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CONTRACT '94

THE WHITE HOUSE

REPUBLICANS AND SOCIAL SECURITY

1. THE REPUBLICAN CONTRACT WITH AMERICA WOULD INEVITABLY LEAD TO SEVERE CUTS IN SUCH PROGRAMS AS SOCIAL SECURITY AND MEDICARE: The Republican Contract's call for a combination of tax cuts, military increases and a balanced budget would create a budget that inevitably would require significant and severe cuts in Social Security and Medicare. Analyses of the plan show that the tremendous budgetary savings necessary to balance the budget, fund the tax cuts and pay for military increases would require cuts of 22% in all other programs, including Social Security. Exempting Social Security would force all other programs, including Medicare, veterans, education and crime to be cut by 31%. Exempting both Social Security and Medicare would force all other programs to be cut by 43%. (See p. 6, An Analysis of Paying for the Contract)

> *Social Security Cuts:* The top Social Security expert in the United States, Robert Ball (the Social Security Commissioner for Nixon, Johnson and Kennedy) has estimated that "there is no place to go" but to cut Social Security and has warned that "Social Security recipients beware." According to the U.S. House Budget Committee, the Contract would cut the average Social Security recipient's benefits by $1,953 yearly. (U.S. House Budget Committee, 9/30/94)
>
> *Medicare Cuts:* Mr. Ball estimates that if Social Security was not included, the Contract would require a 30% cut in Medicare as well as all other programs. (St. Louis Post-Dispatch, October 20, 1994). In the last two years, the Republicans have tried to cut Medicare nine times. The Senate Republican Contract explicitly calls for Medicare cuts. The Senate Republicans put a list of options for paying for a fraction of their trillion dollars in promises. In that list, they included $124 billion in Medicare cuts – cuts that the President had called for only to fund long-term care and drug benefits in the context of universal coverage.

2. THE HOUSE REPUBLICANS EXPLICITLY CHOSE TO ALLOW SOCIAL SECURITY TO BE CUT TO FULFILL THEIR CONTRACT: In both 1992 and 1994, the House of Representatives considered a balanced budget amendment. In each year, a version was presented that would have protected Social Security from the requirements of the balanced budget, while each year another option left Social Security vulnerable to cuts. ***THE HOUSE REPUBLICAN CONTRACT THAT OVER 350 MEMBERS AND CANDIDATES SIGNED EXPLICITLY INCORPORATES THE BALANCED BUDGET AMENDMENT THAT PERMITS SOCIAL SECURITY TO BE ON THE TABLE.*** Some are trying to say that they will not cut Social Security, but any protection of Social Security is completely omitted from the Contract when it could easily have been included.

3. LEADING EXPERTS AND MEDIA OBSERVERS AGREE THAT THE REPUBLICAN CONTRACT IS A THREAT TO SOCIAL SECURITY:

U.S. House Budget Committee: The Contract would cut the average Social Security recipient's benefits by $1,953 yearly. (U.S. House Budget Committee, 9/30/94)

Robert M. Ball, (Commissioner of Social Security from 1962-1973) St Louis Post-Dispatch, 10/20/94: "Is this a 'contract' or a dream? Can they really do all these things without touching Social Security? It doesn't seem possible. Something has to give.... Social Security recipients beware. Unless you seriously believe that those who signed the 'contract' would advocate major defense cuts and major tax increases, there will be no place for them to go in 2002 other than to the $500 billion being paid to the 48 million Social Security beneficiaries.... Given time, the voters will surely realize that the 'Contract with America' doesn't add up. You can't cut taxes, increase expenditures and balance the budget while protecting defense spending and Social Security."

New York Times Editorial, 9/28/94: "The Republicans ought to admit their programs would require cutting hundreds of billions out of about $1.5 trillion in Federal spending - ***thus slicing 20 percent or more out of every program from Social Security to the F.B.I.*** Mr. Gingrich promised a positive vision. What voters get instead was duplicitous propaganda."

E.J. Dionne, Jr., The Washington Post, 9/27/94: "If Republicans want to be the low-tax, small-government party they claim to be, they need to be candid about how much they'd have to cut Social Security, Medicare, and other big, popular programs to get there."

Gloria Borger, U.S. News & World Report, 10/3/94: "Well-off seniors who think Gingrich & Co. are giving them a break ought to think twice: With a balanced budget and no defense cuts or tax increases the money has to come from somewhere."

Thomas Oliphant, Boston Globe, 9/25/94: "To pay for all this largess AND balance the budget would require at least a 20 percent slash across the board in domestic program budget - including Social Security, Medicare and crime. Exempt Social Security and the requirement jumps to 30 percent."

4. IN ADDITION TO THE CONTRACT, REPUBLICAN LEADERS HAVE PROMOTED OTHER EFFORTS THAT THREATEN THE INTEGRITY OF SOCIAL SECURITY: Republican leaders have called for either phasing out or replacing Social Security with the types of voluntary or individually controlled proposals, that the AARP has recently said, "pose... a serious threat to the integrity of the Social Security program, as well as to the retirement system as a whole." (American Association of Retired Persons, 10/4/94)

EXAMPLE 1: **THE REPUBLICAN CANDIDATE FOR SENATE IN VIRGINIA, OLLIE NORTH, HAS CALLED FOR ENDING SOCIAL SECURITY IN ITS CURRENT FORM AND MAKING THE PROGRAM VOLUNTARY:** Ollie North has recently raised the issue of ending Social Security as we know it and making it a voluntary program. ("Volunteer Social Security? North opens a new issue," Richmond Times-Dispatch, 10/25/94, "North Stirs Ruckus On Social Security: Opponents Thrash His 'Voluntary' Idea," Washington Post, 10/26/94, and "North: In future, Social Security may be voluntary," The Virginian Pilot and the Ledger Star, 10/25/94.)

> **Henry Aaron, The Chair of the Economics Division of the Brookings Institution,** "It's positively foolish. Most people have the good sense to understand that making this voluntary would completely defeat the goal of trying to make sure that people have enough income when they reach retirement age." Washington Post, (October 26, 1994) Top Republicans who have endorsed North, including Kemp, Gramm, Gingrich, Dole and Baker have failed to repudiate this policy so far.

EXAMPLE 2: **A MAIN CO-AUTHOR OF THE HOUSE CONTRACT, DICK ARMEY, CO-SPONSORED A PROPOSAL THE AARP CALLS A THREAT AND REFUSED ON CNN TO PLEDGE NOT TO CUT SOCIAL SECURITY TO PAY FOR THE CONTRACT.** Dick Armey co-sponsors H.R. 306, the Individual Social Security Retirement Account Act of 1993 (head sponsor is Rep. Porter, R-Ill.) which was a partial version of a mandatory individually-controlled retirement account. This proposal co-sponsored by Armey and 17 other House Republicans, was specifically cited by the AARP as one of the types of proposals that "poses a serious threat to the integrity of the Social Security program." Furthermore, on CNN's "Crossfire", Republican Congressman Dick Armey refused to pledge that the Republican "Contract with America" wouldn't cut Social Security. The exchange went as follows:

> **MICHAEL KINSLEY** (to Armey): "Are you going to take the pledge? Are you going to promise not to cut people's Social Security to meet these promises?..."
>
> **Rep. DICK ARMEY**: "No, I'm not going to make such a promise." (CNN's Crossfire, 9/27/94)

EXAMPLE 3: **THE OTHER MAIN CO-AUTHOR OF THE REPUBLICAN CONTRACT, NEWT GINGRICH, HAS CALLED FOR PHASING OUT SOCIAL SECURITY AND REPLACING IT WITH MANDATORY IRAS AND A MASSIVE VAT TAX INCREASE. A GINGRICH-PORTER PROPOSAL TO PHASE OUT SOCIAL SECURITY WAS PRAISED BY GEORGE BUSH IN 1990, BUT CRITICIZED BY SENATOR MOYNIHAN:** One of the two main authors of the House Republican Contract, Whip Newt Gingrich, has previously called for abolishing Social Security and turning it into a mandatory IRA program with an additional Value Added Tax to pay for the lost revenue from ending the system of using Social Security payroll taxes to pay for Social Security benefits. (Atlanta Constitution, November 7, 1986) President Bush praised, while Senator Moynihan criticized, a Gingrich-Porter proposal to phase-out Social Security in 1990. ("Bush Calls GOP Lawmakers Social Security Plan Innovative," AP, January 24, 1990.)

Associated Press, January 24, 1990: "Bush said he was 'not prepared to endorse' a plan sponsored by Rep. John E. Porter, R-Ill., and the House Republican whip, Newt Gingrich of Georgia. 'It's worthy, though, of some study,' he said. Under the Porter-Gingrich proposal, Social Security taxes would be gradually channeled into a type of Mandatory Individual Retirement Account. As workers' IRAs grew, their claim on Social Security would decline. By the time today's workers are retired – about 50 years from now, Porter estimated – Social Security would be fully privatized.

Moynihan, who is considered one of the government's top authorities on Social Security, said of the Republican congressmen's proposal, 'The president described that as 'innovative thinking'. Was it innovative thinking after 50 years of steady payments to start dismantling Social Security? I don't think so.'"

PR Newswire, January 22, 1990: "The National Council of Senior Citizens (NCSC) today denounced as 'dangerous and destructive' a proposal by House Republicans to privatize the social security system. Responding to statements by Rep. John Porter (R-Ill.) and House Minority Whip Newt Gingrich (R-Ga.) calling for the 'gradual privatization' of the program, NCSC Executive Director Lawrence T. Smedley said, 'This proposal represents the potential for the destruction of social security, a program on which almost all Americans depend for financial security in their retirement years.'"

Mickey Kaus, *The New Republic*, March 9, 1987: "Gingrich keeps Social Security for those over 40, but requires those under 40 to set aside ten percent of their wages in a 'mandatory IRA' that completely replaces Social Security for them. It all sounds like a delicious free lunch.... Gingrich makes it sound as if today's workers would even come out ahead. He would abolish the 14 percent payroll tax, but only require a ten percent IRA investment. 'Workers under 40 would have their take-home pay increased by four percent,' he says. It's too good to be true. Social Security, remember, is now a pay-as-you-go system. Today's retirees are supported by the payroll taxes paid by today's workers. Du Pont and Gingrich want today's workers to keep supporting these current retirees, without diminishing benefits. But then they also want today's workers simultaneously to be saving up to pay for their own retirement. Something's got to give. It does. Both plans contain huge hidden tax increases on current workers.... Gingrich's scheme has an equivalent kicker: he would eliminate the payroll tax, but replace it with a value-added tax. For decades, however, this value-added tax would have to raise as much revenue as the payroll tax it replaced, because it must pay for regular Social Security benefits for everyone over 40. So the payroll tax is replaced with an equivalent value-added tax, plus younger workers are required to set aside an additional ten percent of their paychecks to pay for their own retirement."

EXAMPLE 4: THE REPUBLICAN CANDIDATE FOR SENATE IN PENNSYLVANIA IS OFFENDED THAT SENIORS ARE ALLOWED TO RECEIVE SOCIAL SECURITY AT AGE 65: Republican candidate Rick Santorum said, "It's ridiculous that we have a retirement age in this country of age 65..." (Lasalle University, 10/18/94) He has called for raising the retirement age to 70.

5. PAST EXAMPLES OF REPUBLICANS SEEKING TO CUT SOCIAL SECURITY:

- In 1981, **Reagan/Bush proposed $81.9 billion in Social Security cuts** over five years, including a COLA delay, cutting benefits for early retirees by 25%. [1981, CQA, p.118]

- In 1982, **Senate Republicans called for a 3-year, $40 billion cut in Social Security** benefits.

- In 1985, **Senator Dole authored a budget resolution that would have eliminated the 1986 Social Security COLA**. 48 Senate Republicans and Vice President Bush (who broke the tie) voted to support the measure, which passed by a 50–49 margin.

- 1986–1987: **Newt Gingrich and Pete Dupont called for phasing out Social Security** and going to a mandatory IRA program.

- 1990: **President Bush partially praises a Gingrich–Porter proposal to phase-out Social Security, though Senator Moynihan criticizes it.**

- In 1992, **Pat Robertson supported ending Social Security** as it exists today. Robertson wrote, "I personally have advocated... the substitution of a compulsory private system... Such a plan in some form would be a boon to the economy and the salvation of retirement benefits for workers under forty." (Pat Robertson's Perspective, April/May, 1992)

AN ANALYSIS OF PAYING FOR THE CONTRACT

The Contract calls for a balanced budget, major tax cuts, and increased defense spending. The five-year cost is more than $1 trillion and the seven-year cost is more than $1.6 trillion. In addition to these cumulative costs, it is important to also look at what percentage of the budget would have to be cut in order to pay for the Contract in the year the Republicans would make good on all of their promises. Since the Contract calls for the budget to be balanced by FY 2002 (Rep. Armey's bill calls for balance by FY 2000), the following analysis examines annual spending for FY 2002 alone.

According to the CBO, there would be $1,891 billion in revenues and $2,209 billion in spending leading to a deficit of $319 billion in FY 2002. Thus, to balance the budget, the House Republicans would need to cut $319 billion off the baseline spending plus find enough savings to pay for their tax cuts and additional spending. A conservative estimate is that their plan would require an additional $102.5 billion in savings in FY 2002. *Thus, while their plan would call for savings of over $1.6 trillion over seven years, supporters of the Contract would have to find a total of $421.5 billion in savings in the single year of FY 2002 alone.*

How would they do it? To be generous, we will assume that they would get $50 billion in interest savings in FY 2002 -- though that is very generous. Subtracting this amount leaves $371.5 billion in savings the Republicans must find in the remaining budget. Since we have given them interest savings, interest has to be taken off the table, as does defense -- since they say they want to increase it. Thus, the Republicans start with a pool of $1,689 billion in available savings to cut from in FY 2002.

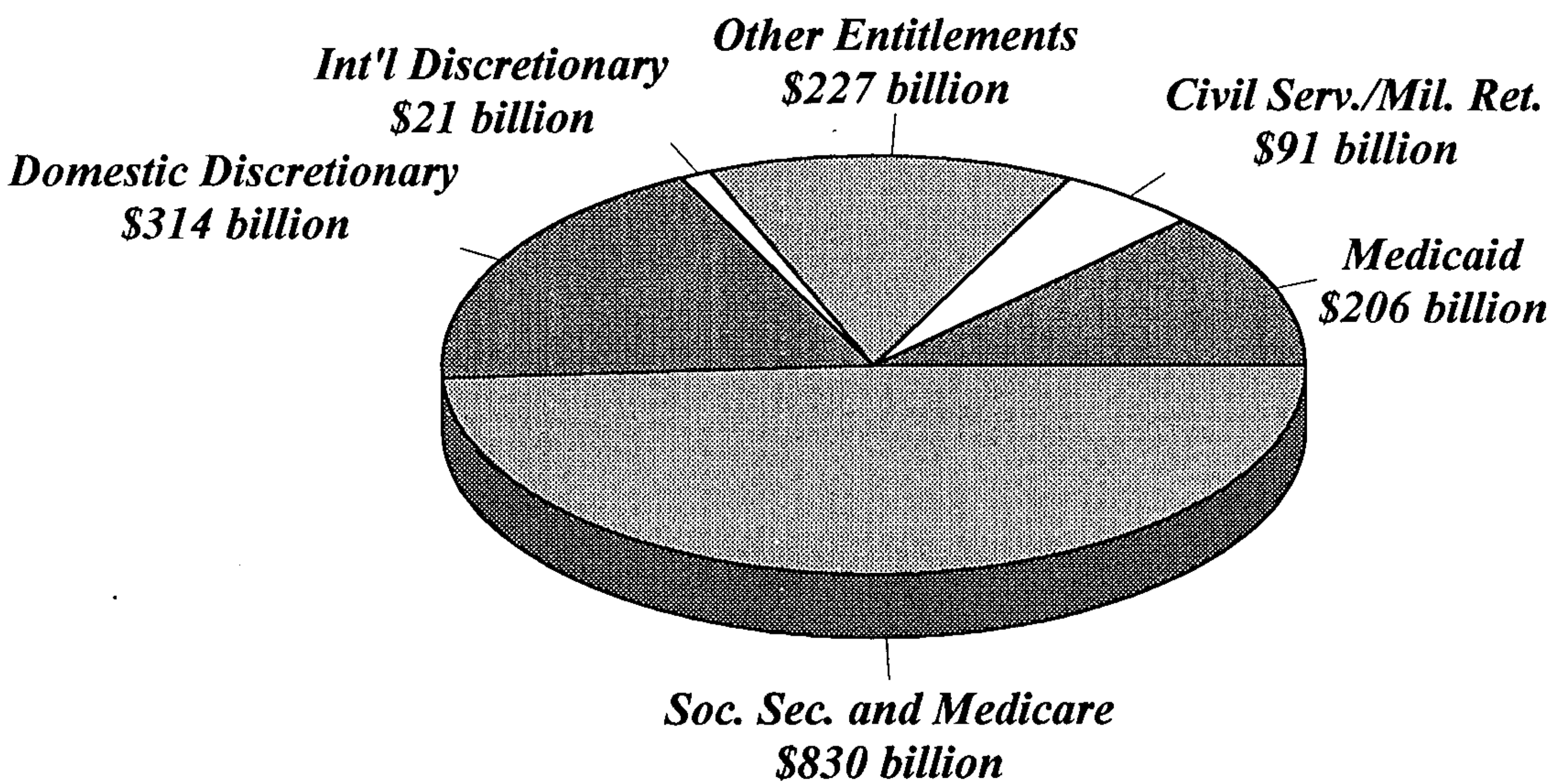
Domestic Discretionary	$314 billion
Int. Discretionary	21
Medicaid	206
Social Security	476
Medicare	354
Civ. Service and Ret.	91
Other	227
TOTAL	$1,689 billion

22% Across the Board Cut on Social Security and Medicare: Thus, they then have to reduce spending by $371.5 billion out of a remaining pool of $1,689 billion. This would mean a 22% reduction across the board in all programs, including Social Security.

31% Cut on Medicare and All Other Programs: If they take Social Security off the table, $476 billion must be removed from the pool of potential savings and they would have to cut $371.5 billion out of $1,213 billion -- a 31% cut in all remaining programs, including Medicare.

43% Cut on All Non-Social Security and Medicare Programs: If they take Social Security and Medicare off the table, $354 billion more must be removed from the available pool of savings and they would have to cut $371.5 billion out of $859 billion -- a 43% cut across-the-board in all other programs.

The Republican "Contract with America" requires *$371.5 billion* in savings in FY 2002. What will they cut?



PROGRAMS AVAILABLE FOR SPENDING CUTS, EXCLUDING DEFENSE
(CBO FY 2002 Projections)

St. Louis Post-Dispatch, Thursday, October 20, 1994, at 7B

'Contract With America' Doesn't Add Up

By Robert M. Ball

Three hundred Republican candidates for Congress — incumbents and aspirants — stood on the steps of the Capitol the other day and signed a "Contract with America," which promises tax cuts, spending increases and a constitutional amendment requiring a balanced budget by the year 2002. These objectives are to be accomplished at the same time and without cutting Social Security and defense.

Is this a "contract" or a dream? Can they really do all these things without touching Social Security? It doesn't seem possible. Something has to give.

If defense and Social Security are ruled out, the respected and nonpartisan Congressional Budget Office estimates remaining expenditures for the year 2002 at $1.13 trillion and the deficit for that year at $319 billion. These are the figures for present programs without change. But eliminating the deficit in 2002 under the "contract" will require even greater reductions because of the proposed tax cuts and spending increases. A conservative estimate of the cost of these changes for 2002 is about $80 billion, offset by interest savings of $50 billion from eliminating the deficit.

To carry out the contract, cuts of about $350 billion would need to be made in the $1.13 trillion of non-defense, non-Social Security spending. This works out to an average cut of 30 percent in all other activities of the federal government: Medicare for some 41 million elderly and disabled beneficiaries, Medicaid (the health-care program for those with low incomes including long-term care for the elderly), food stamps, farm supports, payments to poor mothers and children, payments to retired military and civilian employees, the operation of the FBI, meat inspection, the supervision of drug safety, research into the causes and cures for disease, veterans programs, etc.

Make up your own list of other federal services. If any of them are cut less than 30 percent, others would have to be cut more. Does this sound like a real world proposal?

It isn't.

Perhaps the tax cuts and spending increases could get approval. This is the easier part of the plan to vote for. But you can be sure that average cuts of 30 percent in present programs will not even be proposed. Only savings from "welfare reform," cuts in nutrition programs and cuts in the cost of the recently passed crime bill are part of the "contract." According to the Republican staff of the House Budget Committee, these savings would amount to $45 billion.

Some illustrations of possible additional budget cuts are listed in the material released with the contract, but even if all those illustrations were proposed and passed, a truly improbable event, the total savings claimed are just $176 billion *over five years*. All the savings in present programs even mentioned by the sponsors of the contract make only a small dent in the $350 billion needed for the year 2002 alone.

So what happens when the constitutional requirement, which is part of the plan, kicks in? You've got it. Social Security recipients beware. Unless you seriously believe that those who signed the contract would advocate major defense cuts and major tax increases, there will be no place for them to go in 2002 other than to the $500 billion being paid to the 48 million Social Security beneficiaries.

Given time, the voters will surely realize that the "Contract with America" doesn't add up.

You can't cut taxes, increase expenditures and balance the budget while protecting defense spending and Social Security. But will voters realize it before or after the upcoming election?

Robert M. Ball, commissioner of Social Security from 1962-73 [redacted]

THE WHITE HOUSE

WASHINGTON

September 26, 1994

MEMORANDUM FOR WHITE HOUSE SENIOR STAFF

FROM: Gene Sperling and David Dreyer

SUBJECT: "Contract with America"

Attached are several articles in which the fiscal credibility and political wisdom of the House "Contract with America" have been questioned. Also included are three strong wire stories based on a White House wire tong this afternoon.

1. "The Price of Pandering" by Gloria Borger

2. "GOP Shakedown" by Jack Anderson and Michael Binstein

3. "Voodoo Economics: The Sequel" by Robert S. McIntyre

4. "GOP Congressional Primary Results Rattle Democrats" by Ronald Brownstein

5. "GOP's Fiscal Shell Game" by Thomas Oliphant

6. "The Third Wave is Coming, but it's Not in GOP's 'Contract'" by Morton Kondracke

7. "Republican 'Contract' May Give Democrats Some Issues to Attack" by Charles Cook

8. "Clinton Aides Blast Republican Tax Cut, Budget Bills" by Richard Cowan

9. "Democrats Sat GOP's Numbers Add Up to Return of Reaganomics" Associated Press

10. "Clinton Aides Scornful of Republican 'Contract'" by Gene Gibbons

U.S. News & World Report 10-3-94

ON POLITICS

BY GLORIA BORGER

The price of pandering

Newt Gingrich and the gang long ago figured out that the media often mistake sound and fury for news. So to help fire up their conservative insurrection, they attacked Democratic Papa Bear Tip O'Neill, toppled House Speaker Jim Wright, openly shunned moderate Senate Republicans and pioneered the use of C-SPAN as their personal studio. Back in 1979, when master of ceremonies Newt was new, there were 158 Republicans in the House of Representatives. They mostly lived a quiet life, predictably opposing Democratic taxers and spenders. Now, there are 178 Republicans, and they sense a new opportunity: a real shot at winning effective control of Congress. They can hardly contain themselves.

Their latest production is a grandly orchestrated and carefully planned photo opportunity. The script calls for Republican House incumbents and wannabes to pose together on the Capitol steps this week and unveil a neatly packaged "Contract with America," a set of 10 promises that they pledge to vote on within 100 days *if* they win control of the House. The Capitol is an odd backdrop for candidates who are trying to pose as outsiders, but then their contract is a bit less revolutionary than it appears.

ERIK FREELAND FOR USN&WR

Sound and fury. *GOP leader Gingrich feeds the press.*

Even if the public buys his pitch, Republicans may come to regret it.

For one thing, the Republicans do not actually promise to pass anything: that would smack of governing, which they eschew. "We are saying we know you don't like politicians, and we are drawing a distinction between us and them," says Republican pollster Frank Luntz. But in the best tradition of cynical modern politics, Luntz pretested the GOP's principles on selected focus groups before Gingrich unveiled them.

Golden oldies. The Republicans' message is Gingrich at his clever best: Dream up a Christmas list and paste it to the refrigerator. If we don't deliver, the House Republicans say, throw us out. "This is the first time a group of political candidates have gotten together to sign on the dotted line," says Luntz. The ploy would be a political coup, except for one problem: Gingrich's list is just a collection of GOP golden oldies that pander to the public's desire to get something for nothing – the balanced-budget amendment, a middle-class-tax cut, a capital-gains-tax cut, term limits, the repeal of some Social Security taxes along with the marriage penalty and tough welfare reform.

Gingrich promises to deliver all these goodies without cutting defense or Social Security. Republican cost estimates have inched upward with every new inquiry, but the latest is a relatively modest $140 billion over five years – an amount Republicans argue can be financed with digestible cuts in social spending and revenue gains. "We can pay for this, and we will do it," insists GOP budget entrepreneur John Kasich. In an internal document prepared to rebut the GOP, the Clinton administration reckons the cost at more than $1 trillion. "Not only are they not close," claims one administration official, "they're not even close to close."

Just balancing the federal budget by the year 2000 would require about $700 billion in new budget cuts or tax increases. And Republicans themselves concede that raising the per-child income-tax credit to $500 would cost $100 billion, and a capital-gains-tax cut an additional $56 billion. Another GOP idea, repealing the recent congressional decision to tax some benefits paid to the wealthiest 13 percent of all Social Security recipients, would add $21 billion to the tab over the next five years.

Add a dose of hypocrisy to the questionable math: The same Republicans who rail about ending an "unfair" Social Security tax on the wealthy are proposing to do essentially the same thing with Medicare, reducing some benefits for those whose retirement income exceeds $100,000 a year. Well-off seniors who think Gingrich & Co. are giving them a break ought to think twice: With a balanced budget and no defense cuts or tax increases, the money has to come from somewhere.

Small wonder that Senate Republicans, who recognize that leadership occasionally requires taking responsibility, have decided to pass up this contract. "It's a reflection of people who have never governed," says one GOP moderate. "Our leadership wouldn't let serious people sign on to something like this." Even some House Republicans who hate term limits are fidgety. Still, they took the pledge because it merely promises a vote: they didn't have to say *how* they would vote. It is the sort of pre-election stunt that should make them cringe.

It probably won't. "This is designed to appeal to every American who believes in a strong family and creating jobs and who want a healthy and growing economy," says Gingrich. But even if the public buys his carefully aimed pitch in November, his fellow House Republicans may come to regret it. The voters, after all, might actually make them honor their contract. ■

Washington Post 9.25.94

Jack Anderson and Michael Binstein

GOP Shakedown

More than 300 Republican House candidates will be herded to the steps of the U.S. Capitol Tuesday morning to offer a "contract with America." Later that night, Republicans will cut another contract with lobbyists and special interests at a GOP gala.

During the first two years of the Clinton administration, Republicans have proven they know the price of everything from medical care to midnight basketball. But the fund-raising dinner for this year's congressional candidates shows they also appreciate the value of political access. The National Republican Congressional Committee has fired off a two-page fund-raising letter that reads more like a rate card than a reform agenda.

NRCC Chairman Bill Paxon begins his pitch to GOP contributors by waxing sentimental about standing beneath "the watchful eye of the Statue of Freedom" on Tuesday and restoring "our Founding Fathers' dreams of a government of the people, by the people and for the people."

That's a strange preamble for an old-fashioned political shakedown. For individuals and PACs, a table of 10 is fetching $5,000 for the GOP. Corporations must pay $7,500 for a table—but they won't complain since the GOP "contract" teems with tax breaks they've been coveting. NRCC officials say they've sold 140 tables.

Paxon writes: "With the purchase of a table, donors have the option to request a Member of the U.S. House of Representatives or Congressional Candidate and his/her guest to complete the table of 10. . . . In addition, one attendee per table may join the Private Reception with the House Republican Leadership and other, special VIP guests prior to the Gala."

It's unclear which of the two contracts is binding on Republicans: the written or the unwritten. In both cases, there's a large degree of false advertising.

The unwritten contract will be sealed Tuesday night with the special interests, who will want to collect on it in the future. The written contract is a checklist of 10 bills to be voted on in the first hundred days if Republicans take control of the House. Its economic promises have an all too familiar ring: Trust the Republicans to cut taxes, balance the budget and not hurt the needy.

Though the written contract could turn out to be more fantasy than fact, a senior White House official told our associate Ed Henry that the Clinton administration is taking the Republicans at their word. "Over the next five years, they'd have to cut a total of $858 billion in spending in order to make these tax cuts and still balance the budget," this official said.

Republican pollster Frank Luntz, who has been working on Tuesday's event, explains it this way: "You have to make a commitment to the concept first and then you deal with the details."

There's also the question of how Republicans propose to clean up Congress without reforming the corrupting system of campaign finance. There is no mention of the money chase among the top legislative priorities. "[Campaign finance reform is] a cutting issue with the swing voters," Luntz told us. "A fair conclusion is that you can't change the system if you benefit [from it]. It's going to take people on the outside, a new Congress with a lot of freshmen."

Rep. Dick Armey, a catalyst behind the "contract," suggests Republican candidates will get a sort of freshman orientation Tuesday night. "I have to say that the [fund-raising] event is incidental to the fact we are going to have all our candidates in town that day," Armey told us. "Since our candidates are already [here] for the contract this was an opportunity for the PAC community to meet them."

Paxon declined to be interviewed, but an NRCC spokesman offered this novel justification: Republicans are throwing the special interest gala because it will raise money to defeat "Democratic incumbents who are the main obstacles to PAC reform."

To be sure, both Republicans and Democrats have dirty hands. But Republicans have largely stayed in the rafters, jeering and second-guessing Democrats. Only last week did Democrats manage to overcome Republican opposition to forge a tentative deal on lobbying reform.

That reform was part of Bill Clinton's "contract" with voters in 1992.

Washington Post 9.25.94

Voodoo Economics: The Sequel

From the GOP Witch Doctors Who Busted the Budget, More Tax Cut Sorcery

By Robert S. McIntyre

REMEMBER A decade and a half ago, when supply-side Republicans promised they would cut everybody's taxes and balance the budget at the same time? Remember how, as it turned out, most people's taxes went up and the deficit skyrocketed—while the only thing that went down were taxes on the very rich?

Well, here they go again.

The Republican plan, due to be formally announced with much fanfare this week, is familiar in its cynicism. It promises large, unfunded income tax cuts—targeted to the well-off—and enormous corporate tax reductions bundled together with a constitutional amendment that will magically (and, by implication, painlessly) balance the budget. All across the country, Republicans are campaigning on this incongruous combination. The danger is not just that voters may respond favorably, but that President Clinton may let himself be pushed into a 1995 tax-cut bidding war that could undermine his hard-fought deficit reduction victory of 1993.

The collection of tax-cut proposals to be unveiled on Tuesday could, when fully implemented, add $120 billion a year or more to the budget deficit. An even more radical plan, proposed by unreconstructed supply-sider Rep. Dick Armey (R-Tex.) and endorsed by numerous GOP candidates, could cost in excess of $200 billion annually.

Let's start with the more far-out plan, Armey's Freedom and Fairness Restoration Act. The plan would replace the progressive personal and corporate income taxes with what amounts to a 17 percent flat-rate national consumption tax.

To be sure, the part of Armey's plan that calls for wiping out all loopholes and taxing all income equally has some surface attraction. But that's not what his plan actually entails. Far from eliminating tax breaks that benefit the well-off at the expense of the rest of us, Armey would institute a giant loophole by exempting most capital income—interest, dividends, capital gains, rents, etc.—from taxation entirely.

Under Armey's plan, businesses would be taxed on their gross receipts minus the cost of the goods and services they buy from other producers who have already paid tax on them. But unlike a standard value-added tax, which taxes payments to workers at the employer level, Armey would allow businesses to deduct the cash wages and pensions they pay. Instead, such payments would be taxed as they are received by workers and retirees. This feature allows Armey to cut the apparent regressivity of a standard sales tax by exempting the first $12,350 in wages for single people, $21,200 for a single parent with one child and $34,700 for couples with two children. (Under current law, couples with two kids start paying income taxes when they make more than $23,200 in total income.) In effect, this feature offers families a rebate against their sales tax equal to 17 percent of their wages up to the exemption amounts.

That might sound generous but, in fact, current law, thanks to the expanded earned-income tax credit, is already more generous for many low- and moderate-income families who would face substantial tax hikes under the Armey plan. Still Armey's wage tax rebates would end up exempting over half of total wages from his new tax.

Which brings up the still larger flaw in the Armey scheme: It would aid massively to the federal budget deficit. In fact, a reasonable estimate—just confirmed by the Joint Committee on Taxation—is that Armey's proposal would cost the Treasury over $200 billion a year. That would multiply annual government borrowing, as a share of the economy, back up to Reaganesque levels.

Look at it this way. According to the Congressional Budget Office, the best-off 1 percent of the population now pays just under a third of the total federal personal and corporate income tax bill—at a rate of about 31 percent of that group's total income. Even if Armey's tax applied to all of their income, they would still see their income taxes cut almost in half with his flat rate of 17 percent. But since Armey would exempt investment income from taxation, the tax cut for the well-off would be much, much larger.

Now, if Armey wants to cut income taxes on the wealthy by more than half—and purports to cut taxes for the middle class as well—how does he expect to raise enough money to avoid skyrocketing deficits? The answer is, he doesn't.

Armey's mentors are Hoover Institution economists Robert Hall and Alvin Rabushka. Back in 1983 Hall and Rabushka calculated that for their plan to break even, it would need a rate of 19 percent and wage-tax exemptions only a third as large as Armey proposes (and far below those provided by the current income tax). In that case, they admitted, their plan would "be a tremendous boon to the economic elite"—but also produce much "higher taxes on average people."

The obvious problems with the Armey flat tax have not stopped many Republican political hopefuls from endorsing it. For instance, GOP Senate candidates from Michael Huffington in California to Chuck Haytaian in New Jersey have signed onto the plan. (Haytaian's confusing platform combines a purportedly loophole-free flat tax with a call for keeping many existing tax breaks and adding a new one for health insurance.) Massachusetts's Republican Gov. William Weld also has praised the Armey plan, as has conservative pundit George Will. Weirdly, Will is particularly fond of the fact that Armey's plan would repeal tax-withholding. Although this would require wage-earners to file 12 tax returns each year rather than one, Will sees this added burden as beneficial because it would make people angrier at government. So much, one might say, for tax simplification.

Perhaps recognizing that the Armey plan looks remarkably like the much-criticized flat tax proposed by Democratic presidential candidate Jerry Brown in 1992, GOP leaders in Congress have settled on a different set of tax cut proposals. The leadership's plan includes these costly features:

- A $500-per-child tax credit that would cost more than $26 billion per year.
- Repeal of the 1993 change that, at higher income levels, includes 85 percent of Social Security benefits in adjusted gross income. Under the GOP plan half, at most, of Social Security would be subject to tax. This would cost about $5 billion a year.
- Reduced tax rates for married couples from widening the tax brackets and increasing the standard deduction for joint filers. The cost would be $30 billion a year.
- A huge capital gains tax cut. By excluding 50 percent of capital gains from taxation (on top of the current 30 percent exclusion for top bracket taxpayers) and by indexing gains for inflation, the Republicans would make about three-quarter[illegible] ll capital gains tax-exempt—a $25 [illegible] year tax-break mostly for the weal[illegible] taxpayers.
- Restoration of Individual [illegible] t Account tax breaks for upper [illegible] ople, with a long-term cost excee[illegible] ion a year.
- Elimination of all taxes on [illegible] te investments by allowing an i[illegible] tax writeoff. The cost would qu[illegible] nt to tens of billions of dollars annu[illegible] al far more as time goes by.

The total revenue losses of more than $120 billion a year would far more than wipe out the deficit-reducing benefits of the tax hikes adopted in Clinton's 1993 budget plan. How would the Republicans make up the losses? Unsurprisingly, an unnamed GOP congressional aide told BNA's Daily Tax Report that the Republican plan "will not be in the form of a fully funded, comprehensive package." In other words, this is election-year pandering, pure and simple.

Voters may or may not be gulled by the GOP promises this fall, but Clinton—who has said that he would still like to deliver on his 1992 campaign pledge of a middle-class tax reduction—may feel he has to match the Republicans' promises. If he tries, one GOP House aide told BNA, "the level [of the Republican middle-class tax cut plan] could increase to match or exceed any middle-class tax cut proposal President Clinton decides to offer." The GOP promises may not be paid for, they may violate all the budget rules; but they will put Clinton in a no-win situation.

Back in August 1981, when President Reagan and Ways and Means Chairman Dan Rostenkowski locked horns over tax cuts, their back-and-forth competition for congressional votes quickly got out of control. As Rostenkowski sadly learned, trying to out-Reagan Reagan was futile. In 1981, there was simply no tax cut—whether breaks for oil companies, utilities, railroads or real estate moguls—that Reagan and his supply-side-crazy Treasury Department wouldn't cheerfully match and graft onto their own already excessive plan.

It took the hard fight for the loophole-closing Tax Reform Act of 1986 to curb the tax shelters and abuses that the 1981 act created. And it took the bitter battle for Clinton's 1993 budget to bring taxes on higher-bracket taxpayers more in line with their ability to pay. The Republicans apparently think that they can attract voters once again by promising costless tax relief. Maybe so. But if you're one of those potential voters, keep in mind that unfunded tax reductions virtually guarantee higher taxes in the future. And when the two parties start trying to outdo one another in handing out tax breaks, in the end only the special interests really win.

Robert McIntyre is director of Citizens for Tax Justice.

GOP Congressional Primary Results Rattle Democrats

LOS ANGELES TIMES / WASHINGTON EDITION
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Confident Republicans Prepare for an Election Earthquake by Laying Out Alternatives to Clinton Agenda

WASHINGTON OUTLOOK

By Ronald Brownstein

Democrats in Washington are beginning to get the feeling that Southern Californians know well: the prickly chill in the bones on those hazy days when the cat is acting a little odd and the sky is suspiciously still.

The signs are just as numerous now that an earthquake is coming to Capitol Hill: Last summer, Republicans captured a Kentucky congressional seat that Democrats had held since the Civil War, President Clinton's approval rating remains anemic, and the fall primary results are rattling some of the Democrats' most prominent names.

All this points to substantial GOP gains in November. Republicans are so confident that they're getting an early start on laying out their agenda that on Tuesday House Republicans will gather more than 300 GOP incumbents and congressional challengers on the Capitol steps to offer the GOP plan—what they call a Contract with America. Senate Republicans issued a similar, slightly less sweeping, plan last week.

The House contract in particular is an ambitious effort to nationalize the 1994 campaign: It presents a list of internal congressional reforms and substantive legislative proposals that Republicans promise to bring to a vote within the first 100 days next year—if they win back the House. Even if the GOP falls short of outright control—still the probable outcome—incoming Republican leader Newt Gingrich of Georgia will spotlight these ideas as an alternative to Clinton.

As a policy blueprint, the contract is an odd mix of new-wave conservative thinking and Ronald Reagan nostalgia. On social policy, it has a '90s feel, emphasizing efforts to establish clear rules (such as time limits on welfare recipients and increased pressure on states to adopt "truth in sentencing" laws for prisoners) and taking tough stands against out-of-wedlock births and absent parents who do not pay child support.

On other issues, the agenda reaches back to the formula that elected Reagan: It promises lots of tax cuts and more defense spending. It even exhumes Reagan's call for a "Star Wars" missile defense to protect against "rogue nuclear states like North Korea."

As a political document, the contract sharpens the lines of partisan disagreement with a clarity likely to define the Gingrich era. And it denies Clinton one option for the next two years: accusing the Republicans of having no agenda but to frustrate his own.

But the Republican plan has two flaws that could undermine its effectiveness as anything more than a campaign bludgeon.

One is that it takes positions too conservative in some areas (such as welfare reform) for the three dozen or so House Republican moderates. That could threaten Gingrich's capacity to move these ideas even through a GOP-controlled House. In an interview, Rep. Michael N. Castle (R-Del.), who led the GOP moderates who negotiated the agreement to rescue the crime bill last month, stressed that he (and other moderates) had only committed to allowing a vote on the list: "It is not a guarantee of support," he insists.

The bigger problem with the GOP plan is that it isn't serious about reducing the deficit. It starts by endorsing the balanced budget amendment—and then promises to cut taxes for families with children, expand individual retirement accounts, reduce capital gains taxes, sweeten depreciation for business and repeal the increased taxes on Social Security benefits that Clinton's budget plan imposed. On top of that it would reopen the spigots at the Pentagon.

After some Republican legislators complained, the leadership said it would add to the list a promise to pay for its other promises with specific spending cuts. Rep. John R. Kasich (R-Ohio), one of Congress' most credible deficit hawks, says the cuts are available in the last two GOP alternative budgets, but the contract doesn't lock in the Republicans to supporting any specific cuts except for a few social welfare reductions. Even if the GOP can find the trims, that begs the larger question: Should those hard-won savings immediately be frittered away on tax cuts? Especially since the GOP needs to find another $750 billion in reductions over the next five years to fulfill its balanced budget promise, according to Congressional Budget Office projections.

Even before release of the House Republican plan, the White House and congressional Democrats strafed it. The GOP blueprint could provide a negative focus for the last two years of the Clinton Administration, particularly if the GOP actually wins back either chamber of Congress. "Absolutely, you could just run against Congress," one senior White House official says.

But that's a risky reelection strategy for a President who ran promising to break gridlock—and whose approval ratings only moved above water when he could demonstrate bipartisan cooperation on such issues as the North American Free Trade Agreement. Better for Clinton would be a competition with the Republicans for the mantle of reforming the way Washington does business.

W~~hat could a~~ Clintonite reform agenda look like? It could start with an intensified effort behind campaign finance and lobbying reform—initiatives that have been stalled all year in Congress and face uncertain fates in the session's last days.

It could continue with a renewed drive behind Clinton's reinventing government initiative—whose first year drew high marks from a Brookings Institution analysis that nonetheless warned the effort could still founder without "considerable creativity."

Next could come a commitment to bipartisan welfare reform. The GOP contract may go further than Republican moderates can stomach by requiring all states to cut off aid for recipients after five years on the rolls. That leaves Clinton the chance for a deal with the moderates—if he's willing to risk angering the left. "To get meaningful welfare reform done," Castle says, "they're going to have to go to the middle."

The linchpin of any Clinton reform agenda would have to be another assault on the deficit—a prospect that traumatizes some White House aides still nursing the bruises of 1993.

No President in a position as weak as Clinton can relish the prospect of butting heads with the deficit again. But nothing would declare Clinton's rejection of business as usual as forcefully as attacking wasteful federal subsidies to business (such as the $225 billion identified earlier this year by the Progressive Policy Institute) and imposing common-sense reforms—such as raising the Social Security retirement age and requiring greater income limits—on entitlement programs whose growth drives the budget deficit.

Focusing on a reform agenda would require Clinton to largely defer his goal of increasing public investment on social programs. The last budget fight taught that trying to increase spending while reducing the deficit muddies the message. (That logic also argues against entering a bidding war with the GOP on a middle-class tax cut.) And it could increase the risk of a primary challenge from Jesse Jackson in 1996.

But a Clinton reform agenda would offer a contrast with a GOP reaching back to the themes that elected Reagan. Pressed by reporters about the Reaganite tinge to the House GOP's Top 10 list, Gingrich last week said flatly: "If [the Administration] would be willing to go to a national debate . . . I'm willing to pit Reagan vs. Clinton—you choose." Clinton should take that challenge as inspiration to reinvigorate his own reform agenda, and then accept Gingrich's offer to debate whether the answers for the next decade can be found in the last.

Preview of the GOP Package

House Republicans' so-called Contract With America contains a series of internal congressional reforms and a package of 10 legislative initiatives. Details on some of the programs are still sketchy:

THE REFORMS WOULD . . .

- Force Congress to abide by the provisions of laws that it passes.
- Cut one out of three congressional committee staff members.
- Cut the congressional budget.

THE 10 LEGISLATIVE INITIATIVES INCLUDE . . .

- A congressional amendment requiring the President to submit a balanced budget and giving him line-item veto power.
- A reconsideration of the crime bill to limit death penalty appeals, transfer more money for prisons and federalize any crime committed with a gun.
- Welfare reform that would require states to cut off benefits for all recipients after five years, and discourage out of wedlock births.
- A $500-per-child tax credit for families with incomes up to $200,000 and expanded availability of individual retirement accounts.
- Tougher enforcement of child-support payments, anti-pornography laws.
- A restoration of defense spending reduced under President Clinton and an offer of full membership in the North American Treaty Organization for Central European nations such as Poland and Hungary.
- Allowing the elderly to earn more money without sacrificing Social Security benefits and repealing the Social Security tax increase approved as part of Clinton's economic plan in 1993.
- A cut in capital gains taxes and overall lessening of government regulation.
- Tort reform that would discourage "excessive legal claims, frivolous lawsuits and overzealous lawyers."
- Term limits for members of Congress.

Source: House Republican Conference

Los Angeles Times

Boston Globe 9.25.94

THOMAS OLIPHANT

GOP's fiscal shell game

WASHINGTON

Artifice, more than money, is the mother's milk of politics.

As a nation of multiple personalities – gullible and sensible, cynical and optimistic, irrational and confident, selfish and generous – we tolerate rhetorical baloney as essentially harmless, which it mostly is.

It's when artifice passes for genuine ideas that that we start buying Florida swamp land in the guise of retirement property. The country did that in 1980, to its continuing economic harm; and if House Speaker-to-be Newt Gingrich and Senate Majority Leader-to-be Bob Dole had their way, we'd do it all over again.

Ronald Reagan deserved to win the 1980 election, but his campaign raised artifice to the level of fantasy. Reagan offered goodies – huge tax cuts and gigantic military spending increases – that would have made the most profligate Democratic ward healer blush; and he blithely pledged it could all be financed by economic growth and painless budget surgery aimed at waste and fraud. The truth is that in his entire Presidency he never even made a single proposal that actually paid for his program; an omission compounded by George Bush; and most Democrats, to their eternal discredit, went along.

The result was an explosion of public debt from $1 trillion to $4 trillion, exhorbitant long-term interest rates, exported jobs, and stagnant incomes for working families.

Last week in a gathering of Senate Republican big shots and candidates, and this week in a similar affair to be staged by Gingrich, it is clear that a new horror movie, "The '80s II," is planned.

The cornerstone is a constitutional amendment requiring a balanced budget. This old chestnut is instructive, because it lays bare the artifice. It's not just that the amendment would have to await ratification by the states and then would not be law until five or seven years (depending on the specific proposal) after that.

More importantly, thanks to the Congressional Budget Office, we know what it would require: roughly $750 billion in program evisceration over five years, and $1.2 trillion over seven.

In an act of breathtaking irresponsibility, the Republicans' proposed "contract" with the public doesn't come within a country mile of those figures in the form of specific proposals. Worse, most of the ones they do offer (like a "spending commission" to make recommendations Congress could vote up or down but not change) don't belong in a serious discussion.

But there's more. The Gingrich-Dole crowd actually proposes to first make the problem worse with more than $150 billion in tax cuts, none of which would be of consequence to a typical family.

For example, the Gingrich crowd likes a $500 per child income tax credit, and the Dole bunch prefers doubling the $2500 dependent exemption. Neither would matter to families of average means and below, who pay little or no income taxes as it is. But for a $200,000 family the House GOP contract offer two grand in cash.

And on top of that, the party whose foreign policy is neo-isolationist has the nerve to demand an increase in military spending.

To pay for all this largesses AND balance the budget would require at least a 20 percent slash across the board in the domestic program budget – including Social Security, Medicare and crime. Exempt Social Security and the requirement jumps to 30 percent.

The sickest fact of all is that Gingrich et al could care less that their program is a joke. They're betting on an anti-government, anti-Clinton mood this fall. Their bogus contracts, however, constitute a hedge of that bet, an awareness that there is an impression that they have no genuine ideas of their own. As it turns out, they don't.

And that literal bankruptcy, in turn, provides an opening for counterattack.

The administration's experts, like anyone with a calculator, can eviscerate the Gingrich-Dole "ideas" substantively. Politically, however, they need a spokesman, which is why God created Vice Presidents.

Lousy leg and all, Al Gore needs to board Air Force Two and do to right-wing economic baloney for six weeks what he did to Ross Perot's opposition to NAFTA in one night. Artifice always works until those who know better confront it.

Thomas Oliphant is a Globe columnist.

Pennsylvania Avenue

By Morton M. Kondracke

The 'Third Wave' Is Coming, But It's Not In GOP's 'Contract'

House Republican Whip Newt Gingrich (Ga) and his intellectual allies are working on some fascinating 21st century ideas to reshape American politics for the Information Age. Unfortunately, few of them are apparent in the "Contract With America" that Gingrich and other House Republicans will unveil tomorrow.

Some of the proposals — expanded IRAs and tax incentives for adoptions, home care for the aged and work by seniors — are consistent with the theme of self-reliance inherent in Gingrich's nascent "progressive conservative" program to "renew American civilization."

In the main, though, the contract proposals are not at all futuristic, but rather warmed-over supply-side economic ideas from the 1980s.

At worst, they are cynical empty promises or demagogic appeals to anti-government passions of the moment, such as promises to hold votes on a balanced budget amendment (without saying how the budget would be balanced) and on term limits for Members of Congress, a bad idea that even many Republicans oppose.

The contract is a disappointment, given the depth of change Gingrich has in mind.

Gingrich is a soul mate of futurist Alvin Toffler, whose classic 1980 book, **The Third Wave**, forecast the dramatic shifts taking place as America moved from a factory-based industrial economy to a PC-based information economy. (The "First Wave" was the traditional agricultural economy wiped away by the industrial revolution.)

At worst, they are cynical empty promises or demagogic appeals to anti-government passions of the moment, like the balanced budget amendment and term limits.

Toffler's ideas are the basis for pioneering work going on at a new organization, the Progress and Freedom Foundation, headed by Gingrich associate Jeff Eisenach and soon to be joined by former Rep. Vin Weber (R-Minn), who will direct a project designed to develop a "Third Wave" political party, presumably out of the present GOP.

Toffler and Eisenach contend that the important political battles of the current era are not old-fashioned left-versus-right contests, but instead pit hierarchical, bureaucratic "Second Wave" corporate, social, and political interests against "Third Wave" interests anxious to break down old structures and build decentralized new ones.

But the House GOP contract to be unveiled on Tuesday — and a Senate version released last week — advocates giving "Second Wave" tax breaks to established interests. Defunding the federal government is implicit in the balanced budget proposal, but the contract contains few ideas for solving problems by non-federal means.

So while his allies say that Gingrich is a problem-solving "progressive conservative" whose hero is Theodore Roosevelt, the GOP contract is mainly a traditional-conservative document in the image of William McKinley or Robert A. Taft.

At a press conference along with Gingrich on Friday, Rep. Dick Armey (R-Texas) said that the contract merely forecast a "100-day shakedown cruise for the revolution to come," and Rep. John Kasich (R-Ohio) said that "we intend to reinvent the whole government" by eliminating whole departments, privatizing services, and handing responsibilities back to the states and cities.

Yet the contract itself contains only hints of the dramatic changes to come.

Toffler and his wife, Heidi, in a book published by Eisenach's foundation, criticize Democrats for "reflexive reliance on bureaucratic and centralist solutions to problems like the health insurance crisis...drawn straight from Second Wave theories of efficiency."

But while praising Republicans for favoring deregulation, privatization, free trade, and market economics, they rap Republicans for distributing tax breaks to old industries and appealing to "nostalgia in their rhetoric about culture and values."

Weber and Eisenach both dispute the Tofflers' modernist and secularist approach to values, contending that religion is part of the post-modern "Third Wave." More concretely, they want to find ways to bolster private "mediating institutions" — charities, churches, and community organizations — to do work now performed by government.

Eisenach wants to replace AFDC, for instance, with a full tax credit for contributions to private charity. It's a radical idea, but he says, "If you were poor and you're kid got badly burned, where would you rather have him treated, the Shriners' Burn Clinic or your local city hospital?"

Just as radically, Toffler and Eisenach talk of transferring major departments of government out of Washington, allowing Members of Congress to vote electronically from their districts, and holding interactive electronic town meetings followed by advisory plebiscites on various issues.

Besides Gingrich and his allies, other groups trying to reshape government for the new age include the Democratic Leadership Council and former Tennessee Gov. Lamar Alexander's (R) "New Promise of American Life" project at the Hudson Institute, which is designing models for decentralizing government out of Washington.

Gingrich and his House allies deserve credit for putting forward a positive program for the first 100 days of the 104th Congress. It's too bad they didn't tell voters what they have in mind for the long haul.

Political Surveyor
By Charles E. Cook

publican 'Contract' May Give Democrats Some Issues to Attack

With just six weeks until Election Day, it's hard to see how things could get much better for Congressional Republicans.

President Clinton's job ratings remain low, even after the Haiti incursion, and the latest Wirthlin Group poll shows that only 20 percent of Americans believe the country is headed in the right direction. Predictions that Republicans would be seen by voters as obstructionists haven't manifested themselves in any meaningful way. More specifically, Republicans don't seem to have suffered any backlash from their tactics in fighting either of Clinton's two most recent initiatives, health care reform and the crime bill.

GOP consultants and strategists who for years have toiled in the vineyards can hardly believe things are going so well.

years Congressional Republicans, par- y House Republicans, have reminded the Peanuts cartoon in which Lucy, holding the football for Charlie Brown to kick, jerks the ball out of the way just as Charlie approaches, sending him sailing and landing on his tailbone.

Every time Republicans have an opportunity to score, something happens that prevents them from reaching their potential. So far this year, that hasn't happened. This week, however, Republicans have another opportunity to fumble.

Months ago, when House Republicans started talking up a Sept. 27 rally on the Capitol steps for Congressional candidates to endorse and embrace a reform agenda, I thought it was a brilliant idea.

Republicans always seem to be enamored with the idea of nationalizing elections, and usually the effort is wasted. But this time it seemed to be a good idea.

I've always felt the old **Tip O'Neill** adage, "All politics is local," should have been amended to say, "All politics is local, except when it isn't."

Go tell a Democratic House or Senate can- e caught up in the maelstrom of 1980 or blican in 1974 or 1982 that all politics al. And in the last two election cycles, national trends seemed to have been more prevalent — resulting in lower re-election margins for some and tickets home for others.

There are at least two national dynamics at work this year: one working against incumbents, the other working against Democrats.

Republican gains have been inevitable for some time, but for the really big gains, say 35 or more seats in the House, seven or more in the Senate, the wall that protects incumbents has to come down.

This protective wall — the "I don't like Congress but I like my Congressman" feeling — has allowed incumbents to insulate themselves from institutional anger. It's been crumbling gradually in recent years, but it still exists.

My assumption was that House Republicans would try to build a reform framework around the fact that Democrats have ruled the House for 40 years. That's too long, they could argue, and if you're dissatisfied with government, the first place to change is the Democratic majority in the House.

By trying to nationalize the election with a "time for a change" message, Republicans could coalesce dissatisfied voters of all stripes.

Instead, though no specific plan has been unveiled yet, it appears the GOP agenda will be more specific than that, with a number of tax cuts, spending cuts, and defense increases that are strangely reminiscent of the early 1980s.

Just as their Senate counterparts did last week, House GOP candidates risk finally giving Democrats some issues to use against them. The brilliant thing about what Republicans have pulled off this year is that they have managed to stay on the offensive. Are they about to throw an interception?

> ***The brilliant thing about what Republicans have pulled off so far this year is that they have managed to stay on the offensive. Are they about to throw an interception?***

Though **Ronald Reagan** is remembered fondly by many voters as a president with a vision of where he wanted to take the country who turned public support into Congressional action on many domestic fronts, people also remember many of those policies as leading to mind-boggling deficits.

Democrats in recent days, sensing what Republicans are about to do, have kicked into overdrive.

They are beginning to emphasize the message that Republicans are back to their old tricks again, claiming that they will be able to cut taxes and increase defense spending without cutting entitlements, and that they'll be able to do all of this without worsening the deficit.

If, as rumored, Republicans propose a non-refundable $500 tax credit for families making under $200,000, that non-refundability, essentially eliminating the benefit of the credit for the struggling families who need it most, gives credence to Democratic arguments that all the GOP really wants to do is give breaks to the rich.

Simply put, Democrats, who have lacked a cohesive message all year, may be on the verge of getting one.

In card-playing as in politics, you should not overplay your hand. Republicans have played a perfect game this year, but they risk blowing a golden opportunity for historic gains.

Date: 09/26/94 Time: 18:57

US POLITICS: Clinton aides blast Republican tax cut, budget bills

Knight-Ridder

Washington--Sep 26--The Clinton administration today stepped up its attacks on a package of economic proposals that congressional Republicans would seek if they gain enough seats in the November elections to rule the House or Senate.

With the Republicans' package set to be unveiled formally Tuesday and with the 1994 congressional campaign season getting underway, the Democratic administration wasted no time in condemning the Republican plan.

White House Chief of Staff Leon Panetta, an ex-Republican, former congressman and former budget director, today called the package "a fraud," "flim-flam" and "warmed-over Reaganism of the 1980s."

Robert Rubin, head of President Bill Clinton's National Economic Council, labeled it "horrendous economic policy." He also predicted the long-term bond market would "react" to the Republican plan as "enormously high deficits" would boost interest rates and thereby "choke off" economic growth.

And Laura Tyson, head of the Council of Economic Advisers said the Republicans' call for a balanced budget constitutional amendment, higher defense spending, a series of tax cuts and some spending reductions is "Voodoo Two."

Tyson's characterization was in reference to the 1980 presidential campaign, when candidate George Bush coined the term "voodoo economics" in reference to candidate Ronald Reagan's economic plan for the country.

The Republicans' "Contract with America" would grant a 500-dlr-per-child tax credit, increase incentives for individual retirement accounts and, by some accounts, increase defense spending by some 61 billion dlrs over 5 years.

Meanwhile, 176 billion dlrs in savings would be achieved over the 5 years, through a range of "example" spending reductions. These "examples" include a 1.1-billion-dlr reduction in USDA's export credit guarantee program, Medicaid cuts and the elimination or privatization of several existing government agencies, including federal air traffic controllers.

But the Clinton administration contends the Republican plan would create at least an 800-billion-dlr revenue shortfall over 5 years that would not be offset under the plan. "It would nearly quadruple the national debt," Panetta said of the plan.

On Friday, congressional Republicans disputed the large revenue shortfall being claimed by the Clinton administration. But an aide to one of the lawmakers said spending cuts and other savings needed to achieve a balanced budget could be as much as 700 billion dlrs.

And Rep. John Kasich, R-Ohio, the senior Republican on the House Budget Committee, told reporters Friday, "Don't try to guess right now how we're going to get there." He said Republicans would rely "on some of the best business minds" to help shrink and privatize government and to achieve a balanced budget.

President Ronald Reagan took office in 1981 pledging to reduce deficits largely by reducing "waste, fraud and abuse" in government and creating an atmosphere for economic growth through investment.

But Panetta criticized the ambiguity of the Republicans' economic plan, saying the only way to make up for their budget shortfalls would be a "20-30 pct across-the-board cut" in mandatory federal programs, including Social Security and Medicaid. "They (Republicans) will not tell you that," Panetta added.

With congressional elections just 6 weeks away, Democrats are fearful of losing scores of House seats and a handful of Senate seats to Republicans.

Depending on the extent of those Democratic losses, Republicans conceivably could take control of either house of Congress, although the odds are long.

In berating the Republicans' plan in such a coordinated fashion, however, the Clinton administration may be worried that their legislation is exactly the type of measure needed to garner votes this fall: sort of a rerun of the 1980 Reagan landslide.

Rubin acknowledged it is "very hard" to have a national discussion of economic issues if "others are telling you (the electorate) you can have a free lunch."

If 1994 is anything like 1980, the Clinton administration will have a tough time convincing voters that tax cuts and a balanced budget amendment are things to vote against. End

By Richard Cowan, Knight-Ridder Financial News

Tel: (202) 383-6173

Date: 09/26/94 Time: 16:08

Democrats Say GOP's Numbers Add Up to Return of Reaganomics

WASHINGTON (AP)   Hoping to thwart a major Republican campaign offensive, the White House warned Monday the House GOP's platform was ``warmed over Reaganism'' that would loot Social Security and Medicare to shower tax cuts on the rich.

The White House attack came a day before more than 300 Republican House candidates, a mix of incumbents and challengers, were to gather on the Capitol steps to sign a ``Contract with America'' that pledges swift action on a 10-point agenda if voters give Republicans a House majority for the first time since 1954.

The contract promises votes early next year on congressional term limits, welfare reform, new anti-crime measures and an array of spending and economic initiatives, from a balanced budget amendment to tax cuts for capital gains and some families.

``This is a fraud and I think the American people need to know that,'' said White House chief of staff Leon Panetta. ``This is horrendous economic policy,'' added senior Clinton economic adviser Robert Rubin, who called the GOP policy a recipe to revive the huge deficits, higher interest rates and sluggish economic growth of the Bush administration.

To back up the White House push, the Democratic National Committee purchased time for radio ads in 20 markets with competitive House contests. The ads say the Republicans are promising ``more tax breaks for the rich, forcing devastating cuts in Medicare and Social Security. It's Republican politics as usual.''

Republicans labeled the White House presentation ``the big lie'' and suggested Democrats were panicked because they felt a Republican tide growing with just more than a month to go before the midterm elections. ``They have no agenda now because the American people rejected theirs, so all they can do now is whine and carp,'' said Ed Gillespie, the House Republican Conference spokesman.

But Republicans refused to say specifically where they would find the cuts to balance the budget, leaving them open to the White House assertion that the document was little more than a political gimmick.

In its pre-emptive strike, the White House focused solely on the spending and economic aspects of the GOP document, an area even many Republican strategists concede privately is open to criticism.

For example, a cost analysis prepared by House Republicans said there are ``no costs'' to passing a balanced budget amendment and line-item veto.

Labeling that assertion ``a flimflam,'' Panetta said it would take at least $743 billion in cuts to balance the budget within five years or $1.2 trillion to do it in seven years.

``Do they not have a responsibility then to tell us where they would find these cuts?'' Panetta said.

The Republicans' task would be even harder, because budget rules also require them to pay for the tax cuts promised in the contract, including $56 billion to reduce capital gains taxes and $6.5 billion to raise estate and gift tax exclusions   cuts the White House noted would go predominantly to the wealthy.

All told, Panetta said that balancing the budget and delivering the tax cuts would cost $1 trillion over five years, or $1.6 trillion over seven, and that Republicans had detailed proposed cuts that would cover only a sliver of that. To cover the rest, administration officials said Republicans would have to cut domestic spending across the board by 20 percent or more, and would have little choice but to slash Social Security and Medicare. ``That's where the money is,'' said Rubin.

``They are taxing Social Security and Medicare recipients to pay for tax cuts for the wealthy,'' said Panetta, who was House Budget Committee chairman before joining the administration.

Gillespie accused the White House of ``fear-mongering'' and said Republicans had promised no painful Social Security cuts. But he could not say exactly where the cuts would come from elsewhere in the budget, promising only that Republicans would find them if confronted with a constitutional amendment requiring a balanced budget.

``I can't tell you where all the cuts will come from,'' he said. ``I can tell you that it will compel some tough decisions to be made.''

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BC-USA-POLITICS-CONTRACT

Clinton aides scornful of Republican ``contract''

By Gene Gibbons

WASHINGTON (Reuter) - Top White House officials Monday ridiculed a Republican congressional campaign promise to pass a balanced budget amendment and cut taxes, saying it was either a political ploy or a formula for drastic cuts.

White House chief of staff Leon Panetta led the attack on the Republican ``Contract with America,'' which will be unveiled Tuesday in an elaborate ceremony at the Capitol featuring some 300 Republican legislators and challengers.

Aided by Robert Rubin, who chairs the National Economic Council and Rubin deputy Gene Sperling, Panetta -- a former government budget director -- challenged the key elements of the plan at a White House news briefing.

``This is fraud and I think the American people need to know that,'' Panetta said.

The Republican ``contract'' promises that if the opposition wrests control of the House of Representatives from President Clinton's Democrats in the mid-term elections, passage of a balanced budget amendment and a middle-class tax cut will be top priorities in the new Congress.

Thirty-five Senate seats, 36 governorships and all 435 House seats will be at stake Nov. 8. Republicans are expected to make sweeping gains and have a longshot chance of gaining a majority in one or both Houses of Congress.

``If they're going to be honest with the American people in terms of their proposal ... then there is a fundamental requirement that they tell us what programs are they going to cut in order to reach a balanced budget,'' Panetta said.

``That's what we would ask because if you look at it based on what they're not saying, then most of the cuts would have to come out of Medicare and Social Security.''

Panetta said that well over a trillion dollars in spending cuts would be needed to carry out the Republican plan, and that even after including all of their proposed cuts, there would be
a shortfall of more than $700 billion.

Rubin said the plan was a ``recipe to relive the same kind of environment'' of soaring deficits and a stagnant job market that prevailed in much of Republican George Bush's presidency.

The White House preemptive strike on the Republican plan was followed by a luncheon speech by Laura Tyson, chair of the president's Council of Economic Advisers, in which she referred to the ``Contract with America'' as ``Voodoo Two.''

Tyson was making an unflattering reference to the Reagan administration's ``supply side'' fiscal policy of the 1980's, a policy scorned by candidate George Bush as ``voodoo economics.''

REUTER

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NEC Staff Working Paper:

Preliminary Budget Analysis of House Republican's *Contract with America*

[Not for Distribution]

September 20, 1994

TABLE OF CONTENTS

INTRODUCTION

On September 27, 1994 the House Republican leadership will conduct a press conference in which House Republican incumbents and challengers will sign a specific contract committing themselves to passing certain legislation if the Republicans gain a working majority in the House of Representatives. This "Contract With America" would become their agenda for the first 100 days of the new Congressional session.

At this moment, there is no definitive and detailed list of the exact proposals that the House Republicans will put forward. However, Haley Barbour has stated that the contract will mostly consist of "existing proposals" and there have been several press accounts in which Republicans have laid out elements of their proposals. Therefore, we have based our analysis on proposals that House Republicans have previously offered, while using estimates when possible from the Congressional Budget Office, Joint Tax Committee, Office of Management and Budget, Treasury Department or one of the Congressional Budget Committees. To the degree that more details come out, we will revise this analysis.

While several of these proposals in isolation may have merit, our preliminary analysis suggests that the House Republican agenda as a whole is dramatically underfunded and would lead either to increasing deficits or austere cuts in virtually every spending category.

ONE-PAGE BUDGET SUMMARY OF HOUSE REPUBLICAN CONTRACT

1. TRILLION DOLLAR COSTS: On September 27, 1994, House Republicans will sign a list of promises that, together, would require unprecedented budgetary savings to achieve. They will commit to balancing the budget, while simultaneously enacting expensive new tax reductions and increasing some spending programs. First, the Republicans would need to find dramatic savings just to balance the budget by either 2000 or 2002 -- either $743 billion under a five-year deficit reduction plan (as in Republican Conference Chairman Armey's proposal) or $1.2 trillion under a seven-year deficit reduction plan (the path required by the Balanced Budget Amendment Act). Yet, in addition to the savings required to achieve a balanced budget, the House Republicans will propose $70 billion in increased defense spending and over $200 billion in new tax cuts over five years -- including marriage penalty changes ($72 billion), a child tax credit for families making up to $200,000, ($107 billion), and increased benefits to the top 13% of Social Security recipients ($21 billion). In net, the **Republicans will have to find additional budget savings of $1.0 trillion over five years or $1.7 trillion over seven years.**

2. TAX CUTS: REGRESSIVITY AND EXPLODING COSTS: The plan also includes three proposals that are designed to increase the federal deficit substantially in later years -- or to force additional cuts to pay for them. The rollover to backloaded IRAs, the capital gains tax cut, and the neutral cost recovery system are all specially designed to hide current costs and push out the deficit increases beyond the five-year budget window. Over 70% of the capital gains tax cut benefits go to Americans making over $100,000, while the neutral cost recovery system starts out artificially raising funds, but then costs $8 billion by the fifth year alone -- with dramatically increased costs thereafter.

3. FAILING THE SERIOUSNESS TEST: The House Republican "contract" appears not even to attempt to say how it would be paid for. As the Wall Street Journal reported on Friday, September 16, 1994, even Senate Republicans refused to sign on because, as one Republican Senator stated, "they are just blowing away money." The "contract" makes an iron-clad commitment to balance the budget yet rather than give details out as to what cuts (Medicare, Social Security, veterans) would be made, it instead offers hundreds of additional billions of dollars in new expenditures and tax cuts.

4. HOUSE ALTERNATIVE BUDGET FALLS HUNDREDS OF BILLIONS SHORT: The most specific plan House Republican plan to find savings for deficit reduction and tax cuts relied on severe and largely unrealistic spending cuts. Even it would still fall approximately $500-$700 billion short of what would be necessary to pay for the massive Republican "contract."

5. MEDICARE AND SOCIAL SECURITY: Any effort by the House Republicans to find the hundreds of billions of dollars of savings necessary to balance the budget, while paying for their additional spending and tax cuts without defense cuts or more taxes on well-off Americans would lead to dramatic cuts to Medicare or Social Security or both. Simply to balance the budget under their budget criteria would require a 17% cut across the board -- and over 20% when you add in their new spending and tax benefits. Entitlement cap proposals that focus on the rate of growth would have an ever harsher impact on Medicare. If Social Security were to be exempt from such savings, the impact on Medicare, fighting crime, education and training could be even greater.

The House Republican proposal starts with a commitment to find savings to balance the budget even though they "take off the table" areas like defense spending and taxes on the wealthiest Americans. Even if the House Republicans were to propose this and no additional items, they would need to come forth with a major deficit reduction plan far beyond what they have ever proposed. As their "contract" promises to find savings not only for balancing the budget but also for financing new spending and new tax cuts, they would need to find savings of over $1 trillion.

I. SAVINGS REQUIRED TO MEET BALANCED BUDGET PROPOSALS:

A: Seven-Year Path: There are two current proposals for a balanced budget that some House Republicans have signed on to. One is the Balanced Budget Amendment Act, which was amended to call for a balanced budget by the year 2002. This would phase in a balanced budget over seven years. If the deficit were reduced in equal increments, the necessary deficit reduction plan would call for a $1.2 trillion deficit reduction program over FY1996-FY2002. (See Table 3)

B: Armey's Five-Year Path: The second proposal, recently announced by Congressman Armey, would balance the budget by the year 2000. This would require a five-year deficit reduction plan. Again, assuming this was phased-in in equal increments, this would call for a $743 billion dollar deficit reduction plan over five years. (Both estimates use the current Congressional Budget Office baseline, see, "The Economic and Budget Outlook: An Update," CBO, August 1994, p.31)(See Table 4)

II. SAVINGS REQUIRED TO BOTH SATISFY BALANCED BUDGET AND ADDITIONAL REPUBLICAN PROPOSALS: In addition to the savings required to balance the budget, the House Republican leadership would need to find savings for the following proposals:

($ in billions)	1996-2000	1996-2002
1. Capital Gains Tax Cut	-10.2	-21.4
2. Gramm-Gingrich Indexing	-4.8	-10.0
3. $500 Tax Cut for Children	-107.0	-158.2
4. Defense Increases	-61.1	-98.1
5. Elimination of the Marriage Penalty	-72.7	-108.9
6. Long-Term Care Incentives	-1.5	-2.3
7. Modify Social Security Earnings Test	-11.8	-17.0
8. 85% Soc. Sec. Inclusion Repeal	-21.0	-31.4
9. Tax Incentives for Adoption	-0.2	-0.3
10. Expansion of IRAs	-6.2	-12.9
11. Neutral Cost Recovery	5.0	-11.0
12. Savings Needed for BBA	-743.0	-1,200.0
Total Cuts Needed	**-$1,034.5**	**-$1,671.5**

Table I

Projected Cost of House Republican Proposal: 7-Year Balanced Budget Plan

($ in billions) 07:27 AM 09/19/94

Proposal	Fiscal Year 1996	1997	1998	1999	2000	2001	2002	Total 1996-2002
1 Capital Gains Tax Cut	0.8	3.7	-3.4	-5.7	-5.6	-5.6	-5.6	-21.4
Source: JCT analysis of Bush Administration FY 1992 proposal.								
2 Gramm-Gingrich Indexing	0.5	-0.3	-0.9	-1.5	-2.6	-2.6	-2.6	-10.0
Source: JCT analysis conducted at time of proposal.								
3 $500 Tax Credit for Children	-4.7	-25.6	-25.6	-25.6	-25.6	-25.6	-25.6	-158.2
Source: House Budget Comm. report on FY 1995 Kasich Budget Proposal.								
4 Defense Increases (In Outlays)	-4.7	-9.6	-12.7	-15.6	-18.5	-18.5	-18.5	-98.1
Source: proposed in Rep. Kasich's FY 1995 budget alternative, which also increases budget authority by $73.7 billion over 5 years.								
5 Elimination of the Marriage Penalty	-7.2	-14.7	-15.8	-16.9	-18.1	-18.1	-18.1	-108.9
Source: JCT analysis conducted Sept. 16, 1994.								
6 Long-Term Care Incentives	-0.2	-0.3	-0.3	-0.3	-0.4	-0.4	-0.4	-2.3
Source: CBO analisys of Michel Health Care Bill, 1994.								
7 Modify Social Security Earnings Test	-1.6	-2.5	-2.5	-2.6	-2.6	-2.6	-2.6	-17.0
Source: OMB estimate.								
8 85% Soc. Sec. Inclusion Repeal	-1.7	-4.5	-4.7	-4.9	-5.2	-5.2	-5.2	-31.4
Source: Office of Tax Analysis, Dept. of Treasury, Sept. 16, 1994.								
9 Tax Incentives for Adoption	0.0	0.0	0.0	0.0	0.0	0.0	0.0	-0.3
Source: Office of Tax Analysis, Dept. of Treasury, Sept. 16, 1994.								
10 Expansion of IRAs	-0.2	0.8	-1.4	-2.0	-3.3	-3.3	-3.3	-12.9
Source: JCT estimate of H.R. 11 IRA proposal, Sept. 14, 1992.								
11 Neutral Cost Recovery	3.0	6.0	5.0	-1.0	-8.0	-8.0	-8.0	-11.0
Source: Senate Budget Comm. analysis of Kasich proposal.								
Sub-Total	-16.0	-47.0	-62.3	-76.0	-89.9	-89.9	-89.9	-471.5
12 Savings Necessary to Balance Budget by FY2002	-38.0	-78.0	-121.0	-166.0	-213.0	-265.0	-319.0	-1200.0
Source: CBO projection, Sept. 19, 1994								
TOTAL COST	**-54.0**	**-125.0**	**-183.3**	**-242.0**	**-302.9**	**-354.9**	**-408.9**	**-1671.5**

Table 2

Projected Cost of House Republican Proposal: 5-Year Balanced Budget Plan

($ in billions) 07:26 AM 09/19/94

Proposal	1996	1997	1998	1999	2000	Total 1996-2000
	Fiscal Year					
1 Capital Gains Tax Cut	0.8	3.7	-3.4	-5.7	-5.6	-10.2
Source: JCT analysis of Bush Administration FY 1992 proposal.						
2 Gramm-Gingrich Indexing	0.5	-0.3	-0.9	-1.5	-2.6	-4.8
Source: JCT analysis conducted at time of proposal.						
3 $500 Tax Credit for Children	-4.7	-25.6	-25.6	-25.6	-25.6	-107.0
Source: House Budget Comm. report on FY 1995 Kasich Budget Proposal.						
4 Defense Increases (In Outlays)	-4.7	-9.6	-12.7	-15.6	-18.5	-61.1
Source: proposed in Rep. Kasich's FY 1995 budget alternative, which also increases budget authority by $73.7 billion over 5 years.						
5 Elimination of the Marriage Penalty	-7.2	-14.7	-15.8	-16.9	-18.1	-72.7
Source: JCT analysis conducted Sept. 16, 1994.						
6 Long-Term Care Incentives	-0.2	-0.3	-0.3	-0.3	-0.4	-1.5
Source: CBO analysis of Michel Health Care Bill, 1994.						
7 Modify Social Security Earnings Test	-1.6	-2.5	-2.5	-2.6	-2.6	-11.8
Source: OMB estimate.						
8 85% Soc. Sec. Inclusion Repeal	-1.7	-4.5	-4.7	-4.9	-5.2	-21.0
Source: Office of Tax Analysis, Dept. of Treasury, Sept. 16, 1994.						
9 Tax Incentives for Adoption	0.0	0.0	0.0	0.0	0.0	-0.2
Source: Office of Tax Analysis, Dept. of Treasury, Sept. 16, 1994.						
10 Expansion of IRAs	-0.2	0.8	-1.4	-2.0	-3.3	-6.2
Source: JCT estimate of H.R. 11 IRA proposal, Sept. 14, 1992.						
11 Neutral Cost Recovery	3.0	6.0	5.0	-1.0	-8.0	5.0
Source: Senate Budget Comm. analysis of Kasich proposal.						
Sub-Total	-16.0	-47.0	-62.3	-76.0	-89.9	-291.5
12 Savings Necessary to Balance Budget by FY2000	-46.0	-94.0	-146.0	-200.0	-257.0	-743.0
Source: CBO projection of 5-yr. balanced budget path, Sept. 19, 1994. Rep. Armey calls for a balanced budget by FY 2000.						
TOTAL COST	**-62.0**	**-141.0**	**-208.3**	**-276.0**	**-346.9**	**-1034.5**

ANALYSIS OF LIKELY PROPOSALS IN HOUSE REPUBLICAN CONTRACT

At this moment, there is no definitive and detailed list of the exact proposals that House Republicans will put forward on September 27, 1994 as part of their "Contract." Since they have not yet given out the details of their proposals, we can only take Haley Barbour at his word that the "Contract" will mostly consist of "existing proposals." Therefore, we have estimated costs based on past House Republican proposals, while using estimates when possible from the Congressional Budget Office, Joint Tax Committee, Office of Management and Budget, Treasury Department or one of the Congressional Budget Committees. To the degree that more details come out, we will revise our analysis.

1. LACK OF DETAIL AS TO WHERE THE SAVINGS WILL COME FOR BALANCING THE BUDGET AND ADDITIONAL PROPOSALS: The House Republican "contract" does not attempt to propose financing sources. As the Wall Street Journal reported on Friday, September 16, 1994, even Senate Republicans refused to sign on because as one Republican Senator stated, "they are just blowing away money." This characterization is understandable. First the "Contract" makes an iron-clad commitment to balance the budget -- presumably by 2002 as the balanced budget amendment requires, but possibly by the year 2000 as proposed recently by Republican Conference Chairman Armey. Whatever one's view of this Amendment, it would unquestionably require a deficit reduction plan of either $743 billion over five years or $1.2 trillion over seven years. Yet, rather than give details out for the first time as to what cuts (Medicare, Social Security, veterans) would be made, the "Contract" instead offers additional hundreds of billions of dollars in new spending and tax cuts, that would all have to be paid for in addition to the savings that would have to be found to balance the budget by 2000 or 2002. *Yet, it is still unclear whether the Contract will include agreement on any specific means as to how to find the trillion dollars needed to meet their tax cut, spending increases and deficit reduction pledges.*

2. ESTIMATED COST IN EXCESS OF ONE TRILLION DOLLARS: Under almost any estimates, it seems clear that the essential promise, to balance the budget by the year 2000 (Armey) or 2002 (Balanced Budget Amendment of 1993) ***plus*** increase defense spending ***plus*** provide several tax cuts, would require savings beyond anything that any member of the Republican House Leadership has ever presented. In order to just balance the budget, the Republicans must find $743 billion in savings over five years or $1.2 trillion over 7 years. In addition, they must find additional five-year savings to pay for increased defense spending ($61 billion), marriage penalty changes ($72 billion), a child tax credit for families making up to $200,000, ($107 billion), and increased benefits to the top 13% of Social Security recipients ($21 billion).

- **Five-Year Costs -- $1.034 Trillion:** The savings they would need to find to achieve their contract goals in the first five years (in accordance with the Armey balanced budget proposal) would be $1.047 trillion. (See Table 2)

- **Seven-Year Costs -- $1.67 Trillion:** If the Republican Contract assumes that they will balance the budget by the year 2002 -- a seven-year plan -- the burden will be even greater. This is partly because trends in the deficit require a $1.2 trillion deficit reduction plan just to balance the budget over 7 years (without any new tax cuts), and partly because the costs of the core of their tax cuts (rollovers to backloaded IRAs, capital gains reductions, neutral cost recovery) explode in the out-years --just as they were planning to get the budget in balance. (See Table 1)

3. TAX CUTS: REGRESSIVITY AND EXPLODING COSTS: Other than the child tax credit, they will include three proposals (rollovers to backloaded IRAs, capital gains tax cut, and neutral cost recovery) in which the benefits go disproportionately to the well-off. Each of these 3 proposals relies on gimmicks to push significant costs into the out-years -- beyond the five-year budget scorekeeping window in the House of Representatives. This budget gimmickry contradicts the goal of a balanced budget, since it creates out-year deficit increases that the Republicans have never said how they would overcome.

A. Examples of Regressivity:

- **Capital Gains:** The Joint Tax Committee (1992) has found that over 70% of the gains of a capital gains tax cut would go to Americans making over $100,000 and over 50% would go to the top 1% of Americans -- those making over $200,000.

- **Unnecessary Inequity in Child Tax Credit Proposal:** Even if the Republicans were able to pay for their $500 per child tax credit, their proposals would give significant tax cuts to the top 1-2% of Americans, while denying working poor families even a penny. Under the previous child tax credit proposal, a family of four making $150,000 would get a $1000 tax break while a family of four making $20,000 would get not a single penny since the tax credit is not refundable.

- **Opposition to 1992 and 1993 Budget Proposals:** In 1992, 99% of Republicans voted against a child tax credit and an expanded IRA simply because the program also included a tax increase on the top 1.2% of earners. In 1993, 100% of Republicans voted against a budget with a dramatic expansion of the Earned Income Tax Credit for 15 million working families largely, again, because of tax increases on the top 1.2% -- those making over $180,000 adjusted gross income.

B. Examples of Exploding Costs:

- **Rollovers to Backloaded IRAs:** One proposal is a rollover to "backloaded IRAs." This proposal hides the true costs in the first few years, by allowing only after-tax income to be put in these IRAs, and then making all interest income tax free -- forever. The cost of this proposal will grow to $8 billion a year (or more in out-years) according to previous Joint Tax Committee estimates -- just as the deficit is projected to rise.

- **Neutral Cost Recovery System:** This provision gives huge new depreciation tax cuts that increase each year, so that the main costs fall outside of the five-year period for which cost estimates are required in the House of Representatives. These gimmicks are objectionable not only because they are deceptive to the American people in terms of whether they are fully financed, but also because they directly contradict the goals of a balanced budget, as the rising costs will add to the deficit in the out-years -- where the Congressional Budget Office and OMB now see growing deficit increases as a percentage of GDP. Indeed, even by the fifth year of the proposal, the effect of the neutral cost recovery will change from gaining revenue to losing $8 billion a year, with increasing costs thereafter.

4. MOST AGGRESSIVE REPUBLICAN SAVINGS PLAN FALLS APPROXIMATELY ***$500-$700 BILLION SHORT:*** The most specific House Republican plan to find savings for deficit reduction and tax cuts relies on severe and largely unrealistic spending cuts, yet would still fall $500-$700 billion short of what would be necessary to pay for the massive Republican "contract." The House Republican alternative budget in 1994 (sponsored by Rep. Kasich) sought to pay for tax cuts and additional deficit reduction through spending cuts that were often double counts, unrealistic or called for unjustified reductions in investment programs. The Republican plan included double counting up to $50 billion in overhead and personnel reductions that are already in the President's budget, a $45 billion cut in Medicare, a $30 billion cut in health care, a $53 billion cut in education and training including cuts in college loans ($10 billion), and job training ($10 billion), a $57 billion cut in transportation and infrastructure ($18 billion coming from selling the Air Traffic Control Corporation), and $24 billion in natural resources and environmental programs. The Republican budget also calls for cuts in criminal justice of $21 billion -- which would not allow for the new cops and prison funding in the crime bill. This still leaves over a $500-$700 billion shortfall in the five-year plan, and an even greater shortfall over seven years because of the projected increase in the deficit and because the costs of several House Republican proposals explode after the first few years.

- **Entitlement Cut and Entitlement Caps:** The Kasich plan would have cut entitlements by $101 billion over five years, including a $10 billion cut in agriculture, a $10 billion reduction in student loans, and a $45 billion Medicare reduction. An entitlement cap proposal that cuts $200 billion would likely add only $100 billion in savings after double counting is removed.

- **Double Counting:** The Kasich proposal included provisions such as some personnel and overhead reductions, procurement savings and defense cuts that are already part of the Clinton budget.

5. IMPACT ON SENIORS: The Republican proposal seeks to mask the likely impact it would have on seniors -- either through cuts in Medicare or Social Security. On its face, the House Republican proposal increases spending by $21 billion on Social Security for the top 13% of recipients and another $12 billion on seniors who are still working -- again with most of the benefits going to the most well-off recipients. Yet, if the House Republican were serious about paying for their plan while taking off the table taxes on the well-off and defense, there would be little choice but to call for severe cuts to Medicare or Social Security -- or both.

- **1994 Republican House Alternative:** In the 1994 Kasich proposal, there were $75 billion in cuts to health care -- including an additional $45 billion in Medicare cuts. Yet, the real threat to Medicare is that it seems to be the only viable target for paying for the Republican proposals. As the Republicans are opposed to any tax increases on the wealthiest Americans, and call for defense increases, their main vehicles for spending cuts would have to be Medicare or Social Security.

- **Entitlement Caps:** Armey, among others, has called for entitlement caps that would freeze spending on entitlements per beneficiary at approximately the rate of inflation. Whatever the merits of such a proposal, the clear fact is that such proposals represent plans to dramatically cut Medicare costs. For example, a proposal similar to Armey's would lead to $163 billion in Medicare cuts over five years.

- **Seniors Are the Main Primary Possible Target:** If the budget must be balanced under the Republican criteria, with no cuts in defense and no tax increases on the well-off, there is simply no choice but to call for major cuts in either Medicare or Social Security or both -- anywhere from 24%-33% of their budgets in the year 2002. These are the dramatic reductions in assistance for seniors that would be required to balance the budget and pay for the tax cuts and spending increases that are called for by the Republican contract.

6. FISCAL CYNICISM: The House Republican contract resorts to the type of fiscal cynicism and gimmickry that led to the escalation of the deficit when the Republicans controlled the White House and the Senate between 1981 and 1986. First, at the same time the Republicans talk about "means testing" entitlements and the need for tough choices, they seek to repeal over $20 billion in deficit savings by eliminating the provision that requires the top 13% of Social Security recipients to count a higher percentage of their Social Security benefits as taxable income. Second, as mentioned above, they have three tax cuts which are specifically designed to do exactly what deficit reduction efforts are supposed to alleviate -- pushing costs out to the future to avoid fiscal responsibility today. The rollovers to backloaded IRAs, the neutral cost recovery system and many forms of the capital gains tax cut are specifically designed to mislead the American people as to their true costs by pushing the costs beyond the budget window. The reply from the Republicans who are advocating them is familiar: tax cuts will raise funds, the same fiscal logic that led to exploding deficits when the Republicans controlled the White House.

IMPACT ON SENIORS

The Republican House alternative budget requires close to a trillion dollars in savings over the next five years. It is difficult to understand how they would finance this significant number. Yet, as they have consistently taken off the table both defense (where they call for significant increases) and tax increases on the most well-off Americans, both past history and basic budget logic imply that the major impact would have to be on Medicare or Social Security.

The CBO baseline for FY 2000, breaks up the non-interest part of the budget into the following categories:

	FY2000
Domestic Discretionary	292
Defense	292
Social Security	430
Medicare	290
Medicaid	168
Civil Service and Military Retirement	83
Other Entitlements	213
TOTAL	1768
AVAILABLE SAVINGS SOURCES EXCLUDING DEFENSE	1476
AVAILABLE SAVINGS SOURCES EXCLUDING DEFENSE AND SOCIAL SECURITY	1046

It is first important to note that of the $1.476 billion in federal spending available for reduction under the House Republican alternative, nearly half -- or $720 billion -- is in either Social Security or Medicare. Therefore, it seems unavoidable that they would be major targets for paying for the House Republican "contract." Consider the following:

The deficit for the year 2000 is now projected to be $257 billion. With the addition of the Republican tax cuts and spending increases, the deficit would be $90 billion greater. Thus, the amount of saving needed to balance the budget in the year 2000 would be $347 billion. Even if one assumed $47 billion in interest savings, that would still mean finding $300 billion of savings. Out of the $1.476 trillion of spending available, that would mean a 20% reduction in spending across the board -- including Social Security, Medicare, criminal justice etc. If Social Security were also exempted, ***it would require a near 30% reduction in spending across-the-board.*** While not every program would have to be cut 30%, every additional program that is exempted would require more severe cuts on the remaining programs.

- TABLE 3: DEFICIT REDUCTION NECESSARY TO BALANCE THE BUDGET BY FY 2002
- TABLE 4: DEFICIT REDUCTION NECESSARY TO BALANCE THE BUDGET BY FY 2000

Table 3

Deficit Reduction Necessary to Balance the Budget by FY 2002

($ in billions)

07:27 AM 09/19/94

	Fiscal Year							7-Year
	1996	1997	1998	1999	2000	2001	2002	Total
CBO Baseline Deficit	176	193	197	231	257	287	319	
New Deficit	138	115	76	65	44	22	0	
Deficit Reduction	**-38**	**-78**	**-121**	**-166**	**-213**	**-265**	**-319**	**-1200**

Source: Congressional Budget Office

Note: Projections assume deficit reduction plan of equal increments through FY 2002.The above scenario represents only one of innumerable possible paths that would lead to a balanced budget. The exact path depends on when the deficit reduction begins and the specific policies adopted by Congress and the President. This particular path has a longer time frame for phasing in policies than have previously enacted deficit reduction plans.

Table 4
Deficit Reduction Necessary to Balance the Budget by FY 2000
($ in billion)

07:28 AM 09/19/94

	Fiscal Year					5-Year
	1996	1997	1998	1999	2000	Total
CBO Baseline Deficit	176	193	197	231	257	
New Deficit	130	99	51	31	0	
Deficit Reduction	**-46**	**-94**	**-146**	**-200**	**-257**	**-743**

Source: Congressional Budget Office

Note: Projections assume deficit reduction plan of equal increments through FY 2000.The above scenario represents only one of innumerable possible paths that would lead to a balanced budget. The exact path depends on when the deficit reduction begins and the specific policies adopted by Congress and the President. This particular path has a longer time frame for phasing in policies than have previously enacted deficit reduction plans.

APPENDIX
ANALYSIS OF ANTICIPATED BUDGETARY PROPOSALS

- CAPITAL GAINS TAX CUT
- INDEXING CAPITAL GAINS
- CHILDREN'S $500 TAX CREDIT FOR FAMILIES UNDER $200,000
- ELIMINATION OF THE MARRIAGE PENALTY
- MODIFY THE SOCIAL SECURITY EARNINGS TEST
- REPEAL THE 85 PERCENT MAXIMUM INCLUSION RATE FOR SOCIAL SECURITY BENEFITS
- EXPANDED INDIVIDUAL RETIREMENT ACCOUNTS
- NEUTRAL COST RECOVERY SYSTEM

CAPITAL GAINS TAX CUT

Current Law

Under current law, long-term capital gains are fully included in adjusted gross income. Taxpayers in the 15 and 28 percent brackets therefore pay the same tax rates on capital gains as on other income. Long-term capital gains rates are capped at 28 percent, so taxpayers in the 31 percent and higher tax brackets pay a lower rate on long-term capital gains than on other income. The rate cap was instituted in OBRA-90 and retained in OBRA-93. Under pre-Tax Reform Act of 1986 law, taxpayers were permitted to exclude 60 percent of the excess of long-term gains over short-term losses. Thus the maximum tax rate on long-term capital gains was 20 percent (40 percent of the 50 percent top income tax rate).

Proposals

Republican proposals on capital gains are likely to take one of several basic forms:

1. BUSH/WALKER PROPOSALS: H.R. 1450 (introduced by Rep. Walker on March 23, 1993) provides a 10 percent exclusion for assets held between one and two years and an additional 10 percent exclusion each year the asset is held beyond two years, with a 100 percent exclusion for assets held ten years or more. The Bush Administration made two such proposals for which JCT revenue estimates are given below. The FY 1992 Budget proposal would have allowed a 15 percent exclusion for assets held between one and two years, a 25 percent exclusion for assets held between two and three years, and a 35 percent exclusion for assets held three years or more. The FY 1993 Budget proposal was similar, except the exclusions were 15 percent, 30 percent, and 45 percent.

	1992	1993	1994	1995	1996	1992-96
			(Billions of dollars)			
FY 1993 Budget Proposal	0.8	3.7	-3.4	-5.7	-5.6	-10.2

2. 50% EXCLUSION: Exclude 50% of capital gains income from taxation, which would have the effect of halving the tax rate individuals pay on capital gains. For example, a 50 percent exclusion would reduce the maximum capital gains tax rate to 14 percent (50 percent of 28 percent) and taxpayers in the 15 percent bracket would be subject to a 7.5 percent rate.

3. ARCHER PROPOSALS: H.R. 3739, introduced by Rep. Archer January 26, 1994 would exclude some percentage of long-term gains, but repeal the 28 percent rate cap. A 50 percent exclusion (e.g.,) would reduce the maximum capital gains tax rate to 19.8 percent (50 percent of 39.6 percent) and taxpayers in the 15 percent bracket would be subject to a 7.5 percent rate. Rep. Archer also introduced legislation (on January 5, 1993), H.R. 53, which provides a 30% exclusion.

4. CRANE/DREIER/GRAMS PROPOSALS TO REDUCE THE RATE TO 15% Reduce the rate cap to 15 percent. This would reduce the maximum tax rate to 15 percent. H.R. 151 (introduced by Rep. Crane January 3, 1993), H.R. 1855 (introduced by Rep. Dreier April 28, 1993), H.R. 2424 (introduced by Rep. Grams June 16, 1993), and H.R. 3645 (introduced by Rep. Grams November 22, 1993) all provide a maximum rate of 15 percent, with a 7.5 percent rate for gains in the 15 percent bracket. (These bills also all index gains for inflation.)

DISTRIBUTION:

Over the past few years, the Joint Tax Committee has been asked on numerous occasions to estimate the distributional effects of reducing the capital gains tax. On all occasions, it has been found to go disproportionately to the highest income brackets. The JCT found that under the most recent major Republican proposal, President Bush's 1992 proposal, 70% of the benefits went to taxpayers making over $100,000 and 52.5% of the benefits went to those in the top 1% making over $200,000.

	Distribution of Aggregate Tax Change
Less than $10,000	0.2%
$10,000-$20,000	0.5%
$20,000-$30,000	1.6%
$30,000-$40,000	3.6%
$40,000-$50,000	4.5%
$50,000-$75,000	11.1%
$75,000-$100,000	8.6%
$100,000-$200,000	17.4%
$200,000 and over	52.5%
TOTAL	100%

JOINT TAX COMMITTEE (Estimate of Bush Administration's Capital Gains Proposal, February 3, 1992)

INDEXING CAPITAL GAINS

Index capital gains for inflation (e.g., H.R. 48, introduced by Rep. Archer on January 5, 1993 and the bills listed in point 4 of the Capital gains Tax Cut section). Taxpayers would increase the basis (cost) of their assets to adjust for inflation since the asset was purchased. Variations of this proposal would index capital gains only for inflation after some future date or add indexing to one of the exclusion proposals. S. 1829 (introduced by Sen. Hatch on February 4, 1994) indexes gains for inflation and provides an annual exclusion of $100,000 (joint) and $50,000 (single). JCT revenue estimates for a 1991 Gramm-Gingrich prospective indexing proposal are shown below. Estimates for prospective indexing can hide cost increases in the out-years.

Revenue Estimates

	1992	1993	1994	1995	1996	1992-96
		(Billions of dollars)				
Gramm-Gingrich Indexing Proposal (JCT, September 23, 1991)	0.5	-0.3	-0.9	-1.5	-2.6	-4.8

CHILDRENS' $500 TAX CREDIT FOR FAMILIES UNDER $200,000

Kasich Proposal: In the House Republican alternative, Congressman Kasich proposed a $500 per child tax credit for families making under $200,000 that he himself estimated would cost $107 billion over five years.

Grams Proposal: Rep. Grams proposed a $500 per child tax credit (H.R. 2434, June 16, 1993, and H.R. 3645, November 22, 1993) that would make the credit non-refundable, have no income phaseout, and index the $500 amount, but would apply to children 17 and under.

Revenue Estimates

The following revenue estimates assume an effective date of January 1, 1995.

Kasich Proposal: Kasich estimates his own proposal to cost $107 billion over five years, with an average cost per full year of over $25 billion. (Source: "The Republican Budget Initiative For Fiscal Year 1995," House Budget Committee Republican Caucus, March 3, 1994)

Grams Proposal: The estimate below assumes the credit applies to all children 18 and under. Grams' proposal may call for the credit to apply only to 17-year-olds and under, and might, therefore, have slightly lower costs.

	Fiscal Year					
	1995	1996	1997	1998	1999	1995-99
	(Billions of dollars)					
$500 Per Child Tax Credit (Office of Tax Policy, Treasury Department, 1994)	-12.4	-25.2	-26.9	-16.9	-27.5	-118.1

Analysis

Unnecessary Inequity: Because the proposed child tax credit is available for families making up to $200,000 and because it denies any refundability to families with low tax burdens, the proposal would lead to serious inequities to some working families. For example, a family with two children making $150,000 would get a tax cut of $1000. Yet, a similar family of four making $20,000 would get no tax benefit whatsoever because they would not have taxable income to offset.

House Republicans Opposed a Child Tax Credit in 1992 and 1993:
In 1992, 99% of Republicans voted against a child tax credit and an expanded IRA simply because the program also included a tax increase on the top 1.2%. In 1993, 100% of Republicans voted against a budget with a dramatic expansion of the Earned Income Tax Credit largely, again, because of tax increases on the top 1.2% -- those making over $180,000 adjusted gross income.

ELIMINATION OF THE MARRIAGE PENALTY

Current Law

Under U. S. tax law, getting married can affect a couple's tax liability, both positively ("marriage bonus") and negatively ("marriage penalty").

Proposal

1) Representative Istook Proposal: On February 10, 1994, Rep. Istook (R–OK) introduced HR 3851, to amend the Internal Revenue Code of 1986, eliminating "marriage penalties." Under this proposal, spouses would have the option to file using the tax status they would have had if they had not been married, and to allocate income and deductions between them as if they had not been married.

The bill has been referred to the House Ways and Means Committee and is awaiting further action.

Revenue Estimate

~~Below are estimates revenue estimates made by~~
~~In a September 16, 1994 letter to Representative Gephardt,~~ The Joint Committee on Taxation analyzed the cost of eliminating the marriage penalty, using guidelines similar to the Istook bill. ~~The new~~ (September 16, 1994). ~~The revenue~~

	Fiscal Year					
	1995	1996	1997	1998	1999	1995–99
	(Billions of Dollars)					
Lost Federal Revenue (JCT, ~~September 16~~, 1994)	–7.2	–14.7	–15.8	–16.9	–18.1	–72.7

Analysis

Removing or reducing marriage tax penalties would reduce tax revenues by a very substantial amount. In addition to the lost government revenue, the Istook plan would also create incentives for couples to "game" the tax system and manipulate their unearned income, which would complicate the tax filing process and give some couples an unfair advantage over others.

Married couples would manipulate their unearned income by moving ownership of assets to the spouse facing the lower tax rate. This would enable couples with significant unearned income to reduce their taxes, whereas other married couples with the same total income (but through only salary and wages) could be forced to pay a higher effective tax rate.

MODIFY THE SOCIAL SECURITY EARNINGS TEST

Current Law

Retired workers between the ages of 65 and 69 have their social security benefits reduced by 33 and 1/3 cents for each dollar of earnings over $11,160. Above age 69, persons receive full social security benefits, regardless of their earnings. The earnings test is lower for younger beneficiaries. They can earn up to $8,040 before benefits are reduced, and they are subject to a 50 percent benefit reduction. The earnings test thresholds are adjusted for inflation each year.

Proposals

1) Older Americans Freedom to Work Act of 1993: On January 5, 1993, Rep. Hastert (R–IL) introduced HR 300, which would eliminate the Social Security earnings test altogether. The bill has been referred to the Ways and Means Committee where it is awaiting action.

Budgetary Estimate

The following are OMB estimates.

	Fiscal Year (Billions of dollars)					
	1995	1996	1997	1998	1999	1995–99
Eliminating Earnings Test	–3.2	–4.8	–4.9	–5.0	–5.0	–22.9

2) It has also been proposed that the amount of allowable earnings for social security recipients, age 65 through 69, be increased to $30,000.

Budgetary Estimate

	Fiscal Year (Billions of dollars)					
	1995	1996	1997	1998	1999	1995–99
$30,000 Earnings Test OMB estimate	–1.6	–2.5	–2.5	–2.6	–2.6	–11.8

3) Another alternative would phase the increase to $30,000 in over five years.

Budgetary Estimate

	Fiscal Year					
	1995	1996	1997	1998	1999	1995-99
	(Billions of dollars)					
Five-Year Phase-in of $30,000 Earnings Test OMB estimate	-0.3	-0.9	-1.4	-1.9	-2.3	-6.8

Analysis

This proposal is extremely regressive -- the vast majority of the benefits would go to high-income seniors.

Most retired workers between the ages of 65 and 69 would not benefit from these proposals. Of the 8 million persons in this age group who are covered by social security, 75% -- 6 million -- did not work at any time in 1989. Their decisions to retire were based on many factors in addition to the social security earnings test: health, leisure time, savings, pension income, the size of social security benefits, and employers' demand for elderly workers. For these same reasons, they are unlikely to seek employment once retired, even if the earnings test were raised.

Among those who currently work, many would likely not increase their work effort further in response to changes in the earnings test. Either they currently earn far less than the exempt amount (and would be unaffected by the change) or they earn too much to receive benefits even if the earnings test threshold were increased to $30,000. As the earnings test thresholds are increased, some retired workers, who currently earn too much to qualify for benefits, and their families would become eligible to receive benefits. Receipt of this windfall may cause some of these higher wage workers to reduce their work hours.

REPEAL THE 85 PERCENT MAXIMUM INCLUSION RATE FOR SOCIAL SECURITY BENEFITS

Current Law

Taxpayers with sufficient income must include some of their Social Security benefits in income subject to income tax. Taxpayers with incomes under the first threshold ($25,000 for single taxpayers and $32,000 for married taxpayers, filing jointly) do not include any of their social security benefits in AGI. Those with incomes between the first and second thresholds ($34,000 for single taxpayers and $44,000 for married taxpayers, filing jointly) include up to 50 percent of their Social Security benefits above the threshold in AGI. Finally, those with incomes over the second threshold include up to 85 percent of benefits above the second threshold in AGI, and 50% of their benefits between the first and second thresholds.

Proposals

H.R. 2959, introduced on August 6, 1993 by Rep. Kyl (R-AZ), would replace the 85% maximum inclusion rate with a maximum marginal rate of 50%. On September 28, 1993, Rep. Smith (R-NJ) introduced similar legislation (H.R. 3155). Both bills have been referred to the House Ways and Means Committee.

Revenue Estimates

			Fiscal Year			
	1995	1996	1997	1998	1999	1995-99
			(Billions of dollars)			
Repeal 85% SS Inclusion Rate Office of Tax Analysis, Department of Treasury	-1.7	-4.5	-4.7	-4.9	-5.2	-21.0

Analysis

This proposal would benefit only the highest earning social security recipients. Social security recipients who are in greatest need of income supplements - those who receive less than $25,000 - receive no benefit at all. Instead, wealthier recipients will retain additional money from the Social Security trust fund, potentially at the expense of those who need it most.

Since the revenue from taxation of Social Security benefits is entirely returned to the Social Security and Medicare trust funds from which the benefits were paid, such taxation provides needed revenues for the trust funds and reduces the need for future increases in payroll taxes (which would be particularly burdensome for lower income, younger workers). Moreover, the 85% inclusion rate does not adversely affect lower and middle income retirees. ~~In fact, it may help such retirees by reducing the need to curb future benefit cost-of-living increases.~~

EXPANDED INDIVIDUAL RETIREMENT ACCOUNTS

Current Law

Taxpayers are allowed to deduct up to $2,000 (or earned income, if less) contributed to an IRA if (regardless of income) they are not active participants in an employer-sponsored pension plan (and their spouses are not active participants), or if their AGI is less than $40,000 (joint) or $25,000 (single). The deduction for active participants is phased out over $10,000 of AGI above the income thresholds (e.g., between $40,000 and $50,000 of AGI on joint returns). These income limits were added by the Tax Reform Act of 1986 (TRA). Nonworking spouses may contribute $250 to an IRA. Taxpayers not eligible to make deductible IRA contributions can make nondeductible contributions (subject to the same dollar limits). Earnings on IRA contributions are not taxed currently. Distributions from IRAs are subject to income tax. A additional 10 percent penalty is imposed on IRA distributions made before age 59 1/2.

Proposals: There have been several proposals to expand eligibility for IRAs, to make them more generous, and to allow greater flexibility for penalty withdrawal for uses other than retirement.

Restore Pre-TRA IRAs. All taxpayers would be allowed to make deductible contributions to an IRA under the pre-Tax Reform Act of 1986 (TRA) rules. Nondeductible IRAs would be repealed. H.R. 1885, introduced by Rep. Dreier on April 28, 1993 would restore pre-TRA IRAs, but also double the contribution limit (to $4,000) and index it for inflation, and allow penalty-free early withdrawals for first-time home-buyers and for educational and medical expenses.

	Fiscal Year					
	1995	1996	1997	1998	1999	1995-99
	(Billions of dollars)					
Restore Pre-TRA IRAs (Joint Tax Committee)	-1.3	-6.8	-7.4	-7.8	-8.2	-31.5

Roth-Breaux Proposal (S. 2301, introduced July 21, 1994). IRAs would be universally available, back-loaded "IRA Plus" would be added as an option, and penalty-free early withdrawals would be allowed for first home, education, long-term unemployment, and high medical expenses. The IRA contribution limit would be indexed for inflation. These provisions follow the original Bentsen-Roth proposal. In addition, the Roth-Breaux proposal would increase the nonworking spouse deduction from $250 to $2,000. (S. 1669, introduced by Sen. Hutchinson on November 17, 1993, would also raise the nonworking spouse limit to $2,000, and also make the active participant rule apply separately to each taxpayer.)

	Fiscal Year					
	1995	1996	1997	1998	1999	1995–99
	(Billions of dollars)					
Roth–Breaux Proposal (Joint Tax Committee)	–0.8	–4.0	–4.2	–4.6	–5.0	–18.5

Rollovers to Back–Loaded IRAs. Various IRA proposals (including two bills introduced by Rep. Grams, H.R. 2434, June 16, 1993 and H.R.3645, November 22, 1993) would allow current balances from existing IRAs to be rolled over into back–loaded IRAs. This provision raises revenue in the budget window, because some income tax is imposed on the rolled over amounts. The proposals differ on whether the full amount rolled over or only original contributions are subject to income tax (the Grams bills only tax the original contributions), and on whether the tax is due at the time of rollover or can be paid in installments (e.g., over four years, as in the Grams bills).

H.R.11: An expanded IRA was proposed in H.R. 11 in 1992, but was voted down by 99% of Republicans. The revenue estimates are below.

	1993	1994	1995	1996	1997	1993–97
H.R. 11 expanded IRA proposal (JCT, Sept 14, 1992)	–0.24	.77	–1.4	–1.9	–3.3	–6.2

~~Future Budget Costs. The Roth–Breaux proposal costs less over the budget period than the restoration of pre–TRA IRAs because of the back–loaded IRA option. However, this option has a higher long–run revenue cost because it effectively increases the IRA contribution limit and because no tax is paid on normal withdrawals from these IRAs.~~ *Proposals with rollover options have ~~even~~ larger long–run revenue costs, relative to their five–year budget costs, because the tax that would have been paid on normal withdrawals from existing IRAs is collected early, in the current budget period.*

NEUTRAL COST RECOVERY SYSTEM

Current Law

Under current law, for regular income tax purposes, depreciable assets other than buildings and structures are generally written off over recovery periods of 3, 5, 7, 10, 15, or 20 years (depending upon their "class life"). An accelerated depreciation method may be used (200 percent declining balance for assets with 3, 5, 7, and 10 year recovery periods, and 150 percent declining balance for assets with 15 and 20 year recovery periods). Residential buildings are written off over 27.5 years, and non-residential buildings are written off over 39 years using the straight-line method. For alternative minimum tax (AMT) purposes, less accelerated depreciation methods must be used.

Proposals

There are several Republican neutral cost recovery proposals that are included in legislation currently pending before Congress. The bills differ somewhat in timing and the treatment of depreciation for AMT purposes, but all include the NCRS fundamentals as proposed by Kemp and Kasten in 1985 -- depreciation amounts adjusted for both inflation (based on a GNP deflator) and an additional 3.5% real rate of return.

1) Kemp-Kasten "Fair and Simple Tax" Proposal: A neutral cost recovery system (NCRS) was suggested in 1985 as part of the Kemp-Kasten "Fair and Simple Tax" proposal. The proposal allowed taxpayers to increase future depreciation allowances for inflation plus a specified real rate of return (3.5 percent). For example, if the depreciation that would otherwise have been allowed on a $100 investment in a 3-year ACRS property is $33.33 in the first year, $44.44 in the second year, $14.81 in the third year, and $7.41 in the fourth year (for a total of $100 of allowances), and the inflation rate is 3.9 percent, the first year NCRS depreciation allowance would remain $33.33, but the second year's depreciation allowance would be $47.79 ($44.44*(1.039)*(1.035)), and the third year's allowance would be $17.13 ($14.81*(1.039)*(1.039)*(1.035)*(1.035)), etc. The new total allowance would be $107.46.

The Kemp-Kasten proposal suggested slightly longer recovery periods than were then in effect under the 1981 Accelerated Cost Recovery System (ACRS), and exempted the adjustments from the AMT.

2) Investment Tax Incentive Act of 1993: On January 21, 1993, Rep. Nick Smith (R-MI) introduced H. R. 539, which would amend the Internal Revenue Code to allow the depreciation deduction to be computed based on a neutral cost recovery basis for property placed in service after December 31, 1992. Like the Kemp-Kasten proposal, it would include a real rate of return of 3.5% on top of the inflation adjustment. The bill was referred to the Ways and Means Committee and is awaiting further action.

3) Private Sector Job Creation and Economic Growth Act: On April 28, 1993 Rep. Dreier (R-CA) introduced H. R. 1885, which applies the NCRS adjustments to both the current law regular and AMT depreciation schedules, and proposes a phase-out of AMT depreciation preferences. It also includes a 3.5% adjustment on top of inflation. The bill has been referred to the House Budget, Government Operations, Judiciary and Ways and Means Committees.

4) Putting Jobs and the American Family First Act of 1993 (HR 2434) and Family, Investment, Retirement, Savings and Tax Fairness Act of 1993 (HR 3645): These bills, introduced by Rep. Grams (R-MN) on June 16, 1993 and November 22, 1993, respectively, would also create neutral cost recovery depreciation. H.R. 2434 and H.R. 3645 replace the 200 percent declining balance method allowed under MACRS with the 150 percent declining method before allowing for the NCRS adjustments. They also apply the NCRS adjustments to AMT depreciation and include a 3.5% adjustment on top of the inflation adjustment. H. R. 2434 has been referred to the House Government Operations, Rules and Ways and Means Committees.

5) Kasich Plan: The neutral cost recovery was also proposed by Representative Kasich. His proposal would allow for inflation, add an additional return on top of inflation and change the declining balance from double declining balance to 150% declining balance.

Revenue Estimate:

	Fiscal Year					
	1995	1996	1997	1998	1999	1995-99
	(Billions of dollars)					
Kasich Plan (Senate Budget Committee)	3.0	6.0	5.0	-1.0	-8.0	5.0

This proposal was also analyzed in a March 8, 1994 memo by Jane Gravelle, Senior Specialist in Economic Policy at the Congressional Research Service. ~~Ms. Gravelle found that the proposal would reduce taxable income by over $900 billion.~~

The net effect, Ms. Gravelle concluded, would be to increase taxable income by $87 billion in the first five years, but "*reduce* taxable income by $984 billion - an amount in the opposite direction that is eleven times as large" (p. 1) over a total of 39 years. And that was using only 1994 income levels throughout the time of the analysis.

THE WHITE HOUSE

WASHINGTON

September 29, 1994

MEMORANDUM TO THE PRESIDENT

From: Gene Sperling

Subject: Analysis on "Contract with America"

In your radio interview, you are likely to be asked about the Republican "Contract with America." Prior to the plan's release, we did a preemptive 22-page analysis that was widely circulated and made the case that the "Contract" would require $1 trillion in savings, and that the Republicans had offered no clue about how to pay for the savings without dramatic cuts that would hurt seniors.

In response to our document, Reps. Gingrich and Armey called a press conference on Friday, September 23 -- four days prior to their scheduled event. In that press conference, they released a three-page document that included about $200 billion in what they called "examples of possible offsets." We then widely circulated an eight-page follow-up analysis, which showed that even if one accepted all of their "possible offsets," they were still $800 billion short. As only $40 billion in welfare savings were actually in their contract, this was a generous assumption. Indeed, the New York Times stated that "the White House estimate may be low" because of the deceptive and hidden costs of some of the Republican tax breaks. ("The GOP's Deceptive Contract," September 28, 1994.)

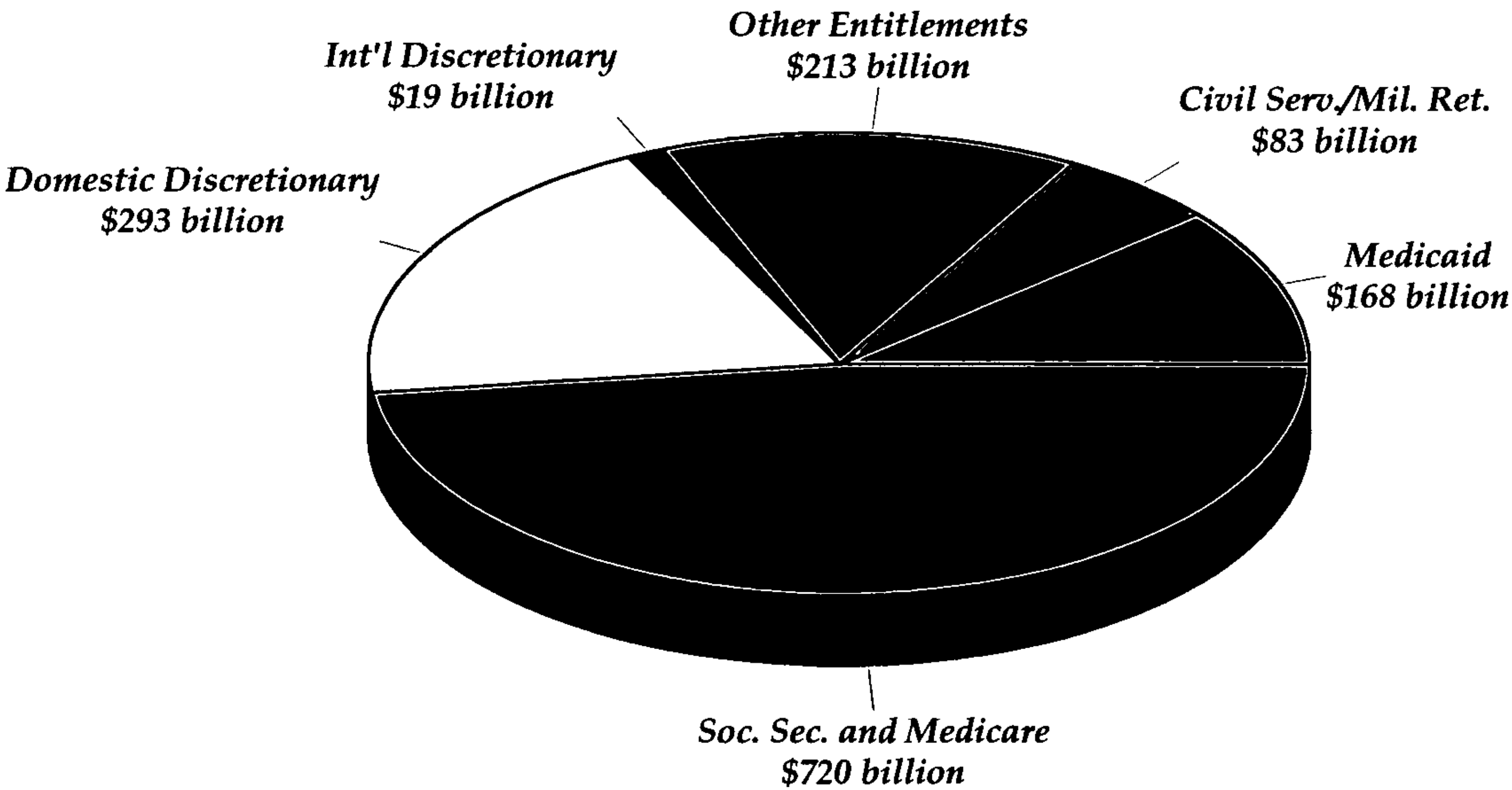
The actual release of their plan on September 27 offered few new details on financing. While their balanced budget amendment called for a balanced budget by the year 2002 (as opposed to Armey's legislation that calls for a balanced budget by 2000), the later date *only makes their hole larger*, as the deficit will grow larger by the year 2002, just as the costs of their tax cuts start to explode.

While it would be best for you to stay on the broad themes of "not going back" and "tax cuts for the well-off and promises that would increase the deficit or dramatically cut Medicare," I am attaching the eight page follow-up analysis that shows the budgetary hole of at least $800 billion. At the back is a chart we did that shows that nearly half of the funds available for cuts under the Republican plan would be in either Medicare or Social Security.

The House Republican's "Contract with America" will require *$300 billion* in cuts in FY 2000. Where do you think the cuts will come from?

PROGRAMS AVAILABLE FOR SPENDING CUTS, EXCLUDING DEFENSE

(CBO FY 2000 Projections)



CURRENT CBO PROJECTED BUDGET FOR FY2001

	FY2001
Revenues	$1.783 trillion
Outlays	$2.039 trillion
Total	-$256 bln. deficit

8 MAJOR COMPONENTS OF THE BUDGET

In billions of dollars

1. Net Interest	$283
Offsetting Recipients	$-94
Deposit Insurance	$-3
2. Social Security	$450
3. Medicare	$320
4. Medicaid	$186
5. Civil Service and Military Retirement	$85
6. Other (Veterans, food stamps, agriculture)	$211
7. Defense	$300(approx)
8. Domestic	$300(approx)
Total	2.039 trillion

HYPOTHETICAL OPTION TO BALANCE THE BUDGET USING 8 COMPONENTS AND REVENUES

1. Interest Reduction	$75 (optimistic assumption)
2. Social Security	$17 (COLA cut for all Soc Sec Recipients)
3. Medicare	$32 (10% cut -- all devoted to deficit reduction)
4. Medicaid	$10 (unprecedented cuts to poor: states would protest)
5. Civil/Mil. Retire.	$8 (10% cut)
6. Other	$17 (unprecedented cuts in many programs for poor, veterans)
7. Defense	$15 (strong bipartisan opposition)
8. Domestic	$60 (20% cut education, cops, kids, technology/defense conv.)
9. 25 Cent Gas Tax	$22 (5 times the 1993 gas tax increase)

$256 Savings to Balance the Budget in 2001

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1. BALANCED BUDGET AMENDMENT BY 2000 (ARMEY)	$700
2. CAPITAL GAINS	$10
3. FAMILY TAX CREDIT	$118
4. RESTORE PRE IRAS	$18.5– $31.5
5. $30,000 EARNING LIMIT	$27.1
6. REPEAL SS EARNING INCREASE	$21.1
7. ELIMINATION OF MARRIAGE PENALTY	????
8. DEFENSE	????
9. LONG–TERM CARE ASSISTANCE	0.5–3.0
10. TAX INCENTIVE FOR ADOPTION	0.2
11. COST–NEUTRAL RECOVERY	50.0
	960.9????

capital gains tax cut	maurice foley/eric toder
family tax credit	jim nunns
marriage penalty	jim nunns
ira	jim nunns/ randy hardock
armey flat tax	jim nunns
earnings limit for seniors	randy hardock/janet holtzblatt
1993 social security increases	randy hardock/janet holtzblatt
long-term care incentives	randy/hardock/janet holtzblatt
tax incentives for adoption	maurice foley/janet holtzblatt
dependency exemption for elderly	jim nunns
neutral cost recovery	eric toder

maurice foley	622-1336
eric toder	622-0120
jim nunns	622-1328
randy hardock	622-0170
janet holtzblatt	622-1327
norm richter	622-1950

All can be reached at home through Treasury operator 622-1260

INTERNAL BUDGETARY ANALYSIS

THE HOUSE REPUBLICAN'S *CONTRACT WITH AMERICA*

[Not for Distribution]

TABLE OF CONTENTS

ONE-PAGE BUDGET SUMMARY OF HOUSE REPUBLICAN CONTRACT

1. TRILLION DOLLAR COSTS: On September 27, 1994, House Republicans will sign an what they will describe as a list of promises that together will require unprecedented budgetary savings to achieve, including balancing the budget and paying for new spending and expensive new tax reductions. First, the Republican "contract" would require dramatic savings in order to balance the budget by either 2000 or 2002 -- which will require either a $700 billion five-year deficit reduction plan (under Republican Conference Chairman Armey's proposal) or a $1.135 trillion seven-year deficit reduction plan under the path required by the Balanced Budget Amendment Act. Yet, in addition to the savings required to achieve a balanced, the House Republicans call for $70 billion in increased defense spending, over $200 billion in new tax cuts -- including changes in the marriage penalty ($72 billion), a child tax credit for families making up to $200,000, ($107 billion), and increased benefits to the top 13% of Social Security recipients ($27 billion). In net, the **Republicans will have to find additional budget savings of between $858 billion and $1 trillion over five years or $1.64 trillion over seven years.**

2. TAX CUTS: REGRESSIVITY AND EXPLODING COSTS: The plan also includes three proposals that are designed to incur large costs to the federal deficit in later years -- or additional cuts to pay for them. The expanded, backloaded IRA, the capital gains tax cut, and the neutral cost recovery system are all specially designed to hide current costs and push out the deficit increases beyond the five-year budget window. Over 70% of the capital gains tax cut benefits go to Americans making over $100,000, while the neutral cost recovery system starts out artificially raising funds, but then costs $8 billion by the fifth year alone -- with dramatically increased costs thereafter.

3. FAILING THE SERIOUSNESS TEST: The House Republican "contract" appears not even to attempt to say how it would be paid for. As the Wall Street Journal reported on Friday, September 16, 1994, even Senate Republicans refused to sign on because, as one Republican Senator stated, "they are just blowing away money." The "contract" makes an iron-clad commitment to balance the budget yet rather than give details out for the first time as to what cuts (Medicare, Social Security, veterans) would be made, it instead offers hundreds of additional billion dollars in new spending and tax cuts.

4. HOUSE ALTERNATIVE BUDGET FALLS HUNDREDS OF BILLIONS SHORT: The most specific plan House Republican plan to find savings for deficit reduction and tax cuts, relied on severe and largely unrealistic spending cuts, yet would still fall approximately $500 billion short of what would be necessary to pay for the massive Republican "contract."

5. MEDICARE AND SOCIAL SECURITY: Any effort by the House Republicans to find the hundreds of billions of dollars of savings necessary to balance the budget, while paying for their additional spending and tax cuts without defense cuts or more taxes on well-off Americans would lead to dramatic cuts to Medicare or Social Security or both. Simply to balance the budget under their budget criteria would require a 17% cut across the board -- and over 20% when you add in their new spending and tax benefits. Entitlement cap proposals that focus on the rate of growth would have an ever harsher impact on Medicare. If Social Security were to be exempt from such savings, the impact on Medicare, fighting crime, education and training could be even harsher.

TRILLION DOLLAR COSTS

The House Republican proposal starts with a commitment to find savings to balance the budget even though they "take off the table" areas like defense spending and taxes on the wealthiest Americans. Even if the House Republicans were to propose this and no additional items, they would need to come forth with a major deficit reduction plan far beyond what they have ever proposed. As their "contract" promises to not only find savings for balancing the budget but paying for new spending and new tax cuts, they would need to find savings in the neighborhood of $1 trillion.

I. SAVINGS REQUIRED TO MEET BALANCED BUDGET PROPOSALS:

A: Seven Year Path: There are two current proposals for a balanced budget that some House Republicans have signed on to. One is the Balanced Budget Amendment Act, which was amended to call for a balanced budget by the year 2002. This would allow for the opportunity to phase in a balanced budget over seven years. If this was done in an even, straight-line approach, the necessary deficit reduction plan would call for a $1.135 billion deficit reduction program over FY1996-FY2002. See Table entitled "Deficit Reduction Necessary to Balance the Budget by FY 2002" in Section V.

B: Armey's Five Year Path: Congressman Armey has recently proposed balancing the budget by the year 2000. This would require a five-year deficit reduction plan. Again, assuming this was phased-in in an equal straight-line approach, this would call for a $704 billion dollar deficit reduction plan over five years. (Both estimates use the current Congressional Budget Office baseline, see, "The Economic and Budget Outlook: An Update," CBO, August 1994, p.31)

II. SAVINGS REQUIRED TO BOTH SATISFY BALANCED BUDGET AND ADDITIONAL REPUBLICAN PROPOSALS: In addition to the savings required to balance the budget, the House Republican leadership would need to find savings for the following proposals:

	1996-2000 ($ in billions)	1996-2002
1. Capital Gains Tax Cut	-10.2	-21.4
2. Gramm-Gingrich Indexing	-4.8	-10.0
3. $500 Tax Cut for Children	-107.0	-158.2
4. Defense Increases	-73.7	-124.7
5. Elimination of the Marriage Penalty	-72.7	-108.9
6. Long-Term Care Incentives	-1.5	-2.3
7. Ease Social Security Earnings Test	-11.8	-17.0
8. 85% Soc. Sec. Exclusion Repeal	-21.0	-31.4
9. Tax Incentives for Adoption	-0.2	-0.3
10. Expansion of IRAs	-6.2	-22.6
11. Neutral Cost Recovery	5.0	-11.0
12. Savings Needed for BBA	-554.0	-1135.0
Total Cuts Needed	**-$858.1**	**-$1,642.8**

PROJECTED COST OF HOUSE REPUBLICAN PROPOSAL

($ in billions)

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Proposal	Fiscal Year 1996	1997	1998	1999	2000	Total 1996-2000	Fiscal Year 2001	2002	Total 1996-2002
1 Capital Gains Tax Cut *Source: JCT analysis of Bush Administration FY 1992 proposal.*	0.8	3.7	-3.4	-5.7	-5.6	-10.2	-5.6	-5.6	-21.4
2 Gramm-Gingrich Indexing *Source: JCT analysis conducted at time of proposal.*	0.5	-0.3	-0.9	-1.5	-2.6	-4.8	-2.6	-2.6	-10.0
3 $500 Tax Credit for Children *Source: House Budget Comm. report on FY 1995 Kasich Budget Proposal.*	-4.7	-25.6	-25.6	-25.6	-25.6	-107.0	-25.6	-25.6	-158.2
4 Defense Increases *Source: proposed in Rep. Kasich's FY 1995 budget alternative.*	-6.4	-11.5	-13.8	-16.5	-25.5	-73.7	-25.5	-25.5	-124.7
5 Elimination of the Marriage Penalty *Source: JCT analysis conducted Sept. 16, 1994.*	-7.2	-14.7	-15.8	-16.9	-18.1	-72.7	-18.1	-18.1	-108.9
6 Long-Term Care Incentives *Source: CBO analisys of Michel Health Care Bill, 1994.*	-0.2	-0.3	-0.3	-0.3	-0.4	-1.5	-0.4	-0.4	-2.3
7 Ease Social Security Earnings Test *Source: OMB estimate.*	-1.6	-2.5	-2.5	-2.6	-2.6	-11.8	-2.6	-2.6	-17.0
8 85% Soc. Sec. Exclusion Repeal *Source: Office of Tax Analysis, Dept. of Treasury, Sept. 16, 1994.*	-1.7	-4.5	-4.7	-4.9	-5.2	-21.0	-5.2	-5.2	-31.4
9 Tax Incentives for Adoption *Source: Office of Tax Analysis, Dept. of Treasury, Sept. 16, 1994.*	0.0	0.0	0.0	0.0	0.0	-0.2	0.0	0.0	-0.3
10 Expansion of IRAs *Source: JCT estimate of Bentsen/ Roth IRA proposal, Sept. 14, 1992.*	-0.2	0.8	-1.4	-2.0	-3.3	-6.2	-8.2	-8.2	-22.6
11 Neutral Cost Recovery *Source: Senate Budget Comm. analysis of Kasich proposal.*	3.0	6.0	5.0	-1.0	-8.0	5.0	-8.0	-8.0	-11.0
Sub-Total	-17.7	-48.9	-63.4	-76.9	-96.9	-304.1	-101.8	-101.8	-507.8
12 Cuts Necessary to Balance Budget *-Based on a 7-year deficit reduction plan.*	-26.0	-68.0	-97.0	-156.0	-207.0	-554.0	-262.0	-319.0	-1135.0
Total Cost	**-43.7**	**-116.9**	**-160.4**	**-232.9**	**-303.9**	**-858.1**	**-363.8**	**-420.8**	**-1642.8**

DEFICIT REDUCTION NECESSARY TO BALANCE THE BUDGET BY FY 2000

($ in billion)

	Fiscal Year 1996	1997	1998	1999	2000	Total
CBO Baseline Deficit	176	193	197	231	257	
Armey proposal	140	105	70	35	0	
Deficit Reduction	**36**	**88**	**127**	**196**	**257**	704

Note: Projections assume straight-line deficit reduction from FY 1996 to FY 2000. Different assumptions are possible that could lead to slightly greater or slightly lesser costs.

DEFICIT REDUCTION NECESSARY TO BALANCE THE BUDGET BY FY 2002

($ in billions)

	Fiscal Year					5-Year Total			7-Year Total
	1996	1997	1998	1999	2000		2001	2002	
CBO Baseline Deficit	176	193	197	231	257		287	319	
Balanced Budget Amendment , as proposed in 1994	150	125	100	75	50		25	0	
Deficit Reduction	**-26**	**-68**	**-97**	**-156**	**-207**	**-554**	**-262**	**-319**	**-1135**

Note: Projections assume straight-line deficit reduction from FY 1996 to FY 2000. Different assumptions are possible that could lead to slightly greater or slightly lesser costs.

ANALYSIS OF LIKELY PROPOSALS IN HOUSE REPUBLICAN CONTRACT

At this moment, there does not exist a definitive and detailed list of the exact proposals that House Republicans will be proposing on September 27, 1994 as part of their "Contract" as to their future agenda. As they have not yet given out the details of their proposals, we can only take Haley Barbour at his word that they will mostly consist of "existing proposals." Therefore, we have estimated costs based on past House Republican proposals, while using estimates when possible from the Congressional Budget Office, Joint Tax Committee, Office of Management and Budget, Treasury Department or one of the Congressional Budget Committees. To the degree that more details come out that differ from the estimates below, we will revise our estimates.

1. LACK OF DETAIL AS TO WHERE THE SAVINGS WILL COME FOR BALANCING THE BUDGET AND ADDITIONAL PROPOSALS: The House Republican "contract" appears to not even attempt to say how it would be paid for. As the Wall Street Journal reported on Friday, September 16, 1994, even Senate Republicans refused to sign on because as one Republican Senator stated, "they are just blowing away money." This characterization is understandable. First the "contract" makes an iron-clad commitment to balance the budget -- presumably by 2002 as the balanced budget amendment requires, but possibly by the year 2000 as proposed recently by Republican Conference Chairman Armey. Whatever one's view of this Amendment, it would unquestionably require a deficit reduction plan of either $700 billion over five years or $1.135 trillion over seven years. Yet, rather than give details out for the first time as to what cuts (Medicare, Social Security, veterans) would be made, the "Contract" instead offers hundreds of billions of dollars in new spending and tax cuts, that would all have to be paid for in addition to the savings that would have to be found to balance the budget by 2000-2002. *Yet, it is still unclear whether the Contract will include agreement on any specific means as to how to find the trillion dollars needed to meet their tax cut, spending increases and deficit reduction pledges.*

2. ESTIMATED COST IN EXCESS OF TRILLION DOLLARS: Under almost any estimates, it seems clear that the essential promise, to balance the budget by the year 2000 (Armey) or 2002 (Balanced Budget Amendment of 1993) ***plus*** increase defense spending ***plus*** several tax cuts, would require savings beyond anything that any member of the Republican House Leadership has ever presented. In order for the plan to add up, the Republicans must find $700 billion in savings over five years to balance the budget or $1.135 trillion over seven years. In addition, they must find five years savings to pay for increased defense spending ($73 billion), change in marriage penalty ($72 billion) a child tax credit for families making up to $200,000, ($107 billion), and increased benefits to the top 13% of Social Security recipients ($27 billion).

- **Five-Year Costs -- $850 Billion to $1 Trillion:** The savings they would need to find to achieve their contract goals in the first five years would be between $850 billion and $1 trillion depending on whether they chose the Armey balanced budget bill or the Balanced Budget Amendment Act path.

- **Seven-year Costs -- $1.5 Trillion:** If the Republican Contract assumes that they will balance the budget by the year 2002 -- a seven-year plan -- the burden will be even greater. This is partly because trends in the deficit require a $1.135 trillion deficit reduction plan just to balance the budget over 7 years (without any new tax cuts), and partly because the costs of the core of their tax cuts (backloaded IRAs, capital gains reductions, neutral cost recovery) explode in the out-years --just as they were trying to get the budget to balance.

3. TAX CUTS: REGRESSIVITY AND EXPLODING COSTS: Other than the child tax credit, they will include three proposals (backloaded IRAs, capital gains tax cut, and Neutral Cost recovery) in which the benefits go disproportionately to the well-off and rely on gimmicks to push their significant costs to the out-years -- beyond the five years where proposals are scored in the House of Representatives. This latter budget reality contradicts the goal of a balanced budget, since they create out-year deficit increasing costs that the Republicans have never said how they would fund.

A. Examples of Regressivity:

- **Capital Gains:** The Joint Tax Committee (1992) has found that over 70% of the gains of a capital gains tax cut would go to Americans making over $100,000 and over 50% would go to the top 1% of Americans -- those making over $200,000.

- **Unnecessary Regressivity on Child Tax Credit:** Even if the Republicans were able to pay for their $500 per child tax credit, their proposals would give billions of tax cuts to the top 2% of Americans, while denying working poor families even a penny. Under the previous child tax credit proposal, a family of four making $150,000 would get a $1000 tax break while a family of four making $20,000 would get not a single penny since the tax credit is not refundable.

- **Opposition to 1992 and 1993 Budget Proposals**: In 1992, 99% of Republicans voted against a child tax credit and an expanded IRA simply because the program also included a tax increase on the top 1.2% of earners. In 1993, 100% of Republicans voted against a budget with a dramatic expansion of the Earned Income Tax Credit for 15 million working families largely, again, because of tax increases on the top 1.2% -- those making over $180,000 adjusted gross income.

B. Examples of Exploding Costs:

- **Backloaded IRA:** One proposal is a "backloaded IRA." This proposal hides the true costs in the first few years, by allowing only after-tax income to be put in these IRAs, and then making all interest income tax free -- forever. This will cost up to $8 billion a year according to previous Joint Tax Committee estimates -- just as the deficit is projected to rise.

- **Neutral Cost Recovery System**: This provision gives huge new depreciation tax cuts that increase each year, so that the main costs fall outside of the five-year period in which proposals are given cost estimates in the House of Representatives. These gimmicks are objectionable not only because they are deceptive to the American people in terms of how to pay for them, but they also directly contradict the goals of a balanced budget, as the rising costs will add to the deficit in the out-years -- where the Congressional Budget Office and OMB now see deficit increases as a percentage of GDP taking place. Indeed, even by the fifth year of the proposal, the effect of the neutral cost recovery has changed from gaining revenue to losing $8 billion a year, with increasing costs thereafter.

4. MOST AGGRESSIVE REPUBLICAN SAVINGS PLAN FALLS APPROXIMATELY $500 BILLION SHORT: The most specific plan House Republican plan to find savings for deficit reduction and tax cuts, relied on severe and largely unrealistic spending cuts, yet would still fall $500 billion short of what would be necessary to pay for the massive Republican "contract." The House Republican alternative budget in 1994 (sponsored by Rep. Kasich) sought to pay for tax cuts and additional deficit reduction through spending cuts that were often double counts, unrealistic or called for unjustified reductions in investment programs. The Republican plan included double counting up to $50 billion in overhead and personnel reductions that are already in the President's budget; a $44 billion cut in Medicare, a $30 billion cut in health care, a $53 billion cut in education and training including cuts in college loans ($10 billion). and job training ($10 billion) a $57 billion cut in transportation and infrastructure ($18 billion coming from selling the Air Traffic Control Corporation), and $24 billion in energy and environmental programs. The Republican budget also calls for cuts in criminal justice of $21 billion -- which would not allow for the new cops and prison funding in the crime bill. This still leaves over a $500 billion shortfall in the five-year plan, and an even greater shortfall over seven years because of the projected increase in the deficit and because the costs of several House Republican proposals explode after the first few years.

- **Entitlement Cut and Entitlement Caps:** The Kasich plan cut entitlements $101 billion over five years, including a $10 billion cut in agriculture, a $10 billion reduction in student loans, and a $44 billion Medicare reduction. An entitlement cap proposal that cut $200 billion in savings would likely add only $100 billion in savings after double counting is removed.

- **Double Counting:** The Kasich proposal included provisions such as personnel and overhead reductions that are already part of the Clinton budget. (ck)

5. IMPACT ON SENIORS: The Republican proposal seeks to mask the likely impact it would have on seniors -- either through cuts in Medicare or Social Security. On its face, the House Republican proposal increases spending by $27 billion on Social Security for the top 13% of recipients and another $10 billions on seniors who are still working -- again with most of the benefits going to the most well-off recipients. Yet, if the House Republican were serious about paying for their plan while taking off the table taxes on the well-off and defense, there would be little choice but to call for severe cuts to Medicare or Social Security -- or both -- at the same time.

- **1994 Republican House Alternative:** In the 1994 Kasich proposal, there were $72 billion in cuts to health care -- including an additional $44 billion in Medicare cuts. Yet, the real threat to Medicare is that it seems to be the only viable target for paying for the Republican proposals. As the Republicans are opposed to any tax increases on the wealthiest Americans, and call for defense increases, their main vehicles for spending cuts would have to be Medicare or Social Security.

- **Entitlement Caps:** Armey, among others, has called for entitlement caps that would freeze spending on entitlements at approximately the rate of inflation. Whatever the merits of such a proposal, the clear fact is that such proposals represent plans to dramatically cut Medicare costs. For example, a proposal similar to Armey's would lead to $161 billion in Medicare cuts over five years. (OMB ck)

- **Seniors Are the Main Primary Possible Target:** If the budget must be balanced under the Republican criteria, with no cuts in defense and no tax increases on the well-off, there is simply no choice but to call for major cuts in either Medicare or Social Security or both -- anywhere from 24%-33% of their budgets in the year 2002. These are the dramatic reductions in assistance for seniors that would be required to balance the budget and pay for the tax cut and spending increases that are called for on the Republican contract.

6. FISCAL CYNICISM: The House Republican contract resorts to the type of fiscal cynicism and gimmickry that led to the escalation of the deficit when the Republicans controlled the White House and the Senate between 1981 and 1986. First, at the same time the Republicans talk about "means testing" entitlements and the need for tough choices, they seek to increase over $20 billion of entitlement spending by repealing the deficit reduction provision that made the top 13% of Social Security recipients count a higher percentage of their Social Security benefits as taxable income. Second, as mentioned above, they have three tax cuts which are specifically designed to do exactly what deficit reduction efforts are supposed to alleviate -- pushing costs out to the future to avoid fiscal responsibility today. The backloaded IRA, the cost-neutral recovery system and many forms of the capital gains tax cut are specifically designed to mislead the American people as to their true costs by pushing the costs beyond the budget window. The reply from the Republicans who are advocating them is familiar: tax cuts will raise funds, the same fiscal logic that led to exploding deficits when the Republicans controlled the White House.

IMPACT ON SENIORS

The Republican House alternative budget requires close to a trillion dollars in savings over the next five years. There is little sense as to how they would make up this significant number. Yet, as they have consistently taken off the table defense (where they call for significant increases) and tax increases on the most well-off Americans, both past history and basic budget logic implies that the major impact would have to be on Medicare or Social Security.

The CBO baseline for FY 2000, breaks up the non-interest part of the budget into the following categories:

	FY2000
Domestic Discretionary	292
Defense	292
Social Security	430
Medicare	290
Medicaid	168
Civil Service and Military Retirement	83
Other Entitlements	213
TOTAL	1768
AVAILABLE SAVINGS SOURCES WITHOUT DEFENSE	1476
AVAILABLE SAVINGS SOURCES WITHOUT DEFENSE AND SOCIAL SECURITY	1046

It is first important to note that of the $1.476 billion in federal spending available for reduction under the House Republican alternative, nearly half -- or $720 billion -- is in either Social Security or Medicare. Therefore, it seems unavoidable that they would be major targets for paying for the House Republican "contract." Consider the following:

The deficit for the year 2000 is now projected to be $257 billion. With the addition of the Republican tax cuts and spending increases, the deficit would be $101 billion greater. Thus, the amount of saving needed to balance the budget in the year 2000 would be $358 billion. Even if one assumed $58 billion in interest savings, that would still mean finding $300 billion savings. Out of the $1.476 trillion of spending available, that would mean a 20% reduction in spending across the board -- including Social Security, Medicare, criminal justice etc. If Social Security were also exempted, ***it would require a near 30% reduction in spending across-the-board.*** While not every program would have to be cut 30%, every additional program that is exempted requires more severe cuts on the remaining programs.

APPENDIX - SUMMARIES OF ANTICIPATED BUDGETARY PROPOSALS

- CAPITAL GAINS TAX CUT
- INDEXING CAPITAL GAINS
- CHILDREN'S $500 TAX CREDIT FOR FAMILIES UNDER $200,000
- ELIMINATION OF THE MARRIAGE PENALTY
- EASE THE SOCIAL SECURITY EARNINGS TEST
- REPEAL THE 85 PERCENT MAXIMUM INCLUSION RATE FOR SOCIAL SECURITY BENEFITS
- EXPANDED INDIVIDUAL RETIREMENT ACCOUNTS
- NEUTRAL COST RECOVERY SYSTEM

CAPITAL GAINS TAX CUT

Current Law

Under current law, long-term capital gains are fully included in adjusted gross income. Taxpayers in the 15 and 28 percent brackets therefore pay the same tax rates on capital gains as on other income. Long-term capital gains rates are capped at 28 percent, so taxpayers in the 31 percent and higher tax brackets pay a lower rate on long-term capital gains than on other income. The rate cap was instituted in OBRA-90 and retained in OBRA-93. Under pre-Tax Reform Act of 1986 law, taxpayers were permitted to exclude 60 percent of the excess of long-term gains over short-term losses. Thus the maximum tax rate on long-term capital gains was 20 percent (40 percent of the 50 percent top income tax rate).

Proposals

Republican proposals on capital gains are likely to take one of several basic forms:

1. BUSH/WALKER PROPOSALS: H.R. 1450 (introduced by Rep. Walker on March 23, 1993) provides a 10 percent exclusion for assets held between one and two years and an additional 10 percent exclusion each year the asset is held beyond two years, with a 100 percent exclusion for assets held ten years or more. The Bush Administration made two such proposals for which JCT revenue estimates are given below. The FY 1992 Budget proposal would have allowed a 15 percent exclusion for assets held between one and two years, a 25 percent exclusion for assets held between two and three years, and a 35 percent exclusion for assets held three years or more. The FY 1993 Budget proposal was similar, except the exclusions were 15 percent, 30 percent, and 45 percent.

	1992	1993	1994	1995	1996	1992-96
			(Billions of dollars)			
FY 1993 Budget Proposal	0.8	3.7	-3.4	-5.7	-5.6	-10.2

2. 50% EXCLUSION: Exclude 50% of capital gains income from taxation, which would have the effect of halving the tax rate individuals pay on capital gains. For example, a 50 percent exclusion would reduce the maximum capital gains tax rate to 14 percent (50 percent of 28 percent) and taxpayers in the 15 percent bracket would be subject to a 7.5 percent rate.

3. ARCHER PROPOSALS: H.R. 3739, introduced by Rep. Archer January 26, 1994 would exclude some percentage of long-term gains, but repeal the 28 percent rate cap. A 50 percent exclusion (e.g.,) would reduce the maximum capital gains tax rate to 19.8 percent (50 percent of 39.6 percent) and taxpayers in the 15 percent bracket would be subject to a 7.5 percent rate. Rep. Archer also introduced legislation (on January 5, 1993), H.R. 53, which provides a 30% exclusion.

4. CRANE/DREIER/GRAMS PROPOSALS TO REDUCE THE RATE TO 15% Reduce the rate cap to 15 percent. This would reduce the maximum tax rate to 15 percent. H.R. 151 (introduced by Rep. Crane January 3, 1993), H.R. 1855 (introduced by Rep. Dreier April 28, 1993), H.R. 2424 (introduced by Rep. Grams June 16, 1993), and H.R. 3645 (introduced by Rep. Grams November 22, 1993) all provide a maximum rate of 15 percent, with a 7.5 percent rate for gains in the 15 percent bracket. (These bills also all index gains for inflation.)

DISTRIBUTION:

Over the past few years, the Joint Tax Committee has been asked on numerous occasions to estimate the distributional effects of reducing the capital gains tax. On all occasions, it has been found to go disproportionately to the highest income brackets. The JCT found that under the most recent major Republican proposal, President Bush's 1992 proposal, 70% of the benefits went to taxpayers making over $100,000 and 52.5% of the benefits went to those in the top 1% making over $200,000.

Distribution of Aggregate Tax Change

Less than $10,000	0.2%
$10,000-$20,000	0.5%
$20,000-$30,000	1.6%
$30,000-$40,000	3.6%
$40,000-$50,000	4.5%
$50,000-$75,000	11.1%
$75,000-$100,000	8.6%
$100,000-$200,000	17.4%
$200,000 and over	52.5%
TOTAL	100%

JOINT TAX COMMITTEE (Estimate of Bush Administration's Capital Gains Proposal, February 3, 1992)

INDEXING CAPITAL GAINS

Index capital gains for inflation (e.g., H.R. 48, introduced by Rep. Archer on January 5, 1993 and the bills listed in point 4 of the Capital gains Tax Cut section). Taxpayers would increase the basis (cost) of their assets to adjust for inflation since the asset was purchased. Variations of this proposal would index capital gains only for inflation after some future date or add indexing to one of the exclusion proposals. S. 1829 (introduced by Sen. Hatch on February 4, 1994) indexes gains for inflation and provides an annual exclusion of $100,000 (joint) and $50,000 (single). JCT revenue estimates for a 1991 Gramm-Gingrich prospective indexing proposal are shown below.

Revenue Estimates

	1992	1993	1994	1995	1996	1992-96
		(Billions of dollars)				
Gramm-Gingrich Indexing Proposal (JCT, September 23, 1991)	0.5	-0.3	-0.9	-1.5	-2.6	-4.8

CHILDRENS' $500 TAX CREDIT FOR FAMILIES UNDER $200,000

Kasich Proposal: In the House Republican alternative, Congressman Kasich proposed a $500 per child tax credit for families making under $200,000 that he himself estimated would cost $107 billion over five years.

Grams Proposal: Rep. Grams proposed a $500 per child tax credit (H.R. 2434, June 16, 1993, and H.R. 3645, November 22, 1993) that would make the credit non-refundable, have no income phaseout, and index the $500 amount, but would apply to children 17 and under.

Revenue Estimates

The following revenue estimates assume an effective date of January 1, 1995.

Kasich: Kasich estimates his own proposal to cost $107 billion over five years, with an average cost for full year of over $25 billion.

Grams Proposal:

	Fiscal Year (Billions of dollars)					
	1995	1996	1997	1998	1999	1995-99
$500 Per Child Tax Credit (Office of Tax Policy, Treasury Department, 1994)	-12.4	-25.2	-26.9	-16.9	-27.5	-118.1

Analysis

Unnecessary Regressivity: Because the proposed child tax credit is available for families making up to $200,000 and because it denies any refundability to families with low tax burdens, the proposal would lead to serious inequities to working families. For example, a family with two children making $150,000 would get a tax cut of $1000. Yet, a similar family of four making $20,000 would get no tax benefit whatsoever because they would not have taxable income to offset.

House Republicans Opposed a Child Tax Credit in 1992 and 1993:
In 1992, 99% of Republicans voted against a child tax credit and an expanded IRA simply because the program also included a tax increase on the top 1.2%. In 1993, 100% of Republicans voted against a budget with a dramatic expansion of the Earned Income Tax Credit largely, again, because of tax increases on the top 1.2% -- those making over $180,000 adjusted gross income.

ELIMINATION OF THE MARRIAGE PENALTY

Current Law

Under U. S. tax law, getting married can affect a couple's tax liability, both positively ("marriage bonus") and negatively ("marriage penalty").

Proposal

1) Representative Istook Proposal: On February 10, 1994, Rep. Istook (R-OK) introduced HR 3851, to amend the Internal Revenue Code of 1986, eliminating marriage penalties. Under this proposal, spouses would have the option to file using the tax status they would have had if they had not been married, and to allocate income and deductions between them as if they had not been married.

The bill has been referred to the House Ways and Means Committee and is awaiting further action.

Revenue Estimate

In a September 16, 1994 letter to Representative Gephardt, the Joint Committee on Taxation analyzed the cost of eliminating the marriage penalty, using guidelines similar to the Istook bill.

	Fiscal Year					
	1995	1996	1997	1998	1999	1995-99
	(Billions of Dollars)					
Lost Federal Revenue	-7.2	-14.7	-15.8	-16.9	-18.1	-72.7

Analysis

Removing or reducing marriage tax penalties would reduce tax revenues by a very substantial amount. If accompanied by other tax changes to prevent a net loss of revenue, the tax burden would shift from two-income families onto one-income families (which frequently have just one parent) and single persons.

In addition to the lost government revenue, the Istook plan would also create incentives for couples to "game" the tax system and manipulate their unearned income, which would complicate the tax filing process and give some couples an unfair advantage over others.

Married couples would manipulate their unearned income by moving ownership of assets to the spouse facing the lower tax rate. This would enable couples with significant unearned income to reduce their taxes, whereas other married couples with the same total income (but through only salary and wages) would be forced to pay a higher effective tax rate.

EASE THE SOCIAL SECURITY EARNINGS TEST

Current Law

Retired workers between the ages of 65 and 69 have their social security benefits reduced by 33 and 1/3 cents for each dollar of earnings over $11,160. Above age 69, persons receive full social security benefits, regardless of their earnings. The earnings test is lower for younger beneficiaries. They can earn up to $8,040 before benefits are reduced, and they are subject to a 50 percent benefit reduction. The earnings test thresholds are adjusted for inflation each year.

Proposals

1) **Older Americans Freedom to Work Act of 1993:** On January 5, 1993, Rep. Hastert (R-IL) introduced HR 300, which would eliminate the Social Security earnings test altogether. The bill has been referred to the Ways and Means Committee where it is awaiting action.

Budgetary Estimate

The following are OMB estimates.

	Fiscal Year					
	1995	1996	1997	1998	1999	1995-99
	(Billions of dollars)					
Eliminating Earnings Test						

2) It has also been proposed that the amount of allowable earnings for social security recipients, age 65 through 69, be increased to $30,000.

Budgetary Estimate

	Fiscal Year					
	1995	1996	1997	1998	1999	1995-99
	(Billions of dollars)					
$30,000 Earnings Test OMB estimate	-1.6	-2.5	-2.5	-2.6	-2.6	-11.8

3) Another alternative would phase the increase to $30,000 in over five years.

Budgetary Estimate

	Fiscal Year					
	1995	1996	1997	1998	1999	1995-99
	(Billions of dollars)					
Five-Year Phase-in of $30,000 Earnings Test OMB estimate	-0.3	-0.9	-1.4	-1.9	-2.3	-6.8

Analysis

This proposal is extremely regressive -- the vast majority of the benefits would go to high-income seniors.

Most retired workers between the ages of 65 and 69 would not benefit from these proposals. Of the 8 million persons in this age group who are covered by social security, 75% -- 6 million -- did not work at any time in 1989. Their decisions to retire were based on many factors in addition to the social security earnings test: health, leisure time, savings, pension income, the size of social security benefits, and employers' demand for elderly workers. For these same reasons, they are unlikely to seek employment once retired, even if the earnings test were raised.

Among those who currently work, many would likely not increase their work effort further in response to changes in the earnings test. Either they currently earn far less than the exempt amount (and would be unaffected by the change) or they earn too much to receive benefits even if the earnings test threshold were increased to $30,000. As the earnings test thresholds are increased, some retired workers, who currently earn too much to qualify for benefits, and their families would become eligible to receive benefits. Receipt of this windfall may cause some of these higher wage workers to reduce their work hours.

REPEAL THE 85 PERCENT MAXIMUM INCLUSION RATE FOR SOCIAL SECURITY BENEFITS

Current Law

Taxpayers with sufficient income must include some of their Social Security benefits in income subject to income tax. Taxpayers with incomes under the first threshold ($25,000 for single taxpayers and $32,000 for married taxpayers, filing jointly) do not include any of their social security benefits in AGI. Those with incomes between the first and second thresholds ($34,000 for single taxpayers and $44,000 for married taxpayers, filing jointly) include up to 50 percent of their Social Security benefits above the threshold in AGI. Finally, those with incomes over the second threshold include up to 85 percent of benefits above the second threshold in AGI, and 50% of their benefits between the first and second thresholds.

Proposals

Although we could not locate any Republican bills on this topic, it is expected that any proposal to alter the inclusion rate would reduce the highest marginal inclusion rate to 50%.

Revenue Estimates

	Fiscal Year					
	1995	1996	1997	1998	1999	1995-99
	(Billions of dollars)					
Repeal 85% SS Inclusion Rate Office of Tax Analysis, Department of Treasury	-1.7	-4.5	-4.7	-4.9	-5.2	-21.0

Analysis

This proposal would benefit only the highest earning social security recipients. Social security recipients who are in greatest need of income supplements - those who receive less than $25,000 - receive no benefit at all. Instead, wealthier recipients will retain additional money from the Social Security trust fund, potentially at the expense of those who need it most.

Since the revenue from taxation of Social Security benefits is entirely returned to the Social Security trust funds from which the benefits were paid, such taxation provides needed revenues for the trust funds and reduces the need for future increases in payroll taxes (which would be particularly burdensome for lower income, younger workers). Moreover, the 85% inclusion rate does not adversely affect lower and middle income retirees. In fact, it may help such retirees by reducing the need to curb future benefit cost-of-living increases.

EXPANDED INDIVIDUAL RETIREMENT ACCOUNTS

Current Law

Taxpayers are allowed to deduct up to $2,000 (or earned income, if less) contributed to an IRA if (regardless of income) they are not active participants in an employer-sponsored pension plan (and their spouses are not active participants), or if their AGI is less than $40,000 (joint) or $25,000 (single). The deduction for active participants is phased out over $10,000 of AGI above the income thresholds (e.g., between $40,000 and $50,000 of AGI on joint returns). These income limits were added by the Tax Reform Act of 1986 (TRA). Nonworking spouses may contribute $250 to an IRA. Taxpayers not eligible to make deductible IRA contributions can make nondeductible contributions (subject to the same dollar limits). Earnings on IRA contributions are not taxed currently. Distributions from IRAs are subject to income tax. A additional 10 percent penalty is imposed on IRA distributions made before age 59 1/2.

Proposals: There have been several proposals to expand eligibility for IRAs, to make them more generous, and to allow greater flexibility for penalty withdrawal for uses other than retirement.

Restore Pre-TRA IRAs. All taxpayers would be allowed to make deductible contributions to an IRA under the pre-Tax Reform Act of 1986 (TRA) rules. Nondeductible IRAs would be repealed. H.R. 1885, introduced by Rep. Dreier on April 28, 1993 would restore pre-TRA IRAs, but also double the contribution limit (to $4,000) and index it for inflation, and allow penalty-free early withdrawals for first-time home-buyers and for educational and medical expenses.

	Fiscal Year 1995	1996	1997	1998	1999	1995-99
	(Billions of dollars)					
Restore Pre-TRA IRAs (Joint Tax Committee)	-1.3	-6.8	-7.4	-7.8	-8.2	-31.5

Roth-Breaux Proposal (S. 2301, introduced July 21, 1994). IRAs would be universally available, back-loaded "IRA Plus" would be added as an option, and penalty-free early withdrawals would be allowed for first home, education, long-term unemployment, and high medical expenses. The IRA contribution limit would be indexed for inflation. These provisions follow the original Bentsen-Roth proposal. In addition, the Roth-Breaux proposal would increase the nonworking spouse deduction from $250 to $2,000. (S. 1669, introduced by Sen. Hutchinson on November 17, 1993, would also raise the nonworking spouse limit to $2,000, and also make the active participant rule apply separately to each taxpayer.)

	Fiscal Year					
	1995	1996	1997	1998	1999	1995-99
	(Billions of dollars)					
Roth-Breaux Proposal (Joint Tax Committee)	-0.8	-4.0	-4.2	-4.6	-5.0	-18.5

Rollovers to Back-Loaded IRAs. Various IRA proposals (including tow bills introduced by Rep. Grams, H.R. 2434, June 16, 1993 and H.R.3645, November 22, 1993) would allow current balances from existing IRAs to be rolled over into back-loaded IRAs. This provision raises revenue in the budget window, because some income tax is imposed on the rolled over amounts. The proposals differ on whether the full amount rolled over or only original contributions are subject to income tax (the Grams bills only tax the original contributions), and on whether the tax is due at the time of rollover or can be paid in installments (e.g., over four years, as in the Grams bills).

H.R.11: An expanded IRA was proposed in H.R. 11 in 1992, but was voted down by 99% of Republicans. The revenue estimates are below.

	1993	1994	1995	1996	1997	
H.R. 11 expanded IRA proposal (JCT, Sept 14, 1992)	-0.24	.77	-1.4	-1.9	-3.3	-6.2

Future Budget Costs. The Roth-Breaux proposal costs less over the budget period than the restoration of pre-TRA IRAs because of the back-loaded IRA option. However, this option has a higher long-run revenue cost because it effectively increases the IRA contribution limit and because no tax is paid on normal withdrawals from these IRAs. *Proposals with rollover options have even larger long-run revenue costs, relative to their five-year budget costs, because the tax that would have been paid on normal withdrawals from existing IRAs is collected early, in the current budget period.*

NEUTRAL COST RECOVERY SYSTEM

Current Law

Under current law, for regular income tax purposes, depreciable assets other than buildings and structures are generally written off over recovery periods of 3, 5, 7, 10, 15, or 20 years (depending upon their "class life"). An accelerated depreciation method may be used (200 percent declining balance for assets with 3, 5, 7, and 10 year recovery periods, and 150 percent declining balance for assets with 15 and 20 year recovery periods). Residential buildings are written off over 27.5 years, and non-residential buildings are written off over 39 years using the straight-line method. For alternative minimum tax (AMT) purposes, less accelerated depreciation methods must be used.

Proposals

There are several Republican neutral cost recovery proposals that are included in legislation currently pending before Congress. The bills differ somewhat in timing and the treatment of depreciation for AMT purposes, but all include the NCRS fundamentals as proposed by Kemp and Kasten in 1985 -- depreciation amounts adjusted for both inflation (based on a GNP deflator) and an additional 3.5% government subsidized rate of return.

1) Kemp-Kasten "Fair and Simple Tax" Proposal: A neutral cost recovery system (NCRS) was suggested in 1985 as part of the Kemp-Kasten "Fair and Simple Tax" proposal. The proposal allowed taxpayers to increase future depreciation allowances for inflation plus a specified real rate of return (3.5 percent). For example, if the depreciation that would otherwise be allowed on a $100 investment is $33.33 in the first year, $44.44 in the second year, $14.81 in the third year, and $7.41 in the fourth year (for a total of $100 of allowances), and the inflation rate is 3.9 percent, the first year NCRS depreciation allowance would remain $33.33, but the second year's depreciation allowance would be $47.79 ($44.44*(1.039)*(1.035)), and the third year's allowance would be $17.13 ($14.81*(1.039)*(1.039)*(1.035)*(1.035)), etc. The new total allowance would be

The Kemp-Kasten proposal suggested slightly longer recovery periods than were then in effect under the 1981 Accelerated Cost Recovery System (ACRS), and exempted the adjustments from the AMT.

2) Investment Tax Incentive Act of 1993: On January 21, 1993, Rep. Nick Smith (R-MI) introduced H. R. 539, which would amend the Internal Revenue Code to allow the depreciation deduction to be computed based on a neutral cost recovery basis for property placed in service after December 31, 1992. Like the Kemp-Kasten proposal, it would include a real rate of return of 3.5% on top of the inflation adjustment. The bill was referred to the Ways and Means Committee and is awaiting further action.

3) **Private Sector Job Creation and Economic Growth Act:** On April 28, 1993 Rep. Dreier (R–CA) introduced H. R. 1885, which applies the NCRS adjustments to both the current law regular and AMT depreciation schedules, and proposes a phase–out of AMT depreciation preferences. It also includes a 3.5% adjustment on top of inflation. The bill has been referred to the House Budget, Government Operations, Judiciary and Ways and Means Committees.

4) **Putting Jobs and the American Family First Act of 1993 (HR 2434) and Family, Investment, Retirement, Savings and Tax Fairness Act of 1993 (HR 3645):** These bills, introduced by Rep. Grams (R–MN) on June 16, 1993 and November 22, 1993, respectively, would also create neutral cost recovery depreciation. H.R. 2434 and H.R. 3645 replace the 200 percent declining balance method allowed under MACRS with the 150 percent declining method before allowing for the NCRS adjustments. They also apply the NCRS adjustments to AMT depreciation and include a 3.5% adjustment on top of the inflation adjustment. H. R. 2434 has been referred to the House Government Operations, Rules and Ways and Means Committees.

5) **Kasich Plan:** The neutral cost recovery was also proposed by Representative Kasich. His proposal would allow for inflation, add an additional return on top of inflation and change the declining balance from double declining balance to 150% declining balance.

Revenue Estimate:

	Fiscal Year					
	1995	1996	1997	1998	1999	1995–99
	(Billions of dollars)					
Kasich Plan (Senate Budget Committee)	3.0	6.0	5.0	–1.0	–8.0	5.0

This proposal was also analyzed in a March 8, 1994 memo by Jane Gravelle, Senior Specialist in Economic Policy at the Congressional Research Service.

Ms. Gravelle found that the proposal would reduce taxable income by a total of about $900 billion.

The net effect, Ms. Gravelle concluded, would be to increase taxable income by $87 billion in the first five years, but decrease taxable income by $984 billion over a total of 39 years. And that was using only 1994 income levels throughout the time of the analysis.

Analysis

NCRS is really a cynical way of sneaking a tremendous tax cut for businesses into the tax code while avoiding both the restrictions in the 5-year budget cycle and the scrutiny of the American public. As Ms. Gravelle found, the long-run loss of government revenue is tremendous. This would be exacerbated even more in times of high inflation when businesses will realize huge cash flow increases at the expense of the government.

The scheme is designed to be net present value neutral to the alternative of expensing an investment in the year the investment is made (hence the name), but by adding an additional 3.5% return factor above inflation, these proposals give businesses a government subsidy, on top of the favorable tax accounting treatment.

THE WHITE HOUSE

WASHINGTON

October 4, 1994

Dear Editor:

As you know, President Clinton vowed when he came to Washington to make improving the economy the number one goal of his Administration. While there have been reasonable disagreements about the specifics, it is hard to disagree with the results. The deficit is being cut virtually in half, the economy has produced nearly 4.5 million new jobs, trade barriers in Asia, Europe, and the rest of our own hemisphere are dropping, and most of the economic indicators are heading in the right direction. We have more to do, but we have taken major steps forward.

I am greatly concerned that this economic progress is imperiled by the package of proposals unveiled by my former Republican colleagues in Congress last week -- their so-called "Contract with America." My concern is that this proposal, if enacted, would not only retard much of the progress we have made on the economy but represent a major step backwards to the fiscal policies of the 1980's that led to exploding Federal deficits and debt. And if the Republicans regard this not as a serious governing proposal, but simply a campaign ploy, I believe the American people will feel even more cynical about their leaders than they do today.

The "contract" -- crafted by the Republican leadership and signed by most House Republican incumbents and candidates -- calls for a balanced Federal budget, while at the same time advocating over $300 billion in new tax cuts and new spending. Despite the leaders' assertion that balancing the budget can be accomplished at "no cost," the fact is it would require savings of $700-$800 billion over five years. Yet not once does the "contract" identify where the spending cuts would come from to pay for even the new tax cuts and spending increases, let alone to balance the budget. That is over $1 trillion in unpaid promises.

While many good things happened to America in the 1980's, there is one experience we must not repeat -- running up the Federal deficit by providing something for nothing and then leaving it to the next generation to pay for the costs. The American people have paid the price for those policies; the last thing they need is for our leaders to return to them.

As John F. Kennedy said, "To govern is to choose." And your readers deserve to know what the choices are. It is important, for example, for your readers to know that one of the inevitable results of this program would be significant cuts in Medicare, Social Security, or both, as the attached chart shows. Given the prominence of these programs in the budget, the signers of the "contract" cannot simply put these programs off limits and still achieve their other goals -- that is, if they take these other goals seriously.

Enclosed with this letter are four inserts that I urge you read: a White House analysis of the budget effects of this proposal; a White House analysis of its effects on senior citizens; an independent analysis by the widely respected Concord Coalition, the group devoted to deficit reduction run by former Senators Paul Tsongas and Warren Rudman, deeply respected fiscal conservatives; and a series of recent articles and editorials on this issue.

Please examine the materials we have provided. I hope you will contact Dawn Alexander in the White House press office at (202) 456-2100 if you have any questions. And if you share my concerns about the Republican contract, please let your readers know as well. Help us to stay on the path of deficit reduction and economic stability, and avoid a return to fiscal irresponsibility as part of an effort to gain partisan advantage.

Sincerely,

Leon E. Panetta
Chief of Staff

ATTACHMENT 1:

Summary of House Republican Contract
Table 1
Table 2
Table 3

SUMMARY OF HOUSE REPUBLICAN CONTRACT

1. TRILLION DOLLAR COSTS: On September 27, 1994, House Republicans signed a list of promises (increased spending, tax cuts, and a balanced budget) that together will require unprecedented budgetary savings of more than $1 trillion over a five-year period and $1.5 trillion over a seven-year period.

2. AT LEAST AN $800 BILLION HOLE -- WITH NO SAVINGS IN THEIR CONTRACT: The House Republican Contract includes no plan as to how to pay for their plan. None. The House Republican leadership's "cost estimate" document included only "*examples of possible offsets*" that are not actually in the "Contract." Yet, even if one assumed unchallenged that they would do all of these cuts -- *there would still be at least an $800 billion shortfall which would likely increase the deficit. Over a seven-year period, the hole would be well above $1 trillion even with the "possible offsets."* The list of "possible" specific cuts includes: $10 billion in student loans cuts, $7.5 billion in worker training cuts, $3 billion in agriculture and rural cuts, $16 billion in international policy cuts, $50 billion in cuts from Medicare, Medicaid and Retirees). (See Tables 1-3, attached).

3. TAX CUTS: HIDDEN COSTS AND CUTS FOR THE WELL-OFF: Many of the tax cuts proposed are either cuts that benefit the most well-off or tax cuts which are designed to hide the large costs they would cause to the federal deficit.

> *Tax Cuts for the Well Off:* The contract includes a $6 billion cut in the estate tax and a large $56 billion capital gains tax cut -- a tax cut of which over 70% of the benefits go to families making over $100,000. Past Joint Tax Committee studies show that 95% of the benefit of the IRA expansion will go to the top one-fifth of taxpayers. Even the child tax credit is more generous to well-off families than working poor families. A family of four making $150,000 would get $1000 while a family making $17,000 would get nothing.
>
> *Hidden Deficit Costs:* The "Contract" includes at least two tax cuts -- the backloaded, roll-over IRA and the neutral cost recovery system -- which are specially designed to hide current costs and push deficit increases beyond the five-year budget window. **If one accepted this deceptive accounting, these two provisions would constitute a $24.2 billion tax increase on private savings and investment.** Yet, once beyond the budget window, a study by the Joint Tax Committee shows that the IRA plan would lose $30-40 billion over five years, while estimates by the Joint Tax Committee and the Congressional Research Service show the depreciation allowance cost swelling to $40-50 billion over five years past the budget window.

4. MEDICARE AND SOCIAL SECURITY: To balance the budget and pay for their new spending and tax cuts, the House Republicans would have to call for dramatic cuts in either Medicare or Social Security -- and most likely both. *To fulfill their contract by the year 2002 would mean a 20% reduction in Medicare and Social Security -- even if the cuts were just across-the-board, which would include cuts in fighting crime, veterans, education and other important areas. Entitlement cap proposals that focus on the rate of growth would have an ever harsher impact on Medicare. If Social Security were to be exempt from such savings, a 30% across-the-board reduction on Medicare, fighting crime, education and training would be required.*

5. HISTORIC REFRAIN OF FISCAL RECKLESSNESS: The President and Congress fought for and signed a historic deficit reduction plan that is working because it was real and did not use phony numbers. The promise of a panoply of tax cuts for well-off Americans, spending increases and a balanced budget with no specifics is the same recipe that lead to the deficit skyrocketing between 1981-1986, when the Republicans controlled both the White House and the Senate. This is not a period we should go back to.

Table 1
Summary of Budget Affects of House Republican
"Contract with America"
($ in billions, totals over 5 years)

Savings Needed to Balance the Budget		$743.00
Total Revenue Losses and Spending Increases	+	278.80
TOTAL COST		**$1.0218 TRILLION**
Proposed Spending Cuts (As estimated by the House Republican leadership)	-	221.07
TOTAL SHORTFALL		**$800.73 BILLION**

Table 2
Cost of House Republican "Contract with America"
($ in billions)

	5-Year Total
Balanced Budget Amendment *Source: CBO estimate of a 5-year balanced budget schedule. Rep. Armey has proposed balancing the budget by the year 2000.*	$743.0
Tax Incentives for Adoption *Source: House Republican Leadership Estimate*	0.9
Dependent Care Tax Credit for Seniors *Source: House Republican Leadership Estimate*	8.0
$500/child Tax Credit *Source: House Republican Leadership Estimate*	107.0
Modify the Marriage Penalty *Source: House Republican Leadership Estimate*	10.0 (1)
Super IRA	0.0 (2)
Defense *Source: House Republican Alternative Budget, March 1994*	61.1 (3)
Raise Social Sercurity Earnings Limit to $30,000 *Source: House Republican Leadership Estimate*	6.8
Phase-Out 85% Social Security Inclusion *Source: House Republican Leadership Estimate*	17.0
Tax Incentives for Private Long-Term Care Insurance *Source: House Republican Leadership Estimate*	1.3
Cut Capital Gains Rates/Index to Inflation *Source: House Republican Leadership Estimate*	56.0
Neutral Cost Recovery	0.0 (2)
Small Business Expensing Provision *Source: House Republican Leadership Estimate*	3.5
Raise Estate & Gift Tax Exclusion *Source: House Republican Leadership Estimate*	6.5
Restore Tax Deduction for Home Office Expenses *Source: House Republican Leadership Estimate*	0.6
Reduce Congressional Staff by One-Third *Source: House Republican Leadership Estimate*	0.1
TOTAL COST	**$1.0218 Trillion**

(1) Initial documents claimed the marriage penalty would be eliminated, as in the Istook proposal (HR 3851). JCT estimates this would cost $72 billion. Apparently the "Contract" has been altered to only reduce the marriage penalty.

(2) The IRA and Neutral Cost Recovery proposals are both listed as tax increases totalling $24.2 billion. In fact, CRS analysis shows that the cost of the Super IRA would be $8 billion per year. Likewise various JCT estimates of rollover, backloaded IRAs also show yearly costs of $4-8 billion per year. The NCR proposal has been projected by the Senate Budget Committee as costing money within 5 years. In light of these differences, we have simply listed both proposals as cost neutral over the next 5 years.

(3) The description in "Contract with America" repeatedly refers to "strengthening" the defense budget. The House Rep. alternative budget introduced by Rep. Kasich called for a $61.1 billion increase in outlays and a $73.7 billion increase in budget authority. However, in a cost estimate document released by the House Rep.leadership on Sept. 23, 1994, they claim that their defense proposal would have 'no costs.' If this reflects that the House Rep. leadership is in agreement with the Clinton defense budget, the total cost of their proposals would be $61.1 billion less, or $961 billion total.

Table 3
Savings Claimed by House Republican Leadership*

($ in billions)

		5-Year Total
Mandatory Spending		
Student Loan Cuts	-9.56	
Health Cuts (Medicare, Medicaid, Retirees)	-53.16	
Welfare Reform	-40.00	
Total, Mandatory Spending Cuts	-102.72	-102.72
Discretionary Spending		
Crime Prevention	-5.00	
International Discretionary	-16.20	
Agriculture and Rural Cuts	-3.27	
Job Training Cuts	-7.56	
Additional Discretionary Cuts Listed	-58.32	
Overhead Reduction (No specifics given)	-28.00	
Total, Discretionary Spending Cuts	-118.35	-118.35
TOTAL CUTS		**-221.07**
Savings Needed for House Republican "Contract with America"		+ **1,021.80**
TOTAL SHORTFALL		**$800.73 BILLION**

* All savings estimates included are taken as given by the House Republican leadership. The accuracy of these estimates is not necessarily endorsed.

ATTACHMENT 2:

Impact on Seniors
Pie Chart

WHAT WOULD THE IMPACT ON SENIORS AND OTHERS BE?

The Republican House alternative budget requires close to a trillion dollars in savings over the next five years. Even assuming considerable savings in interest reductions, this would require a reduction of $350 billion of outlays by the year 2002.

How would they do it?

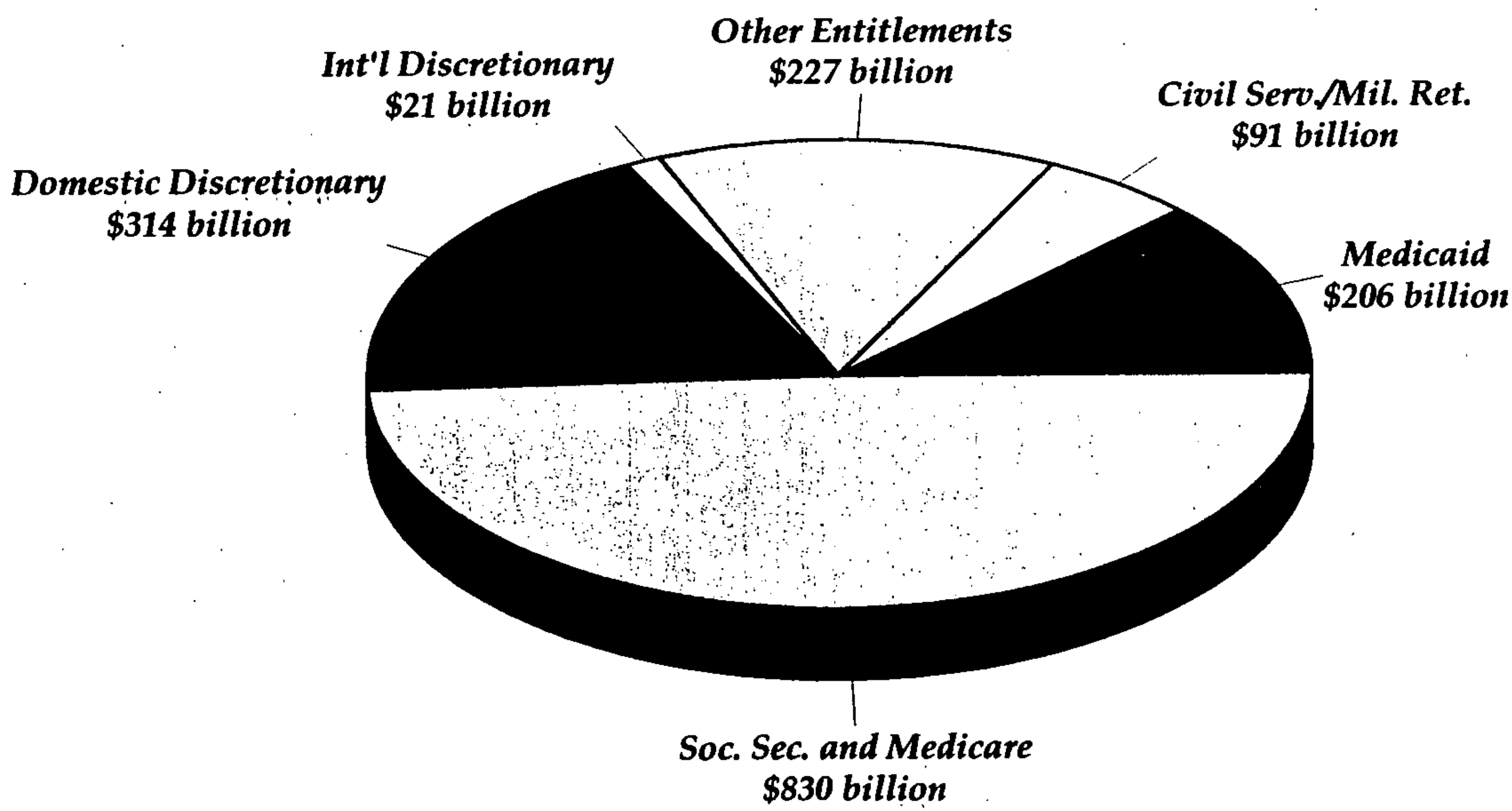
As the House Republicans have given virtually no details on how they would find $1 trillion in savings over five years (or over $1.5 trillion over seven years) or how they would reduce spending by over $350 billion in the year 2002 alone, one can only consider the across-the-board effect. *In this case, there would have to be a 20% across-the-board cut on all spending -- including Social Security and Medicare. If Social Security was to be excluded, there would have to be 30% across-the-board cuts.*

Yet, nearly 50% of the funds available to be cut would be from either Social Security or Medicare so that it is likely that both would have to be subject to dramatic cuts. (See Attached Chart)

The House Republican's "Contract with America" will require $350 *billion* in cuts in FY 2002. Where do you think the cuts will come from?

PROGRAMS AVAILABLE FOR SPENDING CUTS, EXCLUDING DEFENSE

(CBO FY 2002 Projections)



ATTACHMENT 3:

Concord Coalition Anlaysis

THE CONCORD COALITION

CITIZENS FOR AMERICA'S FUTURE

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Budget Update. Vol 2. Number 16 September 28, 1994

SANTA CLAUS FOR CONGRESS?

Overview:

In election years, legislators and politicians who know better often woo voters with promises that both they and their voters know cannot possibly be achieved. As is often the case, if it sounds too good to be true, and it looks too good to be true, it probably IS too good to be true.

The "Contract with America" released by House Republicans on September 27 and the "Agenda for the Republican Majority" released by Senate Republicans on September 21 follow this fine tradition. The Senate document seems to amount to little more than political theater. The House Republicans' "Contract with America" constitutes a set of serious policy recommendations, accompanied by 271 pages of draft legislation and a 41-page summary, that lay out the action agenda they intend to follow next year if they take control of Congress on election day.

Both Republican plans seem to reflect close attention to public opinion polls. Each is jam-packed with attractive proposals intended to draw support from a broad segment of Americans, ranging from middle-income tax breaks, to increased benefits and lower taxes for social security recipients, capital gains cuts, welfare cuts, and tough anti-crime measures.

For now, it is tempting to dismiss these proposals as typical campaign puffery and posturing. It would give cause for concern, however, if the new congress that begins in January actually tried to implement these proposals. Clearly, deficit reduction is not a priority in these plans. These documents are about getting votes, not about balancing the budget. It would also give cause for concern if the Administration, which has started working on next year's budget, tried to "one up" the Republican initiatives. A bidding war to see who can promise the most "goodies" would legitimize political backsliding on the deficit and, if not stopped, could make it virtually impossible to enact deficit reduction. Clearly the Concord Coalition has its work cut out.

Two years ago, presidential candidate Paul Tsongas told the American people that there was no Santa Claus. That's still true today. It's time for politicians to stop pretending to be St. Nick and begin telling voters what tough choices have to be made. Who is going to tell the politicians that there is no Santa Claus?

Analysis:

1. Balanced Budget Amendment:

Ironically, both packages call for amending the Constitution to require a balanced budget. However, a congress that tries to follow these plans will not be a congress that places a high priority on reducing the deficit.

Budget enforcement rules require off-setting deficit reductions to pay for entitlement increases and tax cuts recommended by the Republicans. If several hundred billion dollars of spending cuts are used to pay for the Republicans' agenda, these same policy changes will no longer be available to be used for deficit reduction.

Yet, balancing the budget over five or six years will require deficit reduction of somewhere between $700 and $800 billion over the same period. Concord's *Zero Deficit Plan*, for example, called for $760 billion in deficit cuts from 1995 through 2000.[1] Where should Congress look for $700+ billion in deficit cuts? What do the Republicans recommend? Both Republican plans are silent, except to say that they favor balancing the budget.

The version of the balanced budget amendment advocated by the House Republicans would required a three-fifths majority of the whole number of each House to increase revenues, run budget deficits, or increase the public debt. The balanced budget requirement could be waived by adoption of a joint resolution that the nation "faces an imminent and serious military threat to national security."

2. How to pay for the tax cuts and new priorities:

Both packages offer "ouchless" packages of goodies could lead people to think they could enjoy expanded benefits and tax relief without having to make tough choices. The choices that will have to be made, after election day, will be anything but painless.

The Senate package completely sidesteps hard choices by offering three black boxes of deficit cuts, described as 1) reforming non-social security entitlements, 2) freezing non-defense discretionary spending, and 3) appointing a spending commission to recommend $100 billion of additional non-defense discretionary cuts. Added together, these three black boxes total $432 billion -- about the amount the Clinton 1993 program actually reduced the deficit. Anyone who thinks that $432 billion in loose change can be painlessly shaken from the budget will find out differently when the time comes to open these black boxes.

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[1] Our year by year deficit reduction recommendations totalled $23 billion in 1995, $53 billion in 1996, $97 billion in 1997, $143 billion in 1998, $193 billion in 1999, and $251 billion in 2000.

The House package provides a list of specific deficit reduction "possibilities." The items on this list are, for the most part, plausible and legitimate options that many House Republicans have voted for in fiscal year 1994 and 1995 budget resolutions.[2] However, the *Contract* does not pledge that these spending cuts will be part of the package. It says only that they are "examples of possible offsets."

In the meanwhile, House Republicans are continuing to struggle to define several hundred billion dollars of additional spending cuts that could be offered as part of their budget resolution next year. They should be encouraged in this effort; their task is daunting. Paying for their agenda AND balancing the budget without raising taxes will result in a historical down-sizing of the federal government. The amount of spending they want to cut cannot be produced by merely shaving various programs; it will require a fundamental rethinking and restructuring of the role of a markedly smaller federal government.

3. <u>Deceptive accounting:</u>

The budget projections for the Republican proposals cover 1995 through 1999, the conventional five-year time frame for such projections. However, several "back-loaded" policies contain "time bombs" that will set off large deficit increases in years after the five-year estimating period.

- For example, the IRA-Plus program would reduce the deficit by $4.7 billion (House version) to $14 billion (Senate version) in the first five years because many people would roll over existing IRA accounts into the new IRA-Plus accounts. They would be required to pay back tax breaks they previously received from putting funds into the "old" IRAs, and this influx of revenues would reduce the deficit. However, in the future when retirees withdraw their interest earnings from these new IRAs, they would not be taxed on the interest and revenue to the Treasury would be substantially less under the "new" IRAs than under the "old."

- Similarly, indexing that basis used to calculate capital gains taxes and reducing the tax rate on capital gains create illusionary deficit reductions. These provisions would apply only to investments made after the new law became effective. Therefore, many investors would sell their current holdings, pay the capital gains tax, and then make new investments to which the new law would apply. In a few years, the budget impact of these provisions would swing from mild deficit reduction to major deficit increase.

4. <u>Health Care Reform:</u>

For over a decade, fiscal analysts have realized that federal health care payments were a major contributor to federal budget deficits and that projected growth in these programs, principally medicare and medicaid, would have to be curbed in order to balance the budget.

Health care reform legislation has been pronounced officially dead in the 103rd Congress. But the debate in 1993 and 1994 made it clear that expanding benefits and coverage was far more attractive politically than controlling health care costs.

[2] Not ALL House Republicans were willing to support these cuts. In 1993, 41 Republicans voted no and in 1994, nine Republicans voted no on the Republican budget resolutions.

The Senate Republican's Agenda calls for phasing in "real" health care reform that will build on the current health system to expand access and control costs. They budget a deficit increase of $100 billion over five years for this purpose. The House agenda does not call for health care reform. However, it advocates tax incentives for purchase of long-term health care insurance.

ATTACHMENT 4:

Sample of Nationwide News Analysis of House Republican "Contract"

1. "The G.O.P.'s Deceptive Contract," New York Times Editorial
2. "GOP's 'Let's Make a Deal' is Short on Real Rewards," by David Broder, Los Angeles Times
3. "Aw, C'Mon, Newt," by E. J. Dionne, Jr., Washington Post
4. "The Price of Pandering," by Gloria Borger, U. S. News and World Report
5. "GOP Robs Future to Write 'Contract with America,'" USA TODAY Editorial
6. "The Republicans Shoot an Air Ball," by Al Hunt, Wall Street Journal
7. "Newtspeak," Minneapolis Star–Tribune Editorial
8. "GOP Agenda Short on Specifics," Atlanta Constitution Editorial

New York Times: 9/28/94

The G.O.P's Deceptive Contract

Over 300 Republican candidates for the House of Representatives promised yesterday that, if elected, they will provide a positive new vision for their party and for the country. The body and soul of this vision is to be found in 10 bills they plan to offer in the next session of Congress.

It is a vision that looks backward, Reaganism in a rear-view mirror. What this self-styled "Contract With America" says to voters is that these Republicans do not speak candidly.

Tote up the promises. Led by the minority whip, Newt Gingrich, this group of Republicans would balance the budget while adding to defense spending and cutting taxes on capital gains and Social Security benefits for wealthier recipients. They would also ease the tax burden on non-poor families with children, corporate investment, retirement savings and the estates of wealthy families.

The Republicans, historically a deficit-conscious bunch until Ronald Reagan came along, estimate that their largesse would cost the Treasury about $150 billion over five years. The White House estimates the cost to be about $800 billion. Even the White House estimate may be low.

The Congressional Budget Office says that it would take more than $700 billion in budget cuts over five years to balance the *existing* budget — before the Republicans start hiking defense spending and cutting taxes. The Republicans would keep costs in line by finding fat in Federal programs, though the contract does not say where. In the past John Kasich of Ohio has drawn up bold proposals, but even if Congress adopted every one — a politically preposterous prospect — the Republicans would be hundreds of billions shy of their promises.

The contract is not only reckless but deceptive. The tax cuts on capital gains income, corporate investment and retirement savings are structured to cost little money during the five-year period for which the Republicans do their accounting. But the proposals are certain to pry open gigantic holes in the budget beyond five years.

Nor does the contract reflect a sense of fair play. The cut in the capital gains tax would largely benefit high-income families and, because it would also apply to profits on old investments, is not targeted to stimulate new investment. The tax credit for children would yield nothing to families too poor to owe taxes. The Social Security tax cuts apply only to high-income families. Tax breaks for investment and savings, even if they favor the rich, can be defended. But they would have to be carefully designed to boost productivity and be part of an overall package that spreads tax burdens fairly. By this standard, Mr. Gingrich's compact flunks.

The other bills that make up this vision deal with issues ranging from welfare to crime to long-term health care. Some are good, some bad, but most are presented honestly. That is not true of the economic nostrums. The Republicans ought to admit that their programs would require cutting hundreds of billions out of about $1.5 trillion in Federal spending — thus slicing 20 percent or more out of every program from Social Security to the F.B.I.. Mr. Gingrich promised a positive vision. What voters got instead was duplicitous propaganda.

Los Angeles Times:
9/28/94

GOP's 'Let's Make a Deal' Is Short on Real Rewards

■ **Congress:** Their 'contract' of bills is fine, but Republicans will have to sell it, not just run against Clinton.

By DAVID S. BRODER

There were two very good things about the ceremony on the Capitol steps that House Republicans staged Tuesday; a slew of other things undercut its virtues.

In case you missed it, more than 300 Republican candidates for the House of Representatives—incumbents and challengers alike—signed a "contract" with the American voters pledging to bring 10 bills to a vote in the first 100 days of the 1995 session if they win a majority in the November election. The measures include a balanced-budget amendment, a variety of tax cuts, welfare reform, tort reform and term limits—a set of measures that enjoys broad public support.

The first commendation goes for helping voters understand what is at stake in the midterm voting. The Democrats, clearly on the defensive, want to reduce the election to 435 individual contests devoid of national significance, hoping that their incumbents can fend for themselves even in a

'The House needs a good shot of *perestroika*. After 40 years in the majority, the Democrats have become too adept at bottling up bills in committee.'

hostile environment. But, as House Minority Whip Newt Gingrich (R-Ga.), one of the organizers of Tuesday's event, said at a press briefing, "Our government operates on the party system. We are a team. And we're offering you a contract on what our team will do."

That is a sound proposition. People need to be reminded that Congress writes the laws in a partisan setting (except on a few international issues) in which the opposing parties divide, not just for spite, but on philosophy, program and principle.

House Republicans earned their second medal by promising that each of their priority measures will be brought to the floor "under an open rule (allowing consideration of all serious amendments and substitutes) for full and honest debate." As Dick Armey of Texas, the House Republican Conference chairman, said, "That does not guarantee all 10 of these measures will pass," but it does promise that measures with broad public support will have an airing and receive a vote.

The House needs a good shot of *perestroika*. After 40 years in the majority, the Democrats have become too adept at bottling up bills in committee (as they've done with tort reform and term limits) or bringing them to the floor under such restrictive procedures (as they did last year with campaign-finance legislation) that consensus becomes impossible.

When Tuesday's ceremony was conceived months back, it seemed little more than a campaign gimmick. But now there appears to be at least an outside possibility that Republicans could gain the 40 seats needed for a majority. Their commitment to full and open debate on broadly supported measures is important.

Beyond that, however, the Republican exercise raises more questions than it answers. It's fine for them to talk about positive programs at Washington TV extravaganzas, but across the country, their candidates seem to be running, not for any policy, but against President Clinton. Their favorite tactic is a TV ad that electronically blends the opponent's face with Clinton's, as nice a piece of high-tech demagoguery as you can find. If they think their program is right, they can prove it by running on it.

But the program is full of holes—starting with more tax breaks for the wealthy and that balanced-budget amendment. At the White House last week, Chief of Staff Leon Panetta, a former chairman of the House Budget Committee, called the GOP on its "snake-oil approach," challenging Gingrich & Co. to spell out where they would find the $743 billion in savings needed to balance the budget in the next five years, let alone finance the new tax-cut bonbons they propose to hand out.

Two days after Panetta's challenge, Gingrich and Armey brought Ohio Rep. John Kasich, the GOP's most credible budget strategist, to a briefing to answer Panetta, but he didn't do it. Kasich detailed about $148 billion in claimed savings from the 100-day program, but then fell into the kind of generalizations that raise warning flags. "We're going to reinvent the operations of the federal government," he said, as if Al Gore did not hold the copyright on that cliche. "There are whole agencies that should be privatized, whole programs that should not exist."

Gingrich labeled the Panetta argument "outrageous . . . absurd," and with a real show of indignation, said it proved that Democrats could not grasp how "the dumbest large institution in America," which is his description of the federal government, "can be radically reformed." His example of such a reform would be to change the "informed consent" requirement in existing law so patients suffering a heart attack could be treated with a European-invented CPR device that he said works four times as fast as American manual techniques. "The total savings would be significant," he said.

It would be wonderful if we could balance the budget by improved CPR techniques, while cutting taxes at the same time. But it sounds suspiciously like the fairy-tale economics of the 1980s, which landed us in this budgetary mess.

Do Republicans really want a referendum on that?

David S. Broder is a syndicated columnist in Washington.

E. J. Dionne Jr.

Aw, C'mon, Newt

THE WASHINGTON POST TUESDAY, SEPTEMBER 27, 1994

The GOP can do better than this exercise in election-year cynicism.

In this fall's elections, the Republicans could play a constructive role by asking voters to make some choices about what they want government to do and how much it should cost. Unfortunately, it looks like the Republicans won't be running that kind of campaign at all.

Instead, they will be talking in a lot of detail about tax cuts and improving our military and rather little about what other spending they might junk to pay for this program. If you think this seems suspiciously like a slightly grainy videotape replay of Republican campaign commercials from 1978 and 1980, you're right. "I'm willing to pit Reagan vs. Clinton," GOP House Whip Newt Gingrich told reporters last week. "You choose." Gingrich, who prides himself on looking forward rather than back, figures it's safer to try to win one more for the Gipper.

The shame of this is that Gingrich's idea of having Republican House candidates commit to a "contract with America" at a news conference today is daring and might have been useful. Some of the Republican ideas—on tax credits for families with kids, stricter enforcement of child support payments by absent fathers and welfare reform—are certainly worth debating.

But overall, their program seems to assume a cynical electorate that won't ask many questions about how the goodies in the package are to be paid for. The Republicans would cut taxes on families with kids, roll back the tax on higher-income Social Security recipients passed last year, modify the tax penalty on married people and cut the capital gains tax. They'd let people on Social Security earn more money without sacrificing benefits, further increasing government outlays. And they'd "strengthen defense."

How would they, then, balance the budget? Why, by passing a constitutional amendment requiring a balanced budget and giving the president the line-item veto. Nifty. Specifics on the tax cuts, gimmicks on the spending cuts. The Congressional Budget Office figures it would take about $750 billion to get the budget balanced in five years. If the Republicans really support the balanced budget amendment, where will they get the money to balance the budget?

The Republicans have issued a list of "possible offsets"—note the "possible"—to pay for their program, some of them highly questionable, especially $28 billion in "overhead reductions." But at best, these cuts cover only the near-term costs of the Republicans' tax promises; they don't even begin to close the budget deficit. Are the Republicans serious enough about even these cuts to add them to their "contract"?

It's no wonder that the Clinton administration has had a grand time briefing everyone in sight about the Republican program. President Clinton has his problems, but he's made difficult budget choices—to the point where he's constrained his ability to finance his own new programs.

The Republicans need to do better. At today's news conference, Gingrich and buddies could start by pledging to produce an honest list of spending cuts that would balance the budget in accord with their constitutional amendment—and to put it out well before Election Day. Please, guys, don't tell us that economic growth will solve all the budget problems. You tried that a few trillion dollars of deficits ago. And don't give us vague talk about "entitlements" and "welfare" and "waste." To paraphrase a famous Republican: What will you cut and when will you cut it?

The truth is that the Republican Party has three perfectly honorable ways to approach the electorate that would be entirely in keeping with the party's philosophical orientation. If Republicans want to be the low-tax, small-government party they claim to be, they need to be candid about how much they'd have to cut Social Security, Medicare and other big, popular programs to get there. This would permit a genuine debate about the size of government—and force the country to come to terms with how much federal money goes to a rather small list of purposes.

Alternatively, Republicans could tone down their rhetoric and argue that their real purpose is not to slash and burn but simply to keep things pretty much as they are—no huge cuts, no big new programs. In Germany, the Christian Democrats ran for years on the slogan "No Experiments." That's a fairly good definition of prudent conservatism. It's not flashy, but it has the benefit of being true to what the Republicans actually do in office. Most Republicans don't seem to want to cut government programs for the elderly or for farmers or for veterans or for business or for middle class school districts or for the military. Why don't they just say so and stop pretending that small government is just around the corner?

The third alternative, which could be combined easily with the second, is for Republicans to focus as much on how government does things as on what it does. They could steal some of Clinton's New Democrat clothes by saying they recognize some of the same problems as Democrats do but have different approaches to solving them.

For example, the Heritage Foundation was willing to spend rather a lot of government money to give the uninsured vouchers to buy health insurance. That's quite different from building a big bureaucracy. A lot of Republicans talk about school vouchers to give more kids a chance to go to private schools. But how would

they do it and where would they raise the money—or are they just saying that states should try this if they want to? More generally, Republicans might ponder the suggestion of William A. Schambra, a senior program officer at the conservative Lynde and Harry Bradley Foundation, that many social problems would be better solved through families, neighborhood groups, churches and other institutions outside of government. That's an interesting idea. But how, exactly, could it be done?

Unfortunately, the Republicans aren't even close to grappling with such noble thoughts right now. They want to win by tossing around tax cuts and term limits and hope that Clinton does the rest. C'mon, Newt, you used to be a lot more interesting than that.

U.S. News & World Report
10/3/94

ON POLITICS

BY GLORIA BORGER

The price of pandering

Newt Gingrich and the gang long ago figured out that the media often mistake sound and fury for news. So to help fire up their conservative insurrection, they attacked Democratic Papa Bear Tip O'Neill, toppled House Speaker Jim Wright, openly shunned moderate Senate Republicans and pioneered the use of C-SPAN as their personal studio. Back in 1979, when master of ceremonies Newt was new, there were 158 Republicans in the House of Representatives. They mostly lived a quiet life, predictably opposing Democratic taxers and spenders. Now, there are 178 Republicans, and they sense a new opportunity: a real shot at winning effective control of Congress. They can hardly contain themselves.

Their latest production is a grandly orchestrated and carefully planned photo opportunity. The script calls for Republican House incumbents and wannabes to pose together on the Capitol steps this week and unveil a neatly packaged "Contract with America," a set of 10 promises that they pledge to vote on within 100 days *if* they win control of the House. The Capitol is an odd backdrop for candidates who are trying to pose as outsiders, but then their contract is a bit less revolutionary than it appears.

For one thing, the Republicans do not actually promise to pass anything; that would smack of governing, which they eschew. "We are saying we know you don't like politicians, and we are drawing a distinction between us and them," says Republican pollster Frank Luntz. But in the best tradition of cynical modern politics, Luntz pretested the GOP's principles on selected focus groups before Gingrich unveiled them.

Sound and fury. *GOP leader Gingrich feeds the press.*

Even if the public buys his pitch, Republicans may come to regret it.

Golden oldies. The Republicans' message is Gingrich at his clever best: Dream up a Christmas list and paste it to the refrigerator. If we don't deliver, the House Republicans say, throw us out. "This is the first time a group of political candidates have gotten together to sign on the dotted line," says Luntz. The ploy would be a political coup, except for one problem: Gingrich's list is just a collection of GOP golden oldies that pander to the public's desire to get something for nothing—the balanced-budget amendment, a middle-class-tax cut, a capital-gains-tax cut, term limits, the repeal of some Social Security taxes along with the marriage penalty and tough welfare reform.

Gingrich promises to deliver all these goodies without cutting defense or Social Security. Republican cost estimates have inched upward with every new inquiry, but the latest is a relatively modest $140 billion over five years—an amount Republicans argue can be financed with digestible cuts in social spending and revenue gains. "We can pay for this, and we will do it," insists GOP budget entrepreneur John Kasich. In an internal document prepared to rebut the GOP, the Clinton administration reckons the cost at more than $1 trillion. "Not only are they not close," claims one administration official, "they're not even close to close."

Just balancing the federal budget by the year 2000 would require about $700 billion in new budget cuts or tax increases. And Republicans themselves concede that raising the per-child income-tax credit to $500 would cost $100 billion, and a capital-gains-tax cut an additional $56 billion. Another GOP idea, repealing the recent congressional decision to tax some benefits paid to the wealthiest 13 percent of all Social Security recipients, would add $21 billion to the tab over the next five years.

Add a dose of hypocrisy to the questionable math: The same Republicans who rail about ending an "unfair" Social Security tax on the wealthy are proposing to do essentially the same thing with Medicare, reducing some benefits for those whose retirement income exceeds $100,000 a year. Well-off seniors who think Gingrich & Co. are giving them a break ought to think twice: With a balanced budget and no defense cuts or tax increases, the money has to come from somewhere.

Small wonder that Senate Republicans, who recognize that leadership occasionally requires taking responsibility, have decided to pass up this contract. "It's a reflection of people who have never governed," says one GOP moderate. "Our leadership wouldn't let serious people sign on to something like this." Even some House Republicans who hate term limits are fidgety. Still, they took the pledge because it merely promises a vote; they didn't have to say *how* they would vote. It is the sort of pre-election stunt that should make them cringe.

It probably won't. "This is designed to appeal to every American who believes in a strong family and creating jobs and who want a healthy and growing economy," says Gingrich. But even if the public buys his carefully aimed pitch in November, his fellow House Republicans may come to regret it. The voters, after all, might actually make them honor their contract. ■

GOP robs future to write 'Contract with America'

OUR VIEW **Another name for the Republican plan is 'fiscal irresponsibility.' Don't fall for it.**

Republicans had a a great idea Tuesday: Define specific goals, commit candidates to them, promise action within 100 days.

Voters might finally have had an honest choice between paying more or getting less.

Unfortunately, the GOP blew it, choosing instead to offer up yet another course of all politicians' favorite meal: free lunch.

More than 300 Republican House candidates, led by wannabe House speaker Newt Gingrich, signed a "Contract wi   America" on the steps of the Capitol.

Among the vows: to vote for term limits, a balanced budget amendment, a stronger defense and tax cuts, tax cuts, tax cuts — all to be acted upon if Republicans win the House in November. They need 40 more seats to gain control for the first time in 40 years, a stiff challenge.

But the big trouble with the contract isn't that the GOP might not have the votes; it's that the Republicans might win control and try to keep their promises, which to put it bluntly are a con.

What's wrong with a contract promising to cut taxes, strengthen defense and balance the budget?

Look at recent history.

In 1980, Ronald Reagan led a Republican victory by offering the same politically delectable menu. Republicans took control of the White House and Senate. They cut taxes. They hiked defense spending. They said — knowing full well it was baloney — that economic growth spurred by the tax cuts would pay the bill and balance the budget.

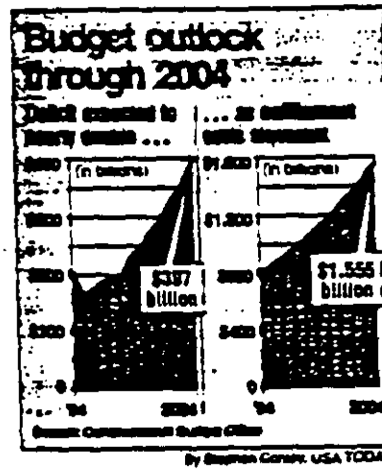
Voters signed on. Who doesn't like something for nothing?

The painful and by now well-known result: deficits soared — adding $3 trillion to the national debt in 12 years, $12,000 for every American.

Finally, Congress, with President Bush in 1990 and President Clinton last year, took steps to stem the flood of red ink. The latest action — a $500 billion, five-year deficit reduction plan in 1993 — finally is pushing the deficit under $200 billion.

But the relief is only temporary. Without further action, skyrocketing health care, Social Security and other entitlements will swell the deficit to almost $400 billion in 2004. And by 2012, entitlements and interest on the national debt will eat up every dollar the government collects.

Then, if the government wants to buy a tank or pay a soldier, build a road or investigate cancer, keep tabs on our borders or put crooks behind bars, it will have to borrow money — $700 billion a year just for the jobs most Americans expect their government to perform. Taxes will soar.



Even as rich a nation as this one can't afford that massive a hemorrhage of debt.

Responsible Republican House candidates could have done voters a favor by proposing program cuts and/or tax increases that attacked the deficit today, before it starts climbing again.

Instead, Gingrich and Co. decided to replay 1980's fiscal games. As Reagan did in 1980, these opportunistic House candidates say they want a balanced budget amendment — but one that wouldn't take effect for eight long years.

Reagan kept right on saying he wanted the amendment through his eight years in office. But never once did he propose a balanced budget to Congress. The political costs of honesty were too high.

And what would likely happen in the next eight years under the Republican contract? Between 1996 and 2001, the tax cuts they've promised would strip $200 billion from the treasury — swelling deficits already expected to total $1.05 *trillion*.

Oh, these modern taxcutters promise to make up for the revenue losses. But their list of possible cuts total only $240 billion over five years. And many are dubious.

They count on $19.5 billion by selling the air traffic control system to airlines. Will they sell the Food and Drug Administration to drug makers next?

And they claim limiting welfare to two years will save $40 billion over five. But what happens when many of those people, mostly women, can't get jobs? Orphanages to care for their kids won't come cheap.

Any way they slice it, the GOP's Contract with America has a trillion dollar hole in it. And budget tricks and promises of economic growth simply will not fill it in.

Gingrich is fond of saying the country needs a new paradigm for action. Maybe so. But what he offers is the same old fraud.

Like 1980's free lunch, this one promises a huge bellyache later.

▶ GOP program, 4A

USA Today: 9/28/94

Wall Street Journal

9/22/94

The Republicans Shoot an Air Ball

Politics & People

By Albert R. Hunt

In 1980 a freshman Republican convinced the senior leadership that all GOP congressional candidates should gather at the Capitol to embrace presidential nominee Ronald Reagan's agenda, whose centerpiece was an across-the-board tax cut.

It struck a responsive chord as voters, reeling from the inflation-ravaged '70s, were looking for radical change; the GOP tax cuts, coupled with promises to deregulate the economy and take on the Soviet Union, made for a serious agenda.

House Republican candidates will try to repeat this show next Tuesday when they take to the Capitol steps to rally behind a "Contract With America," an agenda the GOP pledges will be debated and voted on in the first 100 days of the 104th Congress. The young freshman who conceived the rally 14 years ago, Newt Gingrich, could be the GOP speaker in that Congress.

But this time, despite the high-blown rhetoric, the Republicans are offering more of the same: tax cuts for the affluent, budget promises that don't add up, and political reforms they don't mean -- rather than any radical change. With this contract, voters ought to demand a money- or representative-back guarantee.

There are some good ideas, such as a line-item veto and placing limits on legal damages. But the political and policy centerpieces -- economic and institutional reform -- are frauds.

Although the full details aren't out, the White House and congressional Democrats are having a field day costing out the draft proposals; they don't begin to add up. The GOP contract will promise a balanced budget constitutional amendment, but also some $200 billion of tax cuts over the next five years and higher defense spending. How will we get there? Blue smoke and mirrors.

Republican legislators insist the tax cuts will be financed by spending cuts proposed by the GOP in the House Budget Committee last year. But they would need $700 billion more in cuts to reach a balanced budget in five years, as advocated by Rep. Dick Armey, a leading force behind this "contract." This from politicians who say they aren't going to touch Social Security or raise taxes.

What's more, some of the most important measures are dubious tax and social policy. For political reasons the Republicans won't propose rolling back last year's tax hikes on wealthier Americans, conveniently forgetting all the horrible consequences they proclaimed would occur from the increase. Instead they try to camouflage goodies to upper-income taxpayers.

The biggest tax break would be a $500 tax credit per child for all families making up to $200,000 a year. Since it's not refundable, it wouldn't help low-income taxpayers. Thus, a couple with four kids making $190,000 would subtract $2,000 from their taxes, but a couple with four kids making $19,000 would get nothing. The point of any children's allowance ought to be to help families cope with financial burdens; it's surely an upside-down social policy when it's not paid primarily to those with the greatest need. This initiative would cost $25 billion a year.

The Republicans do vow to repeal the Clinton tax hikes on more affluent Social Security recipients. Under the 1993 budget measure an elderly couple making more than $44,000 has 85% of all Social Security benefits taxed. That's up from 50% but still 15 percentage points below the way ordinary income is taxed. Now, there's no way to deal seriously with the long-term deficit threat without tackling entitlements. Yet these politicians, who gutlessly want to give higher-income retirees a $5 billion-a-year tax break, insist they're going to write a balanced budget into the Constitution.

There's sleight-of-hand, too, starting with a proposal to expand individual retirement accounts. If you make under $40,000 a year, as two-thirds of taxpayers do, and don't participate in an employer-sponsored pension plan you now can take a $2,000 IRA deduction. The GOP wants to restore IRAs to taxpayers making more than $10,000, although the most reliable studies show that when IRAs were available to higher-income taxpayers they didn't increase net savings but merely shifted them around.

The House Republican agenda for 1994 includes offering term limits of six years for House members and 12 years for senators. Here's the number of years that GOP leaders have themselves served:

HOUSE	
Newt Gingrich, *Minority Whip*	16 years
Robert Walker, *Chief Deputy Whip*	18 years
Dick Armey, *Chairman, House Republican Conference*	10 years
Bill McCollum, *Vice Chairman, House Republican Conference*	14 years
Henry Hyde, *Chair, Republican Policy Committee*	20 years
SENATE	
Robert Dole, *Minority Leader*	26 years
Alan Simpson, *Minority Whip*	16 years
Thad Cochran, *Chairman, Senate Republican Conference*	16 years
Don Nickles, *Chairman, Senate Republican Policy Committee*	14 years

Moreover, the taxpayer, instead of getting a tax break when the money is deposited into the account, would get the interest tax-free on withdrawal. That avoids a short-term deficit, as revenue losses would come later. There would be a similar backloaded effect from more generous depreciation write-offs for businesses in the GOP proposal. Add about $10 billion to $12 billion a year to what will be required to balance the budget.

The Republicans are equally disingenuous on congressional reform. Again, there are a few good ideas, including cutting the numbers of committees, and term limits for committee chairmen. But the essence of the Republican change is an ethical housecleaning. Well, the House already has passed legislation subjecting it to most federal laws, and, on ethics, House Democrats have toppled their own speaker and removed the chairman of the House Ways and Means Committee after he was indicted; by contrast, Rep. Joe McDade is still the ranking Republican on the Appropriations Committee more than two years after he was indicted.

Then there's the promise to "allow consideration" of a six-year term limit for House members and 12 years for senators. Privately some leading House Republicans whisper the term-limits drive will lose steam if the GOP becomes the majority. They better hope so, for it would wipe out the entire Republican leadership in both houses. Republican National Chairman Haley Barbour insists this is on the level: "Is it hypocritical for Democrats to attack soft money and PAC contributions and then take them?" You bet it is, Haley, and the GOP term limits proposal is just as duplicitous.

The Senate GOP, led by Bob Dole, whose 26 years in the Senate followed eight in the House, offered a less specific agenda yesterday that omits term limits. But it does promise tax cuts, higher defense spending and a balanced budget amendment.

With these proposals the congressional Republicans will become the New York Knicks of 1994 politics: great on defense, when assailing President Clinton and the Democrats, but pathetically inept when they have the ball.

Newtspeak

Will voters swallow Reagan redux?

With President Clinton's pitch to Minnesotans Saturday and Tuesday's unveiling by Newt Gingrich and Co. of "Contract With America," choices in this fall's congressional elections become well-defined. The choice is especially clear in the contest for the U.S. Senate. While Minnesotans will be choosing between Ann Wynia and Rod Grams, they'll also be choosing between Gingrich and Clinton.

Gingrich's "Contract With America" is a twin to Grams' fiscal program. The central themes boil down to tax cuts, increased defense spending and a balanced budget. That's the same "supply-side" program which got Ronald Reagan elected in 1980 and produced $3 *trillion* in federal debt. It also led to what Business Week calls the "widest rich-poor gap since the Census Bureau began keeping track in 1947," a gap that is tearing hard at the American social fabric. The Grams-Gingrich plan would stretch that gap. A central proposal is a $500 family tax credit for each child. But because the credit isn't refundable, a family with four children earning $19,000 would get nothing while a similar family with 10 times the income — $190,000 — would get $2,000.

The bad effects don't stop there. The Republicans propose total tax cuts of $200 billion over five years. They also propose up to $60 billion in new defense spending. Add those to the balanced-budget pledge, and Republicans need between $800 billion and $1 trillion in spending cuts. They don't tell you where those cuts will come from — except that Social Security and other middle-class entitlements will be off-limits.

The Democrats, meanwhile, have their own story to tell — one that belies the "tax and spend" label Republicans try to stick them with. Last week came a report that the current deficit has fallen substantially this fiscal year and may end up at about $200 billion, $35 billion below predictions. Economists credit economic growth and Clinton's 1993 deficit reduction program. As the president observed Saturday, this marks three straight years of deficit reduction for the first time since Harry Truman.

As Clinton also observed, the country now has the smallest federal bureaucracy since John Kennedy. Yet that pared-back bureaucracy managed to work with the congressional Democratic leadership to pass, in less than two years, the stalled Brady Bill, the stalled crime bill, the stalled Family and Medical Leave Law, the North American Free Trade Agreement, a fledgling national service program for young people, expanded Head Start eligibility, an aggressive immunization program, tax cuts for small business, $255 billion in spending cuts and more. Unless Senate Republicans obstruct again, Clinton also soon will win passage of an important new free-trade agreement, the Uruguay Round GATT, that will further enhance the competitiveness of American business in the world market, where the United States this month once again was pronounced the world's most productive economy.

Those are the options this fall — a rerun of Reaganomics from House Republicans or Clinton's centrist, reasonably successful economic program. From here, the choice doesn't seem difficult. If the Republicans wish to be taken seriously, they'll need to do better.

Minneapolis Star-Tribune

9/28/94

THE ATLANTA CONSTITUTION

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GOP agenda short on specifics

Congressional Republicans are offering an agenda of legislation they would enact if the GOP takes control of the House and Senate in the Nov. 8 elections. So far, the proposals look like Voodoo Economics, Part 2.

Senate Republicans weighed in last week with a seven-point plan that includes a constitutional amendment mandating a balanced budget and pledges to cut the capital gains tax, double the income tax exemption for children and repeal last year's tax hike on the wealthiest Social Security recipients. They would do all that while increasing defense spending.

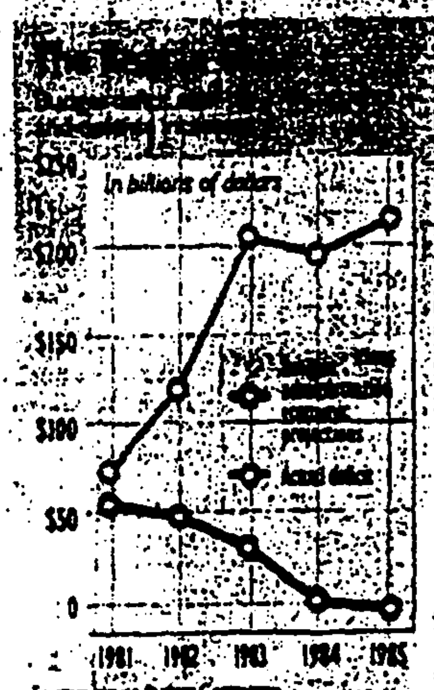
House Republicans, led by Minority Whip Newt Gingrich, are expected to include similar pledges when they unveil their "Contract With America" Tuesday on the Capitol steps.

Of course, Gingrich's agenda for the first 100 days of a Republican Congress has already been tainted by the disclosure that he offered prospective contributors to his $2 million-a-year political action committee the opportunity to have input in the legislative program.

But the main problem with the Republican plans is that they have offered no concrete proposal for paying for them. "We're going to pay for all of our tax cuts by cutting government spending," Sen. Phil Gramm of Texas said in outlining the Senate plan. "We're for real on these issues."

To paraphrase Ronald Reagan's comment in a 1980 debate with Jimmy Carter: There they go again.

The Republicans are continuing a familiar pattern: They refuse to list specific spending cuts for fear of alienating a politically powerful constituency, and they claim that economic growth will ride to the rescue.



WILSON LOWREY / Staff

Reaganomics held out the promise that one could cut taxes, raise defense spending and lower the budget deficit all at the same time. Instead, the country was saddled with spiraling budget deficits that are only now being brought under control.

Due to continued economic recovery and disciplines imposed by the 1993 Clinton economic plan, the 1994 budget deficit could well dip to below $200 billion. Government red ink seems finally to be on a downward slope. But much more cutting needs to be done.

If the Republicans are serious, let them offer specific plans for drying up the remaining red ink.

To do that, they will have to name names of politically popular programs they would cut.

THE WHITE HOUSE

WASHINGTON

November 11, 1994

MEMORANDUM TO THE PRESIDENT

From: Gene Sperling

Subject: Summary of House Contract and Senate Pledge

Leon asked me to give you a summary of the proposals -- particularly the tax and budget proposals -- within the House Contract and Senate Pledge. There is far more detail on the House Contract -- which included legislative language -- while the Senate pledge was quite vague.

I have not had a chance to vet this memo with all of the members of the economic team, so I have just tried to note some basic analytical issues, as well as some budgetary and revenue aspects that we have worked on with Treasury and OMB. Certainly, other members of the economic team will have other thoughts and comments for you during the budget process.

HOUSE CONTRACT WITH AMERICA

The Contract With America contains two sets of promises. First, the Republicans promise to enact a series of procedural and rule changes within the House of Representatives on the first day of the 104th Congress. Second, they promise, within the first 100 days of the Congress, to bring to a House vote 10 major pieces of legislation. While they have promoted this across the nation as an agenda to pass, they have built weasel room into their fine print by claiming that they have only obligated themselves to put it up to a vote. Section I lists the Opening Day reform promises; Section II discusses the major tax and budget aspects of the Contract; and, Section III outlines the remaining aspects of the Contract's legislation.

SENATE PLEDGE

The Senate pledge, "7 More in '94," is comprised of seven broad proposals, including a balanced budget amendment, an increased tax exemption for children, welfare and health care reforms, and anti-crime measures. Unlike their House counterparts, the Senators included no specific legislation in their agenda. Section IV describes the Senate proposals.

APPENDIX

Section V is an appendix which includes budgetary cost estimates the NEC prepared of the House Republican Contract, as well as a short summary and chart of the effect of the entire Contract on Seniors.

I. HOUSE CONTRACT OPENING DAY PROMISES:

1. Apply major national work standards and rules to Congress, including: the Fair Labor Standards Act, Title VII of the Civil Rights Act of 1964, the Americans with Disabilities Act, the Occupational Safety and Health Act, and the Family and Medical Leave Act.

2. Require that any bill which increases revenues be passed by a three-fifths super majority of Members voting.

3. Change baseline budgeting by eliminating adjustments of discretionary appropriations for inflation.

4. Reduce committee staff by one-third, realign and significantly reduce the number of standing committees, abolish most joint committees and limit all committees except Appropriations to 5 subcommittees.

5. Limit the terms of committee chairs to a maximum of three consecutive Congresses.

6. Ban proxy voting in committees and subcommittees.

7. Increase public access to committee and subcommittee meetings by limiting which meetings can be closed and increasing the access of print and broadcast journalists.

8. Select an independent auditing firm to conduct a comprehensive audit of the House of Representatives' financial records, physical assets and operational facilities.

II. MAJOR TAX AND BUDGET ASPECTS OF THE CONTRACT:

Below is a summary of the portions of the House Contract which include the major tax and budget changes. Most of these are included in four of their ten pieces of legislation: *1.) The Fiscal Responsibility Act* (balanced budget, line item veto); *5) The American Dream Restoration Act*; (child tax credit, expanded IRA, partial repeal of marriage penalty); *7) The Senior Citizens Fairness Act* (lift earnings limit to 70, and repeal 85% threshold for Social Security), and *8) The Job Creation and Wage Enhancement Act*, (capital gains tax cut, neutral cost recovery, small business incentives, etc).

After running through the major tax and budget provisions, this memo briefly mentions the provisions in the six other bills of the Contract.

1. BUDGETARY REFORM (THE FISCAL RESPONSIBILITY ACT)

(1A): Balanced Budget Amendment: The proposed balanced budget amendment requires that the federal budget be balanced by FY 2002 or by the second fiscal year after its ratification, whichever comes sooner. It also would require any bill that increases revenues to pass each House of Congress with a three-fifths majority of its members.

Analytical Notes:

- **Three-Fifth Majority for Revenue:** The Simon-Stenholm Amendment does not call for a three-fifth vote for revenues -- and Simon will be opposed to a constitutional amendment that has such a restriction on raising revenues.

- **Effect on Capital Gains and Dynamic Scoring:** Ironically, since they like to describe their capital gains proposals as raising revenues, it seems to me they have made a trap for themselves. If they claim that their proposals raise revenues through dynamic scoring, they will be subjecting their own proposals to a three-fifth scoring.

- **Social Security:** While some balanced budget amendments have specifically excluded Social Security from consideration in the balance calculation, this proposal does not. Yet, it is worth noting that excluding Social Security would make the budget more difficult to balance since the size of the deficit would not be masked by the Social Security surplus

- **Size of Deficit Reduction Plan Needed:** The Congressional Budget Office has estimated that balancing the budget over a seven year time frame would require reducing spending and increasing revenue by a total of $743 billion and the Concord Coalition has confirmed that estimate. Over a seven year period, an evenly phased in plan would require a $1.2 trillion deficit reduction plan.

(1B). Presidential line-item veto over appropriation bills and targeted tax benefits in revenue bills.

This bill would give the President the authority to rescind all or part of any discretionary budget authority or veto targeted tax benefits within revenue bills if the President determines that the rescission or veto would:

1. help reduce the federal budget deficit;

2. not impair any essential government functions; and

3. not harm the national interest.

The President must notify Congress of the veto or rescission within 20 calendar days. Congress would have an additional 20 session days to review the President's action, during which time it could pass a rescission/receipts disapproval bill, that, if enacted, would restore the removed provision(s).

5. **THE AMERICAN DREAM RESTORATION ACT**: This is their middle class tax fairness provision. It has three parts: A) a $500 child tax credit; B) begin repeal of the marriage penalty; C) and an expanded IRA.

(5A): $500 per child tax credit: The Contract calls for a $500 tax credit per child under age 18 in families with income up to $200,000. The tax credit is gradually phased out for families with income in between $200,000 and $250,000. This is essentially the proposal that Rep. John Kasich offered in his 1994 Republican budget alternative in March, 1994.

<u>Analytical Notes:</u>

Unnecessary Regressivity: Because the proposed child tax credit is available for families making up to $200,000 and because it denies any refundability to families with low tax burdens, the proposal would lead to serious inequities to working families. For example, a family with two children making $150,000 would get a tax cut of $1000. Yet, a similar family of four making $20,000 would get no tax benefit whatsoever because they would not have taxable income to offset.

House Republicans Opposed a Child Tax Credit in 1992 and 1993: In 1992, 99% of Republicans voted against a child tax credit and an expanded IRA simply because the program also included a tax increase on the top 1.2%. In 1993, 100% of Republicans voted against a budget with a dramatic expansion of the Earned Income Tax Credit largely, again, because of tax increases on the top 1.2% -- those making over $180,000 adjusted gross income.

(5B). Begin to repeal the marriage penalty: In the preliminary papers on the Contract that the House put out, they called for elimination of the marriage penalty. This was apparently based on legislation by Congressman Istook that called for allowing joint filers to choose whichever filing status they found most beneficial. They had clearly not thought through all of the gaming this would lead to or the cost. When Gephardt asked for scoring of the Istook bill, the cost came out at $71 billion. At this point, the House Leadership backed off their proposal, and changed their proposal from "repealing" the marriage penalty to "begin to repeal" the marriage penalty.

Their crude way of dealing with this in the short time they had to change their proposal was to simply say that married couples who file jointly and would be required to pay more in taxes than if they had not been married and filed separately would be entitled to a tax credit -- *but that the Department of the Treasury is instructed to calculate the tax credit amount so that the total reduction in federal revenues is estimated to equal $2 billion for each taxable year*. Thus, they have simply decided that it would only be as generous as could be afforded for $10 billion over the five year window.

Analytical Notes:

Revenue Loss: Removing any marriage penalty is a revenue losing tax cut. The important thing to note about proposals that eliminate the marriage penalty is that they either cost serious revenue or they call for raising the tax rates of other to lower them for some married couples. More precisely, the tax burden would shift from two-income families onto one-income families (which frequently have just one parent) and single persons.

Gaming: Treasury notes that the Istook plan -- giving two income families the choice of filing separately would create incentives for couples to "game" the tax system and manipulate their unearned income, which would complicate the tax filing process and give some couples an unfair advantage over others. Married couples would manipulate their unearned income by moving ownership of assets to the spouse facing the lower tax rate. This would enable couples with significant unearned income to reduce their taxes, whereas other married couples with the same total income (but through only salary and wages) would be forced to pay a higher effective tax rate.

(5C): Create an Expanded IRA -- "American Dream Savings Account"

Currently, taxpayers are allowed to deduct up to $2,000 and contribute to an IRA if their AGI is less than $40,000 (joint) or $25,000 (single) -- or if they are not active participants in an employer-sponsored pension plan (and their spouses are not active participants they are eligible regardless of income. The deduction is phased out between $40,000 and $50,000 of AGI on joint returns and between $25,000 and $35,000 for single filers. These income limits were added by the Tax Reform Act of 1986 (TRA). Earnings on IRA contributions are not taxed currently, yet distributions from IRAs are subject to income tax. An additional 10% penalty is imposed if distributions are made before the taxpayer is 59 1/2.

The plan creates a new type of IRA that is expanded in the following form:

Withdrawal for First Time Home Buyers, etc.: These IRAs are penalty free from withdrawal prior to retirement (59 1/2) for qualified special purpose distributions, which are for first time home buyers; higher education preventions for family (including grandchildren), medical expenses -- including longterm care insurance.

No income Limit: The new proposal would allow anyone, regardless of income or pension coverage to gain the tax benefits of an IRA. Currently, however, over two-thirds of taxpayers are already eligible. Anyone, regardless of income or pension coverage could benefit. This would essentially repeal the restrictions from the Tax Reform Act of 1986.

Backloaded: Under conventional IRAs, the benefit the taxpayers receive is their ability to contribute pre-tax income and then to allow interest to accumulate tax free. IRA contributors pay taxes eventually, but after significant tax free accumulation and presumably when their tax rates are lower. Therefore, the revenue loss from expansions would be seen right away as more currently taxable income can now be put into an IRA without paying taxes.

By contrast, American Dream Savings Account proposal is "backloaded." There is no revenue loss in the five year budget window because taxpayers are still paying taxes on their income, and depositing after-tax contributions in their IRA.

Roll-Over and Back-Loaded: Indeed, if there is a "roll-over provision in the "back-loaded" IRA, it can actually raise revenues in the first several years. The "rollover" provisions give taxpayers with existing IRA accounts a one-time only option to pay taxes now on the funds in their IRA accounts and transfer the funds into new IRA accounts. Because those who "rollover" pay taxes on pre-tax income, the "backloaded, rollover IRA" actually raises money in the short-run.

Yet, the upside for IRA contributors is that the interest they make on their after-tax principal is exempt from taxation forever! Therefore, this is a very deceptive provision from a fiscal point of view. It is designed to give the impression that it raises revenue -- which it does in the short-run -- yet it pushes off serious revenue loss to the outyears. It is therefore inconsistent with a balanced budget provision, because it is pushing revenue loss off to the future, which will increase deficits in the future.

Revenue Impact: The Contract writers estimate that expanded IRAs will increase revenues by $4.7 billion over the next five years. Past CRS analyses of similar proposals, however, suggest that ADS accounts could cost $50 billion or more over subsequent 5-year period after the rollover period ends and the amount of exempt interest in the ADS account grows.

Analytical Notes:

10 Year Senate Scoring Rule: It will be interesting to see how the Senate's ten year scoring rule will affect the back-loaded, roll-over provision. Indeed, perhaps the best justification for a 10 year rule is that it smokes out bills that are designed only to "fool" the five year budget window.

Tax Break for Wealthy: It also allows even the most wealthy Americans to gain permanent interest free earnings, while it offers little for working poor families who could not afford to put $2,000 a year into a saving account. In 1992, the Joint Tax Committee found that 95% of the benefits go to the top 20% of taxpayers and 33% goes to the top 3%. Nonetheless, many people in the "top 20%" would be seen as solidly in the middle class.

Increase Marginal Savings? One of the justifications for IRAs is that it will encourage savings. Yet, many economists feel that the more it is offered to higher income Americans the more it leads to families simply shifting existing savings. In that case, the expanded IRA works not as a savings incentive that increases private savings, but only as a windfall for existing savings. While most economists do not believe that IRAs for upper middle class families increases savings, Larry Summers is one of the economists who has suggested that comparative studies show that it could have some marginal savings effect.

Secretary Bentsen: Secretary Bentsen was previously a leader for the expanded IRA. His bill was one of the first to call for an expanded IRA that allowed distributions for first-time homebuying, education, long-term unemployment and high medical expenses. His bill -- Bentsen-Roth (now Breaux-Roth) was "backloaded" though many say that he agreed to this as a condition of winning support of Roth support. His bill also included inflation indexing for the IRA contribution limit. It is worth noting that if Democrats were to propose this, that through Secretary Bentsen, Democrats have as much of an original claim to this idea as anyone.

Variations Are Possible: It is worth noting that variations of this provision are possible. Income limits could be raised to $75,000 -- as opposed to being lifted completely.
And early withdrawals for first-time homebuying (or training as well) could be allowed regardless of the income limit.

7. THE SENIOR CITIZENS FAIRNESS ACT)

(7A): Raise the Social Security Earnings Limit: Currently, retired workers between the ages of 65 and 69 have their social security benefits reduced by 33 and 1/3 cents for each dollar of earnings over $11,160. Above age 69, persons receive full social security benefits, regardless of their earnings. The earnings test is lower for younger beneficiaries. They can earn up to $8,040 before benefits are reduced, and they are subject to a 50 percent benefit reduction. The earnings test thresholds are adjusted for inflation each year.

The House contract would phase in an increase to $30,000 in over five years. The cost is likely to be around $7 billion over five years.

Analytical Notes:

Not Benefit Most Seniors: Treasury notes that this is actually an extremely regressive -- the vast majority of the benefits would go to high-income seniors. Most retired workers between the ages of 65 and 69 would not benefit from these proposals. Of the 8 million persons in this age group who are covered by Social Security, 75% -- 6 million -- did not work at any time in 1989. Their decisions to retire were based on many factors in addition to the social security earnings test: health, leisure time, savings, pension income, the size of social security benefits, and employers' demand for elderly workers. For these same reasons, they are unlikely to seek employment once retired, even if the earnings test were raised.

Treasury notes that among those who currently work, many would likely not increase their work effort further in response to changes in the earnings test. Either they currently earn far less than the exempt amount (and would be unaffected by the change) or they earn too much to receive benefits even if the earnings test threshold were increased to $30,000. As the earnings test thresholds are increased, some retired workers, who currently earn too much to qualify for benefits, and their families would become eligible to receive benefits. Receipt of this windfall may cause some of these higher wage workers to reduce their work hours.

(7B): Repeal OBRA '93 tax increases on Social Security benefits: As you know, in OBRA 1993, we increased the portion of benefits subject to taxation for the top 13% of Social Security recipients. This provision seeks to gradually repeal that deficit reduction provision.

Taxpayers with sufficient income must include some of their Social Security benefits in income subject to income tax. Both prior to our economic plan and after our economic plan, approximately 80% of Social Security recipients have all of their Social Security benefits exempt from any taxation. Prior to our economic plan, the top 20% or recipients already had 50% of their benefits counted as taxable income to the degree that they had total income and benefits above the threshold of $25,000 for single taxpayers and $32,000 for married taxpayers. What the economic plan did, was ask the top 13% -- single taxpayers above the $34,000 threshold and married taxpayers, filing jointly above the $44,000 threshold -- to include 85% of the benefits above this higher threshold as taxable income.

The House Contract calls for phasing out the increase in OBRA 1993. They would phase it out as follows:

Taxable year beginning in calendar year:	Percentage:
1996	75 percent
1997	65 percent
1998	60 percent
1999	55 percent

Analytical Notes:

Deficit Increase: The hypocrisy of repealing something that reduced the deficit and affected only high income entitlement recipients is striking. While eliminating it could have cost $20 billion over five years, phasing it out would have
a somewhat lower cost in the short-term.

HI Solvency: The savings from the 85% threshold in OBRA 1993 went into the HI (Medicare) Trust fund and helped keep it solvent for a few more years. Prior to our economic plan it was headed for trouble in 1999.

Seriousness: Calling for repealing this new threshold may have been good short-term politics because of the sensitivity of Social Security and because $44,000 doesn't sound like much, even though it is in the top 13% for retired couples. Nonetheless, to go back and seek repeal of a tough entitlement savings from 1993 will be looked at with a very negative perspective by opinion leaders.

Regressivity: It also is the case, that seeking a special provision to lower the 85% threshold, puts Republicans in a position of choosing to come up with billions of additional savings for seniors and then give them only to the top 13% of recipients -- completely ignoring all others.

(7C) Tax incentives for long-term health insurance:

Individuals will be allowed to deduct private long-term care insurance premiums from their taxable income according to the following schedule:

Taxpayer Age	Maximum Deduction
40 or less	$200
41-50	$375
51-60	$750
61-70	$1,600
More than 70	$2,000

8: THE JOB CREATION AND WAGE ENHANCEMENT ACT

(8A): Capital Gains Tax Cut: Under current law, long-term capital gains that are taxed are capped at 28%. Taxpayers in the 15 and 28 percent brackets therefore pay the same tax rates on capital gains as on other income. Yet, since long-term capital gains rates are capped at 28 percent, taxpayers in the 31 percent, 36 percent and 39.6% tax bracket rate currently pay a lower rate on long-term capital gains than on other income. Thus, it is the case that Clinton economic plan, by raising marginal rates for higher income taxpayers, did create a strong incentive for longterm capital investment.

There have been several capital gains tax cut options over the last few years. President Bush had proposed several variations during his term. The way capital gains tax cuts are designed is that they exclude a portion from adjusted gross income. Under pre-Tax Reform Act of 1986 law, taxpayers were permitted to exclude 60 percent of the excess of long-term gains over short-term losses. Thus the maximum tax rate on long-term capital gains was 20 percent (40 percent of the 50 percent top income tax rate).

The contract calls for excluding 50% of capital gains income from taxation, which would have the effect of halving the tax rate individuals pay on capital gains. For example, a 50 percent exclusion would reduce the maximum capital gains tax rate to 14 percent (50 percent of 28 percent) and taxpayers in the 15 percent bracket would be subject to a 7.5 percent rate.

Congressman Archer, the new Chairman of the House Ways & Means Committee, introduced a slightly less generous option, H.R. 3739, that also excludes 50% of capital gains, but repeals the 28 percent rate cap. The difference is that someone in the 39.6% bracket would face a 19.6% capital gains tax rate (1/2 of 39.6%) as opposed to 14% rate (1/2 of 28%). While Congressman Archer is the likely Ways & Means Chair, the more generous option is the
the one in the Contract and the one that Republicans seem committed to proposing:

(8B): Index capital gains for inflation: This provision calls for indexing capital gains for inflation since assets must held for at least one year. The basis of assets would be adjusted for Gross National Product deflator. Taxpayers would increase the basis (cost) of their assets to adjust for inflation since the asset was purchased. Variations of this proposal would index capital gains only for inflation after some future date or add indexing to one of the exclusion proposals.

Joint Tax Committee Analysis: The JCT did a preliminary analysis of the House Contract provision and found that its revenue effect, in addition to that of the indexing proposal, was $208 billion cost over 10 years. It also found that 72% of the of the individual tax benefits would go to taxpayers making over $100,000.

Different From Bush Proposals: A 50 percent exclusion is a deeper cut than those proposed by President Bush. Bush's proposals gave greater tax reductions depending on how long the capital assets were held. For example, the FY 1992 Budget proposal would have allowed a 15 percent exclusion for assets held between one and two years, a 25 percent exclusion for assets held between two and three years, and a 35 percent exclusion for assets held three years or more. The FY 1993 Bush Budget proposal had the same format, with 15 percent, 30 percent, and 45 percent.

Distribution of Aggregate Tax Change: Below is the
full distribution for the 1992 Bush proposal, which gives a sense of how little of the revenue loss goes to the middle class.

Less than $10,000	0.2%
$10,000-$20,000	0.5%
$20,000-$30,000	1.6%
$30,000-$40,000	3.6%
$40,000-$50,000	4.5%
$50,000-$75,000	11.1%
$75,000-$100,000	8.6%
$100,000-$200,000	17.4%
$200,000 and over	52.5%
TOTAL	100%

JOINT TAX COMMITTEE (Estimate of Bush Administration's Capital Gains Proposal, February 3, 1992)

(8C): Neutral Cost Recovery Depreciation: One of the most complex and deceptive of the proposals in the House Contract is a provision called the neutral cost recovery depreciation. It is deceptive in the same way as the back-loaded, roll-over IRA is: it is designed to give the impression of raising revenues in the short-term, while it creates large, deficit increasing losses in the outyears. The main design tactic is to provide 150% accelerated depreciation schedule to some assets currently on a 200% accelerated depreciation schedule -- in order to raise revenues in the short-term -- while increasing the amount of the depreciable asset for both inflation (based on a GNP deflator) and an additional 3.5% government subsidized rate of return.

The scheme is designed to be neutral in net present value terms to the alternative of expensing an investment in the year the investment is made (hence the name), *but by adding an additional 3.5% return factor above inflation*. These proposals give businesses a government subsidy, on top of the favorable tax accounting treatment.

> Current Law: Under current law, for regular income tax purposes, depreciable assets other than buildings and structures are generally written off over recovery periods of 3, 5, 7, 10, 15, or 20 years (depending upon their "class life"). An accelerated depreciation method may be used (200 percent declining balance for assets with 3, 5, 7, and 10 year recovery periods, and 150 percent declining balance for assets with 15 and 20 year recovery periods). Residential buildings are written off over 27.5 years, and non-residential buildings are written off over 39 years using the straight-line method. For alternative minimum tax (AMT) purposes, less accelerated depreciation methods must be used.
>
> A neutral cost recovery system (NCRS) was suggested in 1985 as part of the Kemp-Kasten "Fair and Simple Tax" proposal. The proposal allowed taxpayers to increase future depreciation allowances for inflation plus a specified real rate of return (3.5 percent). For example, if the depreciation that would otherwise be allowed on a $100 investment is $33.33 in the first year, $44.44 in the second year, $14.81 in the third year, and $7.41 in the fourth year (for a total of $100 of allowances), and the inflation rate is 3.9 percent, the first year NCRS depreciation allowance would remain $33.33, but the second year's depreciation allowance would be $47.79 ($44.44*(1.039)*(1.035)), and the third year's allowance would be $17.13 ($14.81*(1.039)*(1.039)*(1.035)*(1.035)), etc.

Proposals: There are several Republican neutral cost recovery proposals that are included in legislation currently pending before Congress. The bills differ somewhat in timing and the treatment of depreciation for AMT purposes, but all the proposals include the NCRS fundamentals as proposed by Kemp and Kasten in 1985 -- depreciation amounts adjusted for both inflation (based on a GNP deflator) and an additional 3.5% rate of return. The Contract

Proposal seems to follow two bills, the Putting Jobs and the American Family First Act of 1993 (HR 2434) and Family, Investment, Retirement, Savings and Tax Fairness Act of 1993 (HR 3645): These bills, introduced by Rep. Grams (R-MN) on June 16, 1993 and November 22, 1993, respectively, would also create neutral cost recovery depreciation. H.R. 2434 and H.R. 3645 replace the 200 percent declining balance method allowed under MACRS with the 150 percent declining method before allowing for the NCRS adjustments. They also apply the NCRS adjustments to AMT depreciation and include a 3.5% adjustment on top of the inflation adjustment. H. R. 2434 has been referred to the House Government Operations, Rules and Ways and Means Committees.

Analytical Note:

Congressional Research Service Analysis of Longterm Revenue Effect: This proposal was also analyzed in a March 8, 1994 memo by Jane Gravelle, Senior Specialist in Economic Policy at the Congressional Research Service. The net effect, Ms. Gravelle concluded, would be to increase taxable income by $87 billion in the first five years, but decrease taxable income by $984 billion over a total of 39 years. And that was using only 1994 income levels throughout the time of the analysis. These losses would be exacerbated in times of high inflation when businesses will realize huge cash flow increases at the expense of the government.

***(8D) Increasing Small Business Expensing to $25,000*:** Ironically, the House Contract calls for increasing small business expensing from $17,500 to $25,000. This was not in their initial discussions, but was included in the legislation they said they would submit. It is clearly ironic, as you proposed increasing it from $10,000 to $25,000 in your economic plan, and you received no support from Republicans. Against your wishes, the amount of the increase was eventually decreased from $25,000 to $17,500 -- still a 75% increase.

(8E) Regulatory Reform:

• *Risk assessment and cost-benefit analysis for new regulations*:Each executive branch agency would be required to prepare a risk assessment, a cost-benefit analysis and an analysis comparing the economic and compliance costs with likely benefits to human health and the environment for every major rule relating to human health, safety, or the environment.

• *Establish federal regulatory budget:* The Office of Management and Budget and the Congressional Budget Office would be required to jointly report on the total cost to the private sector of complying with federal regulations. They would create a regulatory baseline, similar to the budget baseline, that would be updated annually. A regulatory report cost would also have to be included with the President's annual budget submissions to Congress.

• *Private property rights protection and compensation*: Private property owners would be entitled to compensation for any measurable reduction in the value of their property due to final agency action.

• *Unfunded mandate reform:* Legislation and rules that would require an unfunded mandate on either the public or the private sector must include analysis of the cost of that mandate. In addition, the CBO and OMB would be required to issue a federal mandate baseline, similar to the budget baseline. The Advisory Commission on Intergovernmental Relations would study and make recommendations to Congress and the President regarding ways to reduce the unfunded federal mandates on state and local governments.

• *Taxpayer debt buydown*: Individual taxpayers would be allowed to specify that up to 10 percent of their tax liability be used to pay down the federal debt.

III: REMAINING SIX PIECES OF SOCIAL, DEFENSE AND GOVERNMENT REFORM LEGISLATION:

Below are brief descriptions on the other six major pieces of legislation they have committed to vote on in their first 100 days. I am just providing you with brief descriptions, but we will ensure that the respective departments in the White House are analyzing the portions relevant to them.

2: THE TAKING BACK OUR STREETS ACT:

• *Make the death penalty easier to implement*: This reform would limit the time period for an application for a writ of habeas corpus and would give judges greater latitude to deny a habeas corpus application. It would also create special habeas corpus procedures in capital cases.

• *Mandatory prison terms for the use of firearms in a drug trafficking crime or a crime of violence*: On the first offense, violators would be given a 10–year prison term for possessing a firearm, a 20–year prison term for discharging the firearm or a 30–year prison term for using a machine–gun or gun with a muffling device.

• *Mandatory victim restitution*: Courts would be required to order restitution of the victim of an offense of which a defendant is convicted. Additionally, courts would be given the option to order restitution of any other person who was harmed physically, emotionally and pecuniarily by the unlawful conduct of the defendant.

Law enforcement block grants: This section would provide budgetary authority for a total of $10 billion in block grants from FY 1996 through FY 2000.

Truth in sentencing grants: States which have laws requiring that persons convicted of a serious violent felony serve not less than 85% of the sentence imposed will be eligible for these block grants. Budgetary authority is set at $10.5 billion from FY 1995 through FY 2000.

Cut certain social spending from the Crime Bill: The following provisions of the Crime Bill would be eliminated:

> Drug Courts, Ounce of Prevention Council, Local Crime Prevention Block Grant Program, Model Intensive Grant Programs, Family and Community Endeavor Schools Grant Program, Assistance for Delinquent and At-Risk Youth, Police Recruitment, Local Partnership Act, National Community Economic Partnership, Urban Recreation and At-Risk Youth, Community-Based Justice Grants for Prosecutors, and Family Unity Demonstration Project

3. **THE PERSONAL RESPONSIBILITY ACT:** (welfare reform) This was one of the only aspects of the Contract where they listed a specific savings. They claim that the net impact of their welfare reform proposal would be a savings of $40 billion.

- *Prohibit minor mothers from receiving welfare*: AFDC benefits could not be paid to children born out-of-wedlock to an individual who is less than 18 years of age. States would also be given the option to deny AFDC benefits to children born out-of-wedlock to individuals aged 18, 19 or 20.

- *Deny increased AFDC to parents who have children while on welfare*:

- *Cut spending on welfare reform*: The aggregate amount of federal money spent on welfare (including family support, Supplemental Security Income and housing aid) would be capped at the FY 1995 level, adjusted only for inflation and changes in the poverty population.

- *Restricting welfare for aliens:* Aliens would not be eligible for non-emergency public welfare assistance. Programs which would be prohibited include housing assistance, school lunches, non-emergency health services, WIC, domestic volunteer programs, and LIHEAP. Aliens who currently reside in the U.S. and are eligible for a program would be given a one-year grace period before losing eligibility.

- *Enact a "two years and your out" provision*: States would be allowed to force aid recipients to enter a work training program. After 24 months of receiving aid and participating in a work training program, the aid recipient would be required to engage in work activities at least 35 hours per week. States would be given the flexibility to design their own training programs and would be provided, in total, $9.9 billion in funding over five years.

• *Consolidate food assistance programs*: States would receive block grants administered by the Department of Agriculture to fund food assistance programs. Current food assistance programs would be consolidated into this one block grant program. Budgetary authority would be $35.6 billion for FY 1996 and such funds as are necessary thereafter.

4. FAMILY REINFORCEMENT ACT:

• *Provide tax incentives for adoption*: Certain adoption expenses would be allowed as a tax credit of up to $5,000 per year. The credit is gradually phased out for individuals whose adjusted gross income is from $60,000 to $100,000.

• *Strengthen child protection laws*: This section would create a mandatory minimum sentence of three years for prostitution of children and increase the mandatory sentence to three years for sexual abuse of a minor or ward. In addition, it would increase the penalty for using computers to transmit child pornography.

• *Grant an elderly dependent care tax credit*: Individuals who care for an elderly parent or grandparent within their household may claim a $500 tax credit.

• *Increase child support enforcement*: This section would require noncustodial parents who fail to make required child support payments to enter a job search program. If the noncustodial parent does not make the owed payments after participating in the job search program, he or she would be required to participate in a work program established by the state.

6. THE NATIONAL SECURITY RESTORATION ACT: (Nancy Soderberg is having NSC do an analysis of these provisions for you).

• *Develop an antiballistic missile system*: The bill would require that the U.S. deploy at the earliest possible moment an antiballistic missile system that is capable of providing a highly effective defense of the United States against ballistic missile attacks.

• *Create a "Commission on National Security and Department of Defense Force Structure and Readiness Funding Shortfalls"*
The Commission would examine both immediate supplemental funding needs and "conduct a comprehensive review of our Nation's defense strategy, force structure, modernization and infrastructure needs." The Commission would be required to submit its final report to the President and Congress by May 1, 1996. The President, the Speaker of the House and the President pro tempore of the Senate would each appoint 4 of the 12 Commission members.

• *Prohibit U.S. troops from serving under foreign command*:No U.S. forces would be allowed to be "placed under the operational control of a foreign national acting on behalf of a multinational force or organization" except in circumstances where such "control is necessary to protect vital national security interests of the United States."

• *Restore "budget firewalls" for defense spending*: The bill suggests that Congress should enact additional legislation that would reset budget firewalls around the defense budget, to prevent the shifting of any funds out of defense to help finance domestic discretionary programs.

Note on Cost: As there was no specific scoring on this legislation, we based our cost estimates on the cost of the Defense proposals on the House Republican FY 1995 alternative budget written by Rep. Kasich, which proposed increasing outlays by $61.1 billion and budgetary authority by $73.7 billion over five years. He never backed away from this amount of funds and it was the only Republican proposal that was comparable to the goals of the Contract that had been scored. Yet, it is not a precise cost estimate of what is in their exact legislation.

9. THE COMMON SENSE LEGAL REFORM ACT

• *Require that nonprevailing parties in civil litigation pay the attorney's fee of the prevailing party*

• *Reform product liability laws to limit punitive damages*
Punitive damages in civil actions would be limited to the greater of 3% the amount awarded to the claimant for economic injury or $250,000.

10. TERM LIMITS (The Citizen Legislature Act)

• This Constitutional Amendment would limit Senators to two elected terms and members of the House of Representatives to six elected terms. It would apply only to elections after the Amendment is ratified by the states.

IV. SENATE CONTRACT OR PLEDGE VERSION "SEVEN MORE IN '94"

The Senate Republican Agenda is based on seven broad proposals. Unlike their House counterparts, the Republican Senators have not drafted specific legislation.

Most of these seven proposals would require budgetary savings in order to be enacted without increasing the deficit.

1. ENACT A BALANCED BUDGET AMENDMENT TO THE CONSTITUTION

The Senators promise to "proceed to immediate consideration" of the amendment after swearing-in ceremonies on January 3, 1995. Their proposal does not specify any details about how the Amendment will be structured or about how the balancing process will be timed and enforced.

The Contract with America also proposes a balanced budget amendment.

2. DOUBLE THE INCOME TAX EXEMPTION FOR CHILDREN

This proposal would increase the income tax exemption for children from $2,500 to $5,000. No upward income bound is specified and the proposal says that the tax change will be paid for by "spending cuts".

The Senate version is more regressive than the House version because it relies on tax exemptions instead of tax credits. The additional $2500 exemption would be worth $900 to someone in the 36% tax exemption. Yet, it would only be worth $375 for a family in the 15% tax bracket and zero for a family with no tax liability. Thus, it only exacerbates the current regressivity of the child exemption. As you may recall, prior proposals such as Gore-Downey sought to replace the exemption with a credit. Most other proposals have at least sought to have a credit on top of the existing exemption.

3. REAL HEALTH CARE REFORM BASED ON CONSUMER CHOICE AND PRIVATE MEDICINE

The Republicans promise "to expand access and control costs by expanding consumer choices, promoting competition, reforming medical liability laws, and reducing government paperwork and bureaucracy."

The Contract with America offers tax incentives for private long-term care insurance.

4. ENACT LEGISLATION THAT BRINGS AN END TO CRIME WITHOUT PUNISHMENT IN AMERICA

The Republicans promise to "impose mandatory prison sentences on violent felons and drug traffickers, stops building prisons as though they were Holidays Inns, and put prisoners to work." In addition, they state that they will repeal the "pork barrel spending" from the Crime Bill.

The Contract with America includes similar anti-crime proposals.

5. REFORM WELFARE AND EXPAND JOB OPPORTUNITIES

The Republican welfare reform would be "based on work, more individual responsibility, and less federal spending." They also propose to create jobs with three tax cuts: 1) IRA-Plus bill, 2) lowering the capital gains tax, and 3) indexing taxes on assets for inflation.

The Contract with America includes a capital gains tax cut, IRA expansion and also indexes assets for inflation.

6. TAX FAIRNESS FOR RETIRED AND WORKING ELDERLY

The Republicans promise to repeal both OBRA '93's increased tax on Social Security and the reduced benefits for those who work.

The Contract with America includes both of these proposals.

7. PROTECT NATIONAL DEFENSE

The Republicans promise to stop defense cuts and protect the defense budget from being used to fund non-defense spending.

The Contract with America includes similar defense measures.

FINANCING:

$238 Billion in Entitlements: The Senate Pledge also made vague financing promises. It stated that it would use $238 billion "equal to all proposals made by President Clinton not yet enacted that reduce non-Social Security entitlements. This clearly is a promise to use the Medicare and Medicaid savings in the Health Security Act to pay for their "pledge."

$94 Billion Non-Defense Discretionary Freeze: They claim that a "hard" freeze in non-defense discretionary spending would save $94 billion. Yet, such a hard freeze -- which would amount to a real, inflation adjusted cut of 3% a year, or 10-15% over five years -- does not even appear to get so much money. OMB projects that non-defense discretionary spending only goes up $30 billion over five years -- barely enough (if enough) to keep up with inflation. By 1998, domestic discretionary spending will be the lowest as a percentage of GDP since the Kennedy Administration. As one might guess, there are no details on where the $94 billion would come from.

$100 Billion From Base Closing-type Commission: They also recommend an additional $100 billion that would an independent commission would come up with for an up-or-down vote, like the BRAC. What is somewhat staggering about this idea, is that this is seen as on top of and in addition to the $238 billion in entitlements and $97 billion in non-defense discretionary spending promised above.

TOTAL: If they can accomplish all of the savings above -- $432 billion -- they are still not even half way to balancing the budget and paying for their tax cuts and new spending proposals.

V: APPENDIX - BUDGETARY COST ESTIMATES AND SENIOR ANALYSIS

I. Five–year cost estimate of the House Contract

II. Seven–year cost estimate of the House Contract

III. What Would the Impact on Seniors and Others Be?

IV. Pie Chart of Programs Available for Spending Cuts

TABLE 1
5-YEAR COST ESTIMATE
HOUSE REPUBLICAN "CONTRACT WITH AMERICA"

($ in billions)

	5-Year Total
Balanced Budget Amendment *Source: CBO estimate of a 5-year balanced budget schedule. Rep. Armey has proposed balancing the budget by the year 2000.*	$743.0
Tax Incentives for Adoption *Source: House Republican Leadership Estimate*	0.9
Dependent Care Tax Credit for Seniors *Source: House Republican Leadership Estimate*	8.0
$500/child Tax Credit *Source: House Republican Leadership Estimate*	107.0
Modify the Marriage Penalty *Source: House Republican Leadership Estimate*	10.0 (1)
Super IRA	0.0 (2)
Defense *Source: House Republican Alternative Budget, March 1994*	61.1 (3)
Raise Social Sercurity Earnings Limit to $30,000 *Source: House Republican Leadership Estimate*	6.8
Phase-Out 85% Social Security Inclusion *Source: House Republican Leadership Estimate*	17.0
Tax Incentives for Private Long-Term Care Insurance *Source: House Republican Leadership Estimate*	1.3
Cut Capital Gains Rates/Index to Inflation *Source: House Republican Leadership Estimate*	56.0
Neutral Cost Recovery	0.0 (2)
Small Business Expensing Provision *Source: House Republican Leadership Estimate*	3.5
Raise Estate & Gift Tax Exclusion *Source: House Republican Leadership Estimate*	6.5
Restore Tax Deduction for Home Office Expenses *Source: House Republican Leadership Estimate*	0.6
Reduce Congressional Staff by One-Third *Source: House Republican Leadership Estimate*	0.1
TOTAL COST	**$ 1.0218 Trillion**

(1) Initial documents claimed the marriage penalty would be eliminated, as in the Istook proposal (HR 3851). JCT estimates this would cost $72 billion. Apparently the "Contract" has been altered to only reduce the marriage penalty.

(2) The IRA and Neutral Cost Recovery proposals are both listed as tax increases totalling $24.2 billion. In fact, CRS analysis shows that the cost of the Super IRA would be $8 billion per year. Likewise various JCT estimates of rollover, backloaded IRAs also show yearly costs of $4-8 billion per year. The NCR proposal has been projected by the Senate Budget Committee as costing money within 5 years. In light of these differences, we have simply listed both proposals as cost neutral over the next 5 years.

(3) The description in "Contract with America" repeatedly refers to "'strengthening" the defense budget. The House Rep. alternative budget introduced by Rep. Kasich called for a $61.1 billion increase in outlays and a $73.7 billion increase in budget authority. However, in a cost estimate document released by the House Rep.leadership on Sept. 23, 1994, they claim that their defense proposal would have 'no costs.' If this reflects that the House Rep. leadership is in agreement with the Clinton defense budget, the total cost of their proposals would be $61.1 billion less, or $961 billion total.

TABLE 2
7-YEAR COST ESTIMATE
HOUSE REPUBLICAN "CONTRACT WITH AMERICA"

($ in billions)

	7-Year Total
Balanced Budget Amendment *Source: CBO estimate of a 7-year balanced budget schedule.*	$1,200.0
Tax Incentives for Adoption *Source: House Republican Leadership Estimate (1)*	1.3
Dependent Care Tax Credit for Seniors *Source: House Republican Leadership Estimate (1)*	11.2
$500/child Tax Credit *Source: House Republican Leadership Estimate (1)*	149.8
Modify the Marriage Penalty *Source: House Republican Leadership Estimate (1)*	14.0
Super IRA *Source: Center on Budget and Policy Priorities, and past analyses by JCT and CRS.*	16.0 (2)
Defense *Source: House Republican Alternative Budget, March 1994*	85.5
Raise Social Sercurity Earnings Limit to $30,000 *Source: House Republican Leadership Estimate (1)*	9.5
Phase-Out 85% Social Security Inclusion *Source: House Republican Leadership Estimate (1)*	23.8
Tax Incentives for Private Long-Term Care Insurance *Source: House Republican Leadership Estimate (1)*	1.8
Cut Capital Gains Rates/Index to Inflation *Source: House Republican Leadership Estimate (1) and JCT analysis, October 1994*	109.8
Neutral Cost Recovery *Source: Center on Budget and Policy Priorities, and estimates based on CRS analysis.*	16.0 (2)
Small Business Expensing Provision *Source: House Republican Leadership Estimate (1)*	4.9
Raise Estate & Gift Tax Exclusion *Source: House Republican Leadership Estimate (1)*	9.1
Restore Tax Deduction for Home Office Expenses *Source: House Republican Leadership Estimate (1)*	0.8
Reduce Congressional Staff by One-Third *Source: House Republican Leadership Estimate (1)*	0.1
TOTAL COST	**$ 1.6537 Trillion**

(1) Estimates based on the House Republican Leadership numbers assume that the cost over seven years equals 7/5 (140%) of the five-year cost.

(2) The IRA and Neutral Cost Recovery proposals are both listed by the Republicans as tax increases, totalling $24.2 billion. In fact, CRS analysis shows that the cost of the Super IRA would be $8 billion per year once fully implemented. The NCR proposal has also been projected by CRS as costing money. In light of these differences, we have calculated both proposals as cost neutral over the first 5 years and estimate the outyear cost on these objective analyses.

WHAT WOULD THE IMPACT ON SENIORS AND OTHERS BE?

The Contract calls for a balanced budget, major tax cuts, and increased defense spending. The five-year cost is more than $1 trillion and the seven-year cost is more than $1.6 trillion. In addition to these cumulative costs, it is important to also look at what percentage of the budget would have to be cut in order to pay for the Contract in the year the Republicans would make good on all of their promises. Since the Contract calls for the budget to be balanced by FY 2002 (Rep. Armey's bill calls for balance by FY 2000), the following analysis examines annual spending for FY 2002 alone.

According to the CBO, there would be $1,891 billion in revenues and $2,209 billion in spending leading to a deficit of $319 billion in FY 2002. Thus, to balance the budget, the House Republicans would need to cut $319 billion off the baseline spending plus find enough savings to pay for their tax cuts and additional spending. A conservative estimate is that their plan would require an additional $102.5 billion in savings in FY 2002. *Thus, while their plan would call for savings of over $1.6 trillion over seven years, supporters of the Contract would have to find a total of $421.5 billion in savings in the single year of FY 2002 alone.*

How would they do it? To be generous, we will assume that they would get $50 billion in interest savings in FY 2002 -- though that is very generous. Subtracting this amount leaves $371.5 billion in savings the Republicans must find in the remaining budget. Since we have given them interest savings, interest has to be taken off the table, as does defense -- since they say they want to increase it. Thus, the Republicans start with a pool of $1,689 billion in available savings to cut from in FY 2002. (See attached chart.)

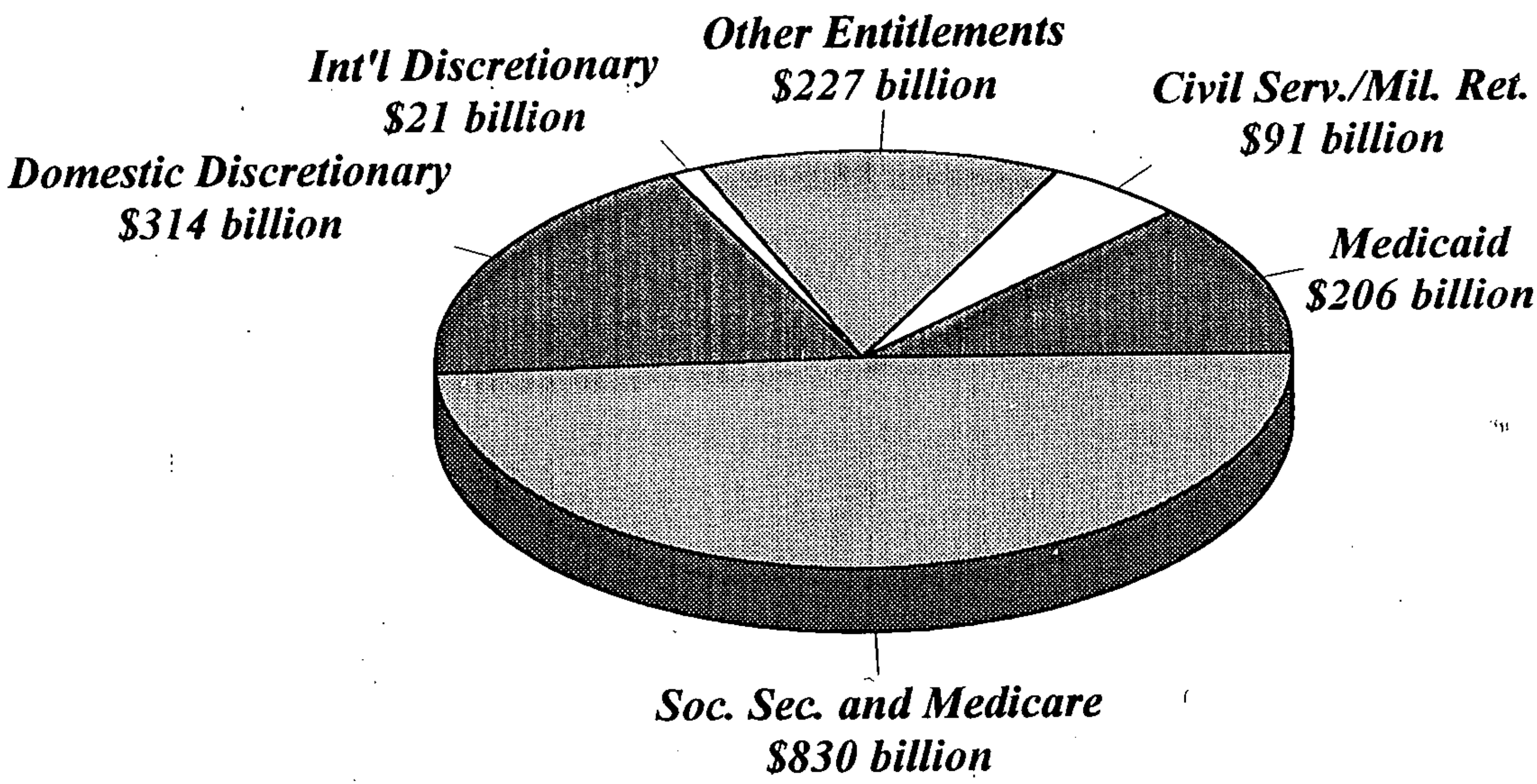
Domestic Discretionary	$314 billion
Int. Discretionary	21
Medicaid	206
Social Security	476
Medicare	354
Civ. Service and Ret.	91
Other	227
TOTAL	$1,689 billion

22% Across the Board Cut on Social Security and Medicare: Thus, they then have to reduce spending by $371.5 billion out of a remaining pool of $1,689 billion. This would mean a 22% reduction across the board in all programs, including Social Security.

31% Cut on Medicare and All Other Programs: If they take Social Security off the table, $476 billion must be removed from the pool of potential savings and they would have to cut $371.5 billion out of $1,213 billion -- a 31% cut in all remaining programs, including Medicare.

43% Cut on All Non-Social Security and Medicare Programs: If they take Social Security and Medicare off the table, $354 billion more must be removed from the available pool of savings and they would have to cut $371.5 billion out of $859 billion -- a 43% cut across-the-board in all other programs.

The Republican "Contract with America" requires *$371.5 billion* in savings in FY 2002. What will they cut?



PROGRAMS AVAILABLE FOR SPENDING CUTS, EXCLUDING DEFENSE

(CBO FY 2002 Projections)