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POSSIBLE HOUSE APPROACH TO CHILD CREDIT ISSUE WOULD NOT BE FISCALLY RESPONSIBLE

Proposal Would Be More Likely to Harm Children than to Assist Them

by Robert Greenstein

In coming days, House Republican leaders will consider how to proceed on legislation relating to the child tax credit, following approval of such legislation last week by the Senate. According to news accounts, House leaders are considering an approach that would result in yet another costly tax-cut bill, with a price tag of $130 billion or more and with none of this cost being offset. Such an approach was floated in Senate negotiations last week on the child tax credit legislation but was rejected because of the effect it would have in worsening an already grim deficit picture. Due to the fiscal recklessness of such an approach, it would be likely to harm rather than help children — especially low-income children — over the long run. As explained below, if the choice becomes one between passing such legislation and failing to act on the exclusion of low-income working families from the child tax credit provision of the newly enacted tax-cut law, these families and their children would be better served by no action.

The Senate Child Tax Credit Legislation

Child tax credit legislation that the Senate approved June 5 would provide modest assistance to 6.5 million low-income working families with 11.9 million children in 2003 and 2004. The Senate-passed bill would accelerate a provision of law that was enacted in 2001, under which the size of the child tax credit for low-income families is scheduled to increase in 2005. Under the Senate measure, this increase would occur in 2003 rather than 2005. The result would be an increase of $3.5 billion in child tax credits for low-income working families over the next two years.

The low-income families affected would receive an average annual increase in their child tax credit of approximately $150 per child in 2003 and 2004. This Senate provision would have no effect after 2004, and it would not make eligible for the child credit any low-income families that are not already eligible. (Working families with earnings of less than $10,500 are ineligible and would remain so.)

The Senate bill also would extend the child tax credit later in the decade to many higher-income married families, by raising the income level at which the credit begins to phase down for married families from $110,000 to $150,000 by 2010. This would make married families in the $110,000-$150,000 range, who now receive a partial child credit, eligible for a full credit. It also would extend a partial credit to many families in the $150,000-$200,000 range. (The income level at which a family's credit entirely phases out depends on the number of children in the family.) The extension of the credit to these higher-income families would cost $3 billion to $4 billion in tax year 2010. If this provision were extended beyond 2010, as it likely would be, it would provide $30 billion to $40 billion in tax cuts to these higher-income families in the decade after 2010. Analysis by the Urban Institute-Brookings Institution Tax Policy Center shows that, as a result of this provision, 74 percent of the tax benefits that the Senate bill would provide in 2010 would go to the top 10 percent of households, and 99 percent of the tax benefits in 2010 would go to the top fifth of households.

The Senate bill also includes a couple of smaller provisions. Its total cost is $10 billion over ten years. This cost is fully offset through an extension of custom user fees that are slated to expire on September 30, 2003. Both the President's budget and this year's Congressional budget resolution call for these user fees to be extended.

The Possible House Approach

House leaders are reportedly considering adding to the Senate child tax credit provisions a provision that would add approximately $125 billion in cost. The provision they are considering adding would make *permanent* the child tax credit provisions enacted in 2001 and 2003. (The child tax credit provisions included in the tax-cut bill signed into law on May 28 are scheduled to expire — or "sunset" — at the end of 2004. The child tax credit provisions of the 2001 law, like most other provisions of that law, are slated to expire at the end of 2010.)

Under this possible House provision, both the 2004 and the 2010 "sunsets" would be repealed. This would mean that the provision sunsetting the child tax credit increases in the new tax-cut law at the end of 2004 — one of the measures used to keep the law's cost from exceeding $350 billion — would be repealed before the ink on the law is barely dry.

House leaders reportedly do not intend to offset these new costs. The costs would be deficit-financed instead. If House leaders follow this course, it will indicate they are seeking to capitalize on the attention focused on the low-income child tax credit provision to fashion a bill that can serve as the opening wedge of an ongoing effort to eliminate the sunset provisions in the newly enacted tax legislation.

Consequences for Children

The federal revenue base is contracting sharply. Moreover, new budget projections show that if the numerous "sunsets" now written into the tax code are extended without the costs of these extensions being "paid for," federal budget deficits ultimately will reach rather staggering proportions.

- With enactment of the new tax-cut legislation last month, federal revenues will fall this year to their lowest level, measured as a share of the economy, since 1959. Federal *income tax* revenue will reach their lowest level, as a share of the economy, since 1943.

- A new analysis by Brookings economists William Gale and Peter Orszag shows that largely as a result of the 2001 tax cut and the just-enacted tax cut, the federal income tax code now contains "sunsets" to a vastly greater degree than in the past. Gale and Orszag demonstrate that if all of the provisions of the tax code that are set to expire in coming years are extended without those extensions being "paid for," the cost of the extensions will reach *$430 billion* a year by 2013. They

> also show that this cost will equal 2.4 percent of the Gross Domestic Product, which is triple the average size of the Social Security shortfall that the Social Security trustees project over the next 75 years.
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> Orszag has noted that "it is not an exaggeration to state that the future fiscal health of the nation will depend in important part on whether these extensions are paid for."

As a result, what is at stake is much more consequential than whether the low-income child tax credit provision takes effect in 2003 or 2005. The matter at stake is not whether the increase in the child credit to $1,000 should or will be extended beyond December 31, 2004; sooner or later, the increase in the child credit almost certainly will be extended. Rather, the issue at stake is whether major tax cuts will be extended *without* the costs of the extensions being offset, or whether a more responsible course will be steered and such costs will be paid for. Goldman-Sachs recently described the nation's long-term fiscal situation as "terrible." If the tax-cut measures that are scheduled to expire are extended without the resulting costs being offset, the nation's long-term fiscal picture will become markedly worse.

The decisions made on this matter are likely to have profound consequences for children. If the "sunsets" in the tax code are removed without the costs of such action being offset, the result will be both to pass a greater mountain of debt to the nation's children and to create intense pressures for increasingly severe cuts over time in federal programs. With low-income children being one of the nation's weakest political constituencies, programs to assist them will likely suffer from the deep budget cuts that will become almost inevitable.

For these reasons, in the days ahead, if the choice comes down to being between a) passing a measure that restores the low-income child tax credit provision but uses this restoration as a vehicle for a tax-cut bill with these large costs, and b) failing to accept such a bill even if that means no action is taken on the provision for low-income children, then low-income children will be better served by no action.