would drop to 38.6%. Republicans argue that the provision enables taxpayers to spend their excess income in ways that they see fit, rather than to allow the government to determine how the excess will be spent.

Just how greatly would taxpayers benefit from such a provision? An individual with a yearly taxable income of \$25,000, for example, currently pays 15% of that income, or approximately \$3750, to the government. Under the TRA, that individual would be required to pay only 14%, or \$3500, in income taxes, amounting to a 7% decrease in the amount spent on taxes.

The TRA would also eliminate the "marriage penalty" tax.¹⁶ Currently, individuals who file separately receive a standard deduction of \$4300, while married couples filing jointly receive a net deduction of only \$7200. In addition, when couples file jointly, their combined income often serves to raise them into a higher tax bracket. Being in a higher tax bracket forces couples to pay a greater percentage of income tax than they would if they filed separately. Under the proposed legislation, not only would married couples be entitled to a standard deduction of \$8600, twice the standard deduction received by

an individual taxpayer, but in situations where the individual income of each spouse fell into the newly-formed 14% tax bracket when filing separately, the couple filing jointly would be taxed at the 14% rate on their combined income as well.¹⁷

Further, the proposed legislation completely phases out the Federal estate, gift, and generation-skipping taxes by 2009.¹⁸ "Death should not be a taxable event," declared Senator Rick Santorum (R-Pa) in a speech to constituents.¹⁹ Under the proposal, estates would be taxed when the property was sold, and not upon the death of the estate-holder. For example, where a deceased parent left a home to a child, the child would incur taxes only if she sold the property, and even then only on the realized capital gain from the sale. In addition, the TRA would index capital gains, so that a taxpayer selling property would not incur capital gains tax on the total amount of gain realized from the sale.²⁰ Instead, the amount taxed would be offset by an amount proportional to the rate of inflation.

Finally, the TRA would allow families to increase contributions to educational IRAs, or educational savings accounts as they are referred to in the bill.²¹ The maximum annual contribution that is currently allowed, \$500, would be increased to \$2000 annually, and the bill would allow individuals to immediately claim tax deductions for interest paid on student loans. Presently, the tax law allows such a deduction only when the taxpayer has been paying interest on student loans for a minimum of 60 months.²²

Ultimately, the proposed tax cuts under the TRA would equal approximately \$800 billion in revenue "returned" to the American public.²³ Republicans argue that this is a good policy, enabling Americans to take advantage of the national surplus as each tax-payer sees fit, and encouraging individuals to provide for their own retirement future.²⁴ Democrats, comparing the Taxpayer Refund Act to that tax-cut program enacted by the Reagan administration, which promptly increased the deficit from \$80 billion to \$200 billion, call the plan a "disaster."²⁵

III. The Arguments: Pro and Con

Although there are provisions in the bill that some Democrats favor, including the elimination of the marriage penalty and even the elimination of estate taxes, the majority of Democrats have strongly argued against the fairness of the bill to low- and moderate-income taxpayers.²⁶ Republicans respond that the bill actually benefits low-income taxpayers the most.²⁷ As mentioned earlier, cutting the tax rate

from 15% to 14% for low-income taxpayers would result in a 7% decrease in taxes paid by individuals in that income bracket. Republicans emphasize that cutting the tax rate from 39.6% to 38.6% for taxpayers in the highest income bracket results in only a 2.6% reduction in taxes paid—less than half the percentage reduction enjoyed by individuals in the 15% bracket.²⁸ Therefore, Republicans conclude, the argument that this legislation disproportionately benefits those in higher income brackets “doesn’t fly.”²⁹

Democrats have been quick to point out the flaws in such logic. While an individual earning \$25,000 will pay 7% less in taxes under the new law, that savings amounts to only \$250 annually. Conversely, the wealthiest 1% of taxpayers in America earns approximately \$830,000 of annual income. Although these individuals will “only” see a 2.6% reduction in taxes paid, they will realize an extra \$46,000 annually.³⁰ “If this is fair, I do not understand fairness,” remarked Senator Kent Conrad (D-N.D.).³¹ A Treasury Department study finds 67% of the benefits from this cut would go to Americans in the top income bracket.³²

The other major issue that Democrats have taken against the bill involves the possibility that such a drastic tax-cut would leave the government short of funds for Social Security and the deficit, ultimately spoiling the rapid economic growth that the U.S. has experienced in the last half of this decade. Referring to what has been termed “fiscal discipline,” Democratic Senator Bob Graham of Florida pointed to the economic growth and the budget surplus of fiscal year 1998 as an example of how prudent financial policy-making during the 1990’s benefitted the Nation.³³ The financial surplus realized in 1998 was the first in nearly thirty years.³⁴ In addition, the Office of Management and Budget recently released a report estimating that the total deficit reduction since 1993 has been approximately \$1.2 trillion.³⁵ Finally, the American economy is in its ninth year of expansion, with nationwide unemployment hovering at only 4%.³⁶

Alan Greenspan, speaking before the Senate and House Banking Committees in August, suggested that “the most effective means that we can have to regenerate the economy and keep the long-term growth path moving higher is if we hold tax cuts until we need a stimulus.”³⁷ Democrats refer to the Chairman’s statement and to the increased deficit that resulted from similar measures taken during the Reagan years in support of their position against tax cuts. According to Democratic Senator Daniel Patrick Moynihan, “To stimulate [the economy] when you don’t need it is to invite inflation . . . which is a tax on anyone when interest rates go up.”³⁸

In defense, GOP members point to another comment in which Chairman Greenspan cautioned that if the only alternative to tax cuts is simply to spend the surplus revenue, then the country would be better off with tax cuts.³⁹ House Ways and Means Committee Chairman Bill Archer (R-TX.) argues that President Clinton's veto of the TRA is simply a "license to spend, and spend he will."⁴⁰ Based on Chairman Greenspan's statements, Archer implies that, although the TRA might wreak havoc on the nation's economy, the President's recent veto of the bill will create even more chaos through increased spending. The conclusion that Archer seems not to reach, however, is that if neither plan is beneficial to the economy then both must be rejected. Perhaps the solution to the present situation is not "all of the above," as Senator Domenici was quoted as saying, but rather "none of it."⁴¹

Ironically, the GOP seems to have obtained its own "license to spend," having already over-spent before budget negotiations have even concluded. A recent CBO report revealed that currently-approved Congressional expenditures are likely to create a \$19 billion deficit in the 1999 surplus.⁴² In other words, although the GOP Taxpayer Refund Act was vetoed, leaving Congress with significantly more funds than those which would have been available had the measure passed, over-spending is still likely to occur. The same report, however, also estimates White House spending proposals to create a deficit as high as \$24 billion, perhaps portending the country's inevitable descent from its current economic boom.⁴³ Democrats certainly do have justifiable concern regarding the future strength of the economy, regardless of whether tax cuts are enacted. Although they decry the lack of fiscal discipline among Republican legislators, they appear to be quite as eager to make the same mistakes.

At the beginning of the current session, Congress vowed to pass the spending bills on time, keep them within the spending limits Congress imposed in 1997, and abstain from spending surplus Social Security money to run the government.⁴⁴ The first of these promises is now broken. Senate majority leader Trent Lott of Mississippi has predicted that the second will be broken soon.⁴⁵

IV. Public Cause for Concern

According to Chairman Greenspan, neither of the current budget proposals are ideal for the American economy.⁴⁶ The public should be concerned that both parties have continued to thwart each other's attempts to arrive at viable solutions, choosing to engage in a

twisted popularity contest rather than to address the pressing economic needs of the country. Did Congress really have the interests of Americans in mind when the tax-cut provisions were created? It would appear not. In a recent Wall Street Journal / NBC News poll, 49% of those polled said the surplus should be spent on Social Security, Medicare, and education, and 25% favored using the funds to pay down the national debt.⁴⁷ Only 20% of those polled favored using the surplus for tax cuts, reflecting a 10% drop from the number who favored tax cuts in the beginning of 1999.⁴⁸ An Illinois shipping clerk remarked to one reporter that he didn't support tax cuts because, "I don't make enough to really get anything back. If they save me \$100, they can keep it."⁴⁹

The Wall Street / NBC poll indicates that Americans are concerned about the deficit, yet for the second year in a row, Congress has spent the surplus funds that were intended to be used to reduce the deficit. As Senator Graham explained, the United States started out with a total surplus from 1998 of \$137 billion, of which \$124 billion was ear-marked for Social Security.⁵⁰ At that point, legislators felt that future surplus revenue could be set aside regularly to save the rapidly declining Social Security program and pay down the deficit. Unfortunately, when legislators were unable to find a way to fund an emergency appropriations bill passed last October, the needed funds, \$13 billion, were taken out of the surplus for 1999. Another \$5 billion was also taken out for 2000.⁵¹ In June of 1999, the surplus was raided again, this time in the interest of the Kosovo crisis, to the tune of \$11 billion. What remains left of the 1998 "surplus" is basically nothing, meaning that no money was set aside to decrease the deficit in fiscal year 1999.⁵² Furthermore, of the \$124 billion which was supposed to be set aside in 1999 for Social Security, only \$108 billion remains.⁵³ According to the CBO report, nothing remains of the 1999 surplus, either. This makes it likely that again, nothing will be applied toward the deficit in 2000.⁵⁴ What will remain of the \$147 billion Social Security surplus from 1999 by the conclusion of fiscal year 2000 is anyone's guess.

V. Conclusion

Unfortunately, the current grid-lock which threatens to hold Congress in session "past Thanksgiving, past Christmas" seems to reflect the partisan interests of Republicans and Democrats more clearly than it does an interest in the American public. Similar face-offs in 1995 and 1996 resulted in government shut-downs and outraged

voters, making it unlikely that a shutdown will occur again. However, perhaps a new crowd of outraged voters would stimulate a greater effort by Congress on the voters' behalf.

Although voters do not seem to be preoccupied with tax cuts, they are concerned with economic stability.⁵⁵ Economists agree that partisan division which has resulted from the debate over this issue is threatening that stability.⁵⁶ By not putting political differences aside, both the Congressional houses and the White House have caused the public to suffer. If Republicans truly believe that Americans "deserve" something for their hard work, and the President truly wants what is "good" for America, then both parties must put themselves aside and put the interests of America first.

Endnotes

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3. See 145 CONG. REC. S10290-01, S10297 (daily ed. August 5, 1999) (statement of Sen. Conrad).
4. Jacob Schlesinger, *Social Security Surplus Triggers Concern*, WALL ST. J., Sept. 7, 1999, at A3.
5. See *GOP Calls Showdown on Tax Cut; Stage Set for Clinton Veto Fight*, DAILY OKLAHOMAN, July 31, 1999, at 1.
6. 145 CONG. REC. H6249, H6253 (daily ed. July 22, 1999).
7. Karin Fischer, *Rockefeller, Byrd Blast GOP Tax Plan*, CHARLESTON DAILY MAIL, July 29, 1999, at 1A.
8. Rod Grams, *Senate Passes Significant Tax Relief* (August 30, 1999), in GOVT. PRESS REL.
9. See 145 CONG. REC. H6249, *supra* note 6.
10. 145 CONG. REC. S10305-01, S10321 (daily ed. August 5, 1999) (statement of Sen. Kerry).
11. *Ruling Out a Compromise, GOP Says Tax Cut Doomed for This Year*, CHI. TRIB., Sept. 10, 1999, at 7.
12. Tim Weiner, *Congress Extends Spending by 3 Weeks*, NEW YORK TIMES, Sept. 29, 1999, at A20.

13. Pianin, *supra* note 11.
14. 145 CONG. REC. S10290-01, S10291 (daily ed. August 5, 1999) (statement of Sen. Roth).
15. *See id.*
16. *See id.*
17. *See* 145 CONG. REC. S10290-01, S10302 (daily ed. August 5, 1999) (statement of Sen. Nickles).
18. *See* 145 CONG. REC. S10290-01, *supra* note 14.
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21. *See id.*
22. *See* Joshua H. Simon, *Harvard U.: Educators Happy With Tax Reform Legislation, Clinton Veto Still Possible*, HARVARD CRIMSON, Aug. 6, 1999.
23. 145 CONG. REC. S10290-01, *supra* note 14.
24. *See id.*
25. 145 CONG. REC. S10290-01, *supra* note 3.
26. 145 CONG. REC. S10290-01, S10294 (statement of Sen. Kerrey).
27. 145 CONG. REC. S10290-01, *supra* note 17.
28. *See id.*
29. *Id.*
30. 145 CONG. REC. S10290-01, *supra* note 3.
31. *Id.*
32. *See* Fischer, *supra* note 7.
33. *See* 145 CONG. REC. S10290-01, S10299 (statement of Sen. Graham).
34. *See id.*
35. 145 CONG. REC. S10290-01, S10293 (statement of Sen. Moynihan).

36. *See id.*
37. *Id.*
38. *Id.*
39. 145 CONG. REC. S10305-01, S10317 (statement of Sen. Gramm).
40. WHITE HOUSE BULL., *supra* note 12.
41. *See* Domenici, *supra* note 1.
42. *Id.*
43. *Id.*
44. Weiner, *supra* note 12.
45. *See id.*
46. *See* 145 CONG. REC. S10290-01, *supra* note 35.
47. Greg Hitt, *GOP Sends Tax Cut to Meet Veto as Prospects for Real Change Dim*, WALL ST. J., Sept. 16, 1999, at A6.
48. *Id.*
49. Jane Norman, *GOP Lawmakers: Iowans Cool to Tax Cut*, DES MOINES REG., Sept. 9, 1999, at 1.
50. *See* 145 CONG. REC. S10290-01, *supra* note 33.
51. *See id.*
52. *See id.*
53. *See id.*
54. *See id.*
55. *See* Hitt, *supra* note 47.
56. *See* 145 CONG. REC. S10290-01, *supra* note 35.

