



U.S. House of Representatives
Washington, DC 20515

The People's Budget

Budget of the Congressional Progressive Caucus

Fiscal Year 2012

Executive Summary

Budgets are more than collections of numbers; they are a statement of our values. The Congressional Progressive Caucus Budget is a reflection of the values and priorities of working families in this country. The “People’s Budget” charts a path that keeps America exceptional in the 21st century, while addressing the most pressing problems facing the nation today. Our Budget eliminates the deficit and stabilizes the debt, puts Americans back to work, and restores our economic competitiveness.

The CPC Budget addresses these problems by listening to the American people. In poll after poll, they are telling us, their representatives in the American government, that they want to preserve Social Security, Medicare, and Medicaid, to make higher education more affordable, to expand job-training programs, to cut taxes burdening the middle class, to subsidize affordable housing, and to provide financial assistance for those struggling to prevent foreclosures.

The majority of America thinks cuts to Social Security, Medicare and Medicaid, K-12 education, heating assistance to low-income families, student loans, unemployment insurance, and scientific and medical research are completely unacceptable. In contrast, Americans find a progressive tax policy very acceptable. The overwhelming majority of America supports additional taxes on millionaires and billionaires, eliminating unnecessary weapons systems, eliminating tax credits for the oil and gas industries, phasing out Bush tax cuts, and eliminating subsidies for new nuclear power plants. Poll after poll give voice to what Americans are asking of us.

Our Budget, in response, listens to what the American people are telling us. It does all of the above in a fiscally responsible way that dramatically reduces our borrowing from banks and foreign governments and ensures our long-term economic competitiveness. It does all of the above recognizing that in order to compete, we need every American to be productive, and in order to be productive, we need to raise the skill level of every American and meet the basic needs of every working family. It does all of the above while remaining rooted in fairness, recognizing that America works only when everyone has an opportunity to make it in America.

Our Budget Eliminates the Deficit by 2021

The CPC budget eliminates the deficit in a way that does not devastate what Americans want preserved, specifically, Medicare, Medicaid, and Social Security. Instead of eroding America’s hard-earned retirement plan and social safety net, our budget targets the true drivers of deficits in the next

decade: the Bush Tax Cuts, the wars overseas, and the causes and effects of the recent recession. By implementing a fair tax code, by building a resilient American economy, and by bringing our troops home, we achieve a budget surplus of over \$30 billion by 2021 and we end up with a debt that is less than 65% of our GDP. This is what sustainability looks like.

Our Budget Puts America Back to Work & Restores America's Competitiveness

The CPC budget rebuilds America and makes it competitive again. We put America back to work. We rebuild our roads and bridges, ensuring that those who use it help pay for it. We rebuild our dams and waterways with seed money for shipping systems that can compete with the rest of the world. We rebuild our education system by training more and better teachers, restoring schools, helping each student graduate, and supporting community colleges. This is what competitiveness looks like.

Our Budget Creates a Fair Tax System

The CPC budget implements a fair tax system based on the American notion that fairness and equality are integral to our society. Our budget restores fairness to a system that unfairly benefitted the richest few while hurting the majority of America. Our budget heeds America's call to end the Bush Tax Cuts and the estate tax and create fair tax brackets for millionaires and billionaires while maintaining credits for the middle class and students. It ensures that the banks that wrecked our economy pay a modest financial responsibility fee and that exotic trading by Wall Street traders who gambled away America's savings is levied a tax. It guarantees that hedge fund managers (and those who use them) do not get special treatment by taxing capital gains and dividends as ordinary income. It eliminates charity to oil companies making record profits from prices paid at the pump by the American people, given that it is unfair that the American people must also give these oil companies billions of dollars in handouts. Finally, our budget taxes US corporate income as it is earned, in much the same way Americans are taxed. This is what fairness looks like.

Our Budget Brings Our Troops Home

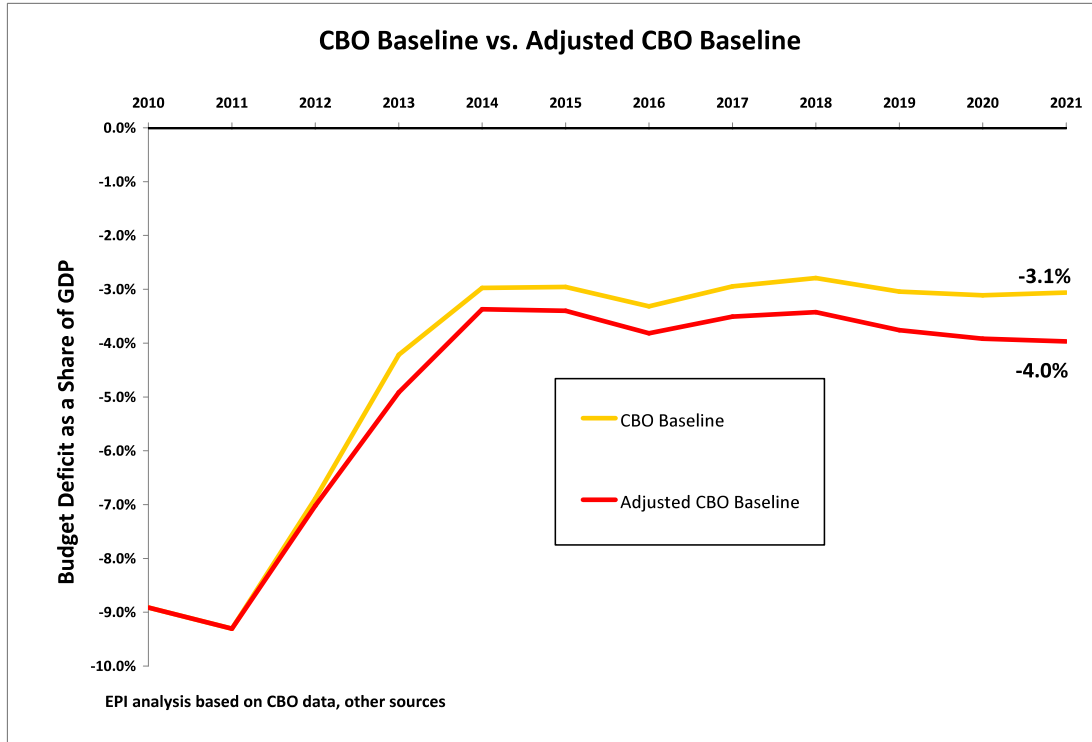
The CPC budget responsibly ends our wars that are currently paid for by American taxpayer dollars we do not have. We end these wars not simply to save massive amounts of money or because the majority of America is polling in favor to do so, but because these wars are making America less safe, are reducing America's standing in the world, and are doing nothing to reduce America's burgeoning energy security crisis. The CPC budget offers a real solution to these fiscal, diplomatic and energy crises, leaving America more secure, both here and abroad. The CPC budget also ensures that our country's defense spending does not continue to contribute significantly to our current fiscal burden – a trend we reverse by ending the wars and realigning conventional and strategic forces, resulting in \$2.3 trillion worth of savings. This is what security looks like.

Our Budget's Bottom Line

- Deficit reduction of \$5.6 trillion
- Primary spending cuts of \$869 billion
- Net interest savings of \$856 billion
- Total spending cuts of \$1.7 trillion
- Revenue increase of \$3.9 trillion
- Public investment of \$1.7 trillion
- Budget surplus of \$30.7 billion in 2021, debt at 64.1% of GDP.

The Baseline

The CPC Budget baseline includes both a ten-year doc fix and Alternative Minimum Tax Patch.¹ The adjusted deficit, which was the starting point for this proposal, is compared with the CBO current law deficit below. We have calculated an adjusted debt level to reflect adjusted deficit levels. We have also calculated the net deficit impact of various policies to include interest adjustments based on net interest levels identified in the CBO's March budget update.



¹ Note: Not patching the AMT would save \$683 billion over ten years. Not maintaining the doc fix would save \$298 billion over ten years. The cost of maintaining these policies amounts to just under \$1 trillion over ten years, but not including these costs would amount to budget gimmickry.

Overview of Our Policies

Individual Income Tax Policies

- Allow the Bush-era tax cuts to expire at the end of 2012, but extend marriage relief, credits, and incentives for children, families, and education
- Immediately rescind the upper-income tax cuts in December's tax deal
- Index the AMT for inflation for a decade (the AMT patch is fully paid for)
- Schakowsky millionaire tax rates proposal (adding 45%, 46%, 47%, 48%, and 49% top rates)
- Tax all capital gains and qualified dividends as ordinary income
- Progressive estate tax (Sanders' estate tax, repeal of Kyl-Lincoln)
- Limit the rate at which itemized deductions can reduce tax liability to 28% for high earners
- Replace the tax exclusion for interest on state and local bonds with a subsidy for the issuer

Corporate Tax Reform

- Tax U.S. corporate foreign income as it is earned
- Eliminate corporate welfare for oil, gas, and coal companies
- Enact a financial crisis responsibility fee
- Financial speculation tax (derivatives, foreign exchange)
- Reinstate Superfund taxes

Health Care

- Enact a public option
- Negotiate Rx payments with pharmaceutical companies
- CMS program integrity and other Medicare and Medicaid savings in the president's budget
- Prevent a cut in Medicare physician payments for a decade (maintain doc fix)

Social Security

- Raise the taxable maximum on the employee side to 90% of earnings and eliminate the taxable maximum on the employer side
- Increase benefits based on higher contributions on the employee side

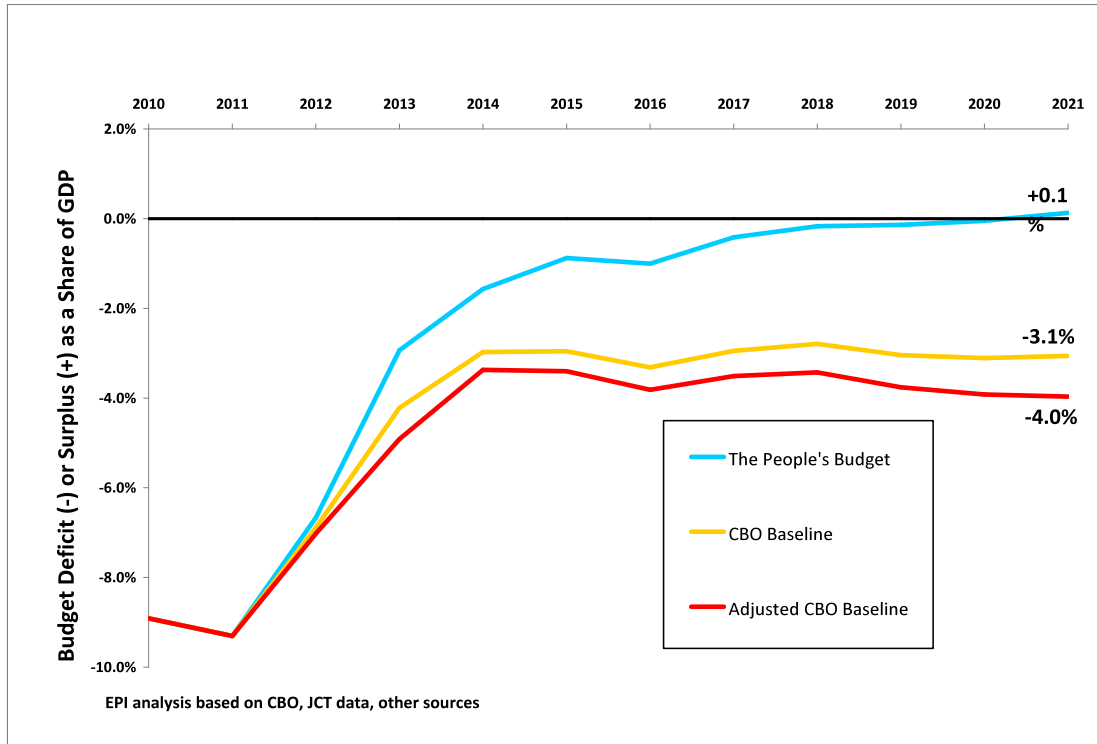
Defense Savings

- End overseas contingency operations emergency supplementals starting in Fiscal Year 2013, providing \$170 billion in FY2012 to fund redeployment, while saving more than \$1.8 trillion from current law spending levels over ten years.
- Reduce baseline defense spending by reducing strategic capabilities, conventional forces, procurement, and R&D programs

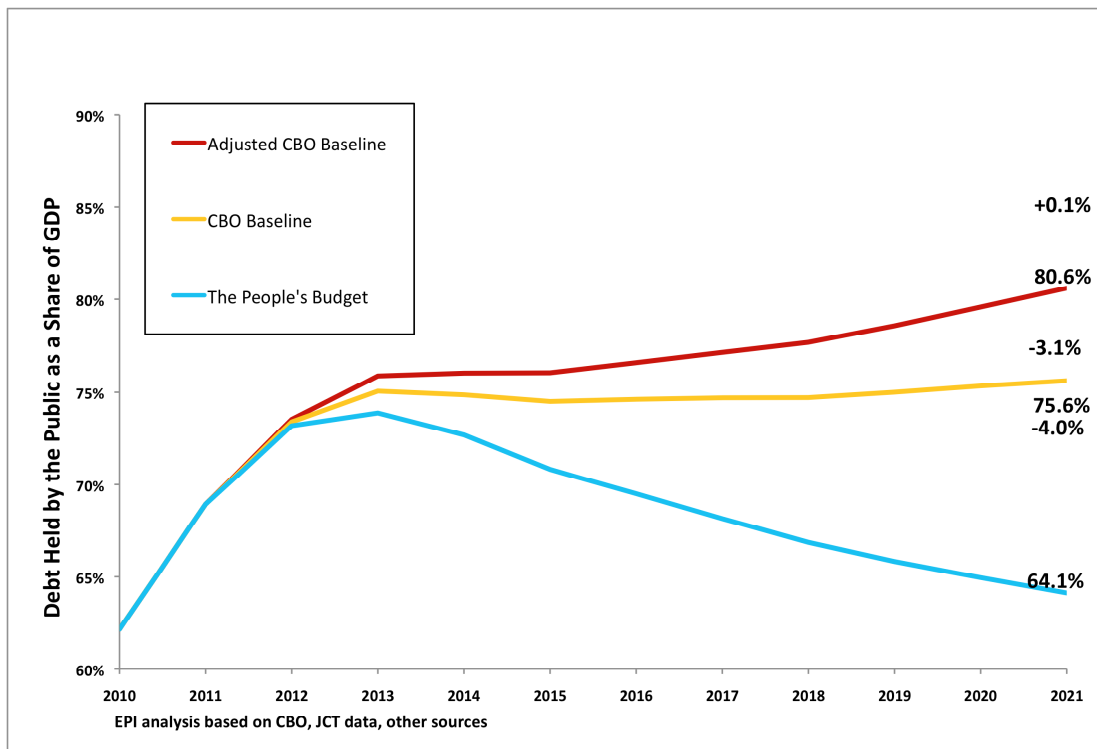
Comprehensive Jobs Program

- Invest \$1.45 trillion in job creation, education, clean energy and broadband infrastructure, housing, and R&D
- Infrastructure bank
- Surface transportation reauthorization bill (\$213 billion)

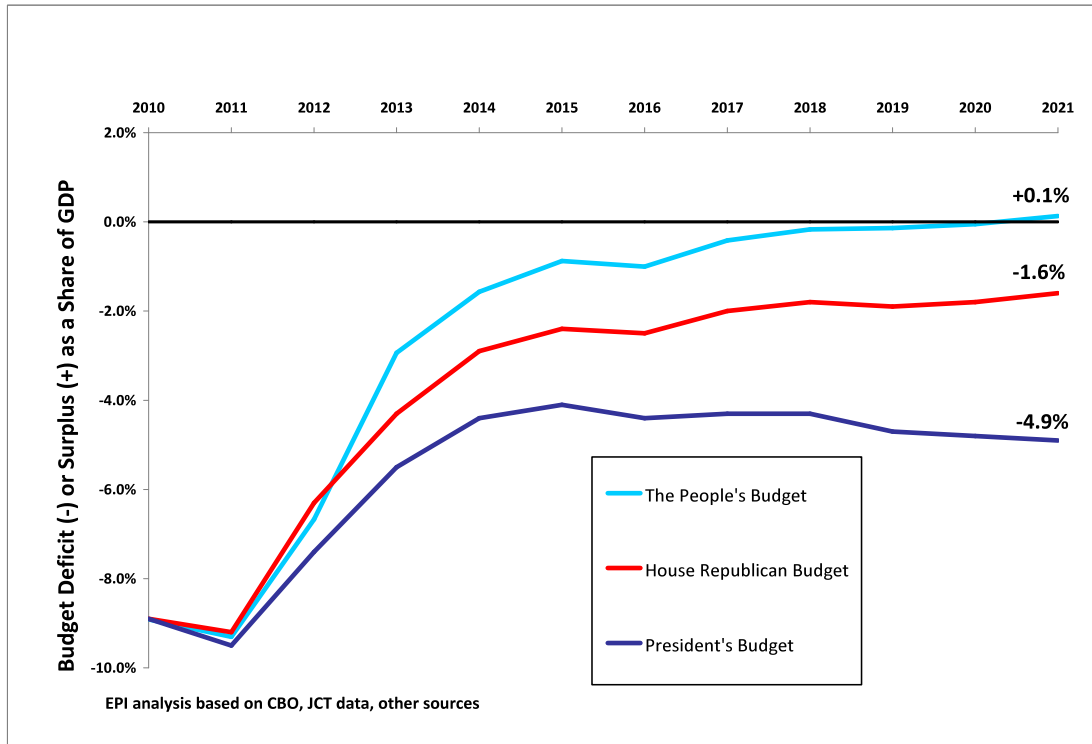
The People's Budget Eliminates the Deficit Achieves Budget Surplus by 2021



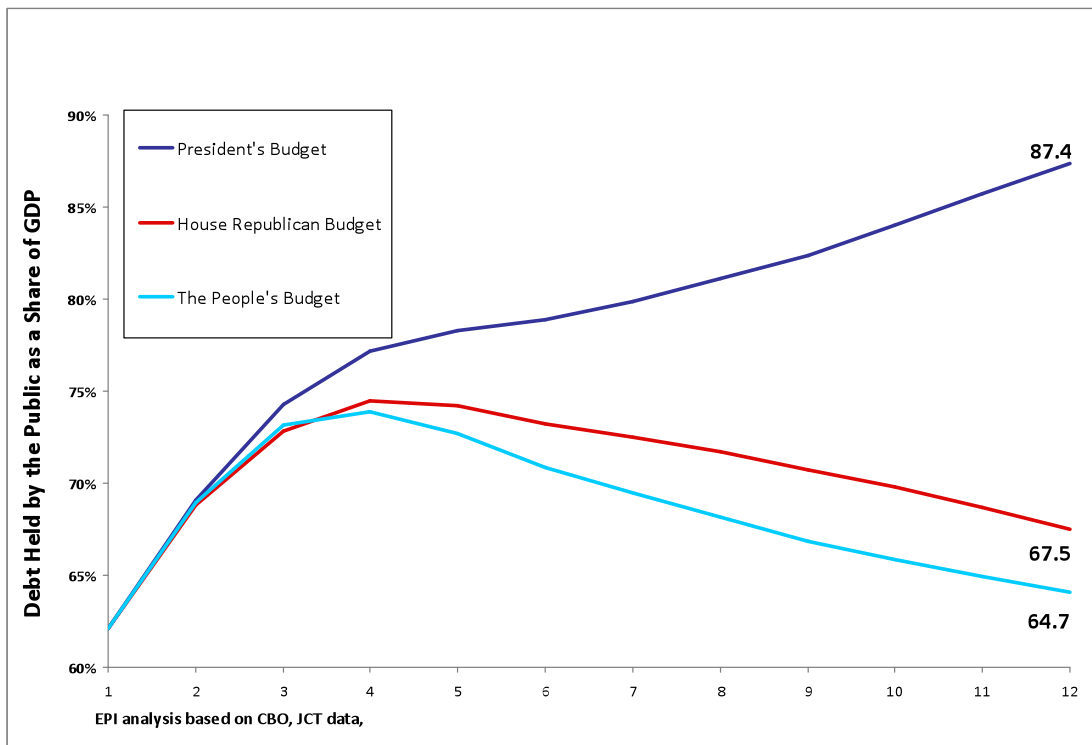
The People's Budget Brings Debt Below 65% of GDP by 2021



The People's Budget Offers a More Sustainable Path for *Deficits* than the House Republican Budget or the President's Budget



The People's Budget Offers a More Sustainable Path for *Public Debt* than the House Republican Budget or the President's Budget



Putting America Back to Work and Restoring American Competitiveness

Education In addressing the nation's long-run fiscal challenges, investments in education enhance the long-term growth potential of the economy by investing in the skills of our present and future workforce. The nation's human capital can be increased in many ways, including through formal and informal education, experience gained over time on a job, and training in the workplace. Front-end investment in Pre-K, K-12 and higher education is the most important contribution we can make to our economic growth in the long run. A more skilled workforce can produce more, and higher-skilled workers tend to earn higher wages.

Transportation Rebuilding our highways and waterways will create jobs in the short term and is at the heart of our international competitiveness in the long term. Our budget dramatically increases transportation outlays through a surface transportation reauthorization bill as outlined in the president's 2012 budget request.

Infrastructure The new Infrastructure Bank will provide loans and grants to support individual projects and broader activities of significance to our nation's economic competitiveness. For example, the IBank could support improvements in road and rail access to a West Coast port that benefits farmers in the Midwest, or a national effort to guarantee private loans made to help airlines purchase equipment in support of the Next Generation Air Transportation System (NextGen). A cornerstone of the IBank's approach will be a rigorous project comparison method that transparently measures which projects offer the biggest value to taxpayers and our economy. This marks a substantial departure from the practice of funding projects based on more narrow considerations.

Energy Independence With only 3% of the known oil reserves in the world, the United States cannot become energy independent or measurably affect the world price of oil simply by drilling more within our borders. We need to set loose the clean energy industry that is ready to take hold if we make the public investments in transportation and storage. Our budget will unleash American ingenuity and talent to build a new clean energy economy in which the United States will regain its rightful place as a world leader, move energy independence and address our global warming challenges.

Housing The middle of a historic recession and a "jobless recovery" is not the time to cut support for affordable housing. Investments in housing are one of the most potent job creation tools we have, because every dollar invested in housing creates two dollars and twelve cents in additional economic activity and induces as much as seven additional dollars in indirect economic activity. Providing housing not only reduces the rate of homelessness, which costs state, local and federal governments tens of thousands of dollars for every homeless family, but provides the vital backbone for creating long-term economic viability for every family in America: a place to call home.

Bringing Our Troops Home and Reducing Defense Spending

End emergency war funding beginning in FY 2013 The CBO baseline assumes that all discretionary funding—including emergency war funding—grows with inflation (from a starting point of \$159 billion in 2011) when projecting future discretionary spending. Eliminating all emergency defense funding starting in 2012 would save \$674 billion over 2012-16 and \$1.6 trillion over 2012-21 relative to this baseline.

Reduce base discretionary defense spending Our budget institutes a realistic reduction in defense spending on conventional and strategic forces and capabilities that would not compromise our national security interests or capabilities. Savings would accrue from decreasing routine deployment of U.S. troops overseas (ignoring overseas contingency operations), slowing the growth of the Army and Marine Corps as the wars in Iraq and Afghanistan wind down, reducing the fleet size of the U.S. Navy, reducing the number of Air Force squadrons, reducing the strategic capabilities, and canceling outdated cold-war weapon systems (including variations of the F-35, MV-22 Osprey, and Expeditionary Fighting Vehicle), among other savings.

This proposal does not touch Tri-Care.

A Fair Tax System

Individual Income Tax Policies

Allow the Bush-era tax cuts to expire at the end of 2012 (allowing rates to revert to Clinton-era levels), but extend marriage relief, credits, and incentives for children, families, and education Our budget maintains marriage penalty relief (standard deduction, EITC phase-out, and the 15% bracket), the expanded CTC, education incentives, and other incentives for children and families.

Rescind the upper-income tax cuts in the tax deal Repealing the 33% and 35% tax brackets, reinstating the limitation on itemized deductions and personal exemption phase-out, ending capital gains and dividends tax cuts, and returning the estate tax to 2009 parameters would save roughly \$95 billion over 2012-14 (tax-year 2012 spills into FY2013 and the capital gains tax cut spills into FY2014).²

Index the AMT for inflation for a decade The Alternative Minimum Tax (AMT) was designed to keep wealthy taxpayers from using loopholes to avoid paying taxes. But because it is not automatically updated for inflation, more middle-class taxpayers are getting hit with the AMT. While we need a long-term solution to this problem, until one exists we have to be honest about our obligations to the middle class families in this country. Our budget fully pays for the AMT patch for the next decade.

Schakowsky millionaire tax rates proposal (adding 45%, 46%, 47%, 48%, and 49% top rates) The Schakowsky plan creates five additional income tax brackets, starting at 45 percent for married couples making over \$1 million dollars a year and increasing to 49 percent for people making \$1 billion and over. The current top tax rate is 35 percent for people making \$379,150 a year or more.

Progressive estate tax Our budget rescinds the estate tax in the tax deal and replaces it with Sen. Sanders' progressive estate tax. This would generate \$173 billion over 2012-16 and \$330 billion over 2012-21. The policy would include a \$3.5 million exemption followed by a progressive series of marginal tax rates as follows: a 45% rate on the taxable portion of estates up to \$50 million, a 55% rate on the portion of estates up to \$500 million, and a 65% rate on the portion of estates worth over \$500 million.

Tax capital gains and qualified dividends as ordinary income This policy would eliminate the preferentially low rates on long-term capital gains and qualified dividends (currently 15%) and again tax all capital income as ordinary income under the marginal tax rate structure. The tax rate on long-term capital gains is scheduled to rise to 20% in 2013 and dividends are scheduled to be taxed again as ordinary income.

Cap the benefit on itemized deductions at 28%. For itemizing tax filers, the value of itemized deductions rises with their marginal tax rate (the rate on the last dollar earned), which makes many tax code preferences regressive (let alone the fact that non-itemizers see no benefit). This policy would limit the tax benefit of itemized deductions (home mortgage interest, etc.) to 28%.

² Assumes these three tax cuts expire for *all* tax filers, not just those making above \$200,000/\$250,000. The estate tax is treated separately.

Replace the tax exclusion for interest on state and local bonds with a subsidy for the issuer.

The budget would replace the tax exclusion for interest income on state and local government bonds with a direct subsidy to borrowers (i.e., state and local governments), which would be a more cost-effective way of reducing their borrowing costs. Under this policy, state and local governments would make taxable interest payments to borrowers and receive a 15% subsidy from the federal government for the interest paid on those bonds. This would simplify the tax code, increase budgeting transparency, and more cost-effectively subsidize borrowing by state and local governments.

Corporate Tax Reform

Tax U.S. corporate foreign income as it is earned Taxing the earnings of U.S.-controlled foreign subsidiary corporations (incorporated overseas) as earned rather than when earnings are repatriated to the United States would increase domestic investment and make it harder for firms to offshore jobs. The tax deferral on earnings from U.S.-controlled foreign subsidiary corporations enables firms to indefinitely avoid repatriating foreign earnings, because firms are taxed only when foreign earnings are received by the U.S. parent company as dividends. Our budget eliminates the deferral of income from U.S.-controlled foreign subsidiary corporations. Foreign tax credits (reducing U.S. tax liability by the amount of tax paid to foreign governments) would still be allowed, although the credit limits would be treated differently. The U.S. parent corporation would no longer split domestic and foreign expense activities, so the credit would only be allowed against tax liability to foreign governments. Additionally, because all earnings would be treated identically, the differentiation between active and passive foreign income would no longer matter.

Eliminate corporate welfare for oil, gas, and coal companies Our budget repeals exploration and development expensing, preferential tax treatment of royalties, and domestic manufacturing deductions, among other tax preferences, for oil, natural gas, and coal producers.

Reinstate Superfund taxes. The Environmental Protection Agency's Superfund program, once largely funded by dedicated taxes, is now largely funded by general revenue. Having a stable source of funding, rather than relying on year-to-year appropriations, would help plan multi-year cleanup of hazardous chemical waste. The budget would reinstate the Superfund excise taxes that expired in 1995 in order to finance cleanup of hazardous waste.

Enact a financial crisis responsibility fee Our budget levies a leverage tax (0.15% of covered liabilities) on the large banks with more than \$50 billion in assets (as proposed in the President's 2011 budget request).

Wall Street gaming tax A tax on credit default swaps, both sides of futures and forwards, option premiums and foreign exchange spot transactions. This is a tax levied directly against the manipulators who caused the financial crisis.

Reducing tax avoidance and evasion through better compliance and enforcement For our tax system to operate efficiently, we must ensure taxpayers truly fulfill their obligations, this includes and will focus on corporations that notoriously dodge taxes. Revenues will reduce the deficit even further than currently scheduled.

Functional Increases by Proportional Formula for FY12

After recouping significant savings and reforming the tax code so that it is in line with the values of working families, the CPC budget provides a portion of additional discretionary spending with which to increase investment in domestic and international priorities. The following proposed formula would dictate how CPC's additional discretionary spending is allocated by functional category in the alternative budget. Even with additional discretionary spending over current law, the CPC budget still eliminates the deficit within ten years and provides a budget surplus by Fiscal Year 2021.

Function 150: International Affairs (15% plus-up)

- SMART Security
- Foreign Assistance
- U.S. Institute of Peace
- McGovern-Dole International Food for Education and Child Nutrition Program
- Bilateral Global HIV/AIDS Programs (PEPFAR)
- Global Fund to Fight AIDS, Tuberculosis, and Malaria (The Global Fund)
- Global Health and Child Survival – USAID, Maternal Health, Child Health, and Nutrition Programs; USAID, President's Malaria Initiative; USAID, Family Planning and Reproductive Health; USAID, Bilateral Tuberculosis Programs

Function 270: Energy (10% plus-up)

- Renewable energy technology and deployment

Function 300: Natural Resources and Environment (5% plus-up)

- Reestablishment of the Civilian Conservation Corps
- Natural Resources Conservation Service
- Wetlands Reserve Program
- Conservation Stewardship Program

Function 450: Community and Regional Development (5% plus-up)

- Community Development Block Grant (CDBG)
- Community Development Fund

Function 500: Education, Training, and Social Services (20% plus-up)

- ESEA
- IDEA
- Drop-out prevention
- Head Start
- Job Training and Workforce Development
- Youth Summer Jobs
- Social Services Block Grants (SSBG)
- On-the-Job Training
- Early Learning Challenge Fund
- Dislocated Workers Program
- National Endowment for the Humanities

Functional Increases by Proportional Formula for FY12 (con.)

Function 500: Education, Training, and Social Services (con.)

- Senior Community Service Employment Program
- Green Jobs Innovation Fund
- Pell Grants
- TRIO
- National Endowment for the Arts

Function 550: Health (10% plus-up)

- Domestic HIV/AIDS
- Maternal Health
- Enhanced Federal Medical Assistance Percentages (FMAP)
- Community Services Block Grant (CSBG)
- National Institutes of Health (NIH)
- Global Fund to Fight AIDS, Tuberculosis, and Malaria (The Global Fund)
- Mentoring of Children of Prisoners
- Community Health Centers

Function 600: Income Security (20% plus-up)

- Extend and Safeguard Unemployment Insurance
- Child Nutrition
- Supplemental Nutritional Assistance Program (Food Stamps)
- Food and Nutrition Service (including WIC)
- Temporary Assistance for Needy Families (TANF)
- Low Income Housing Energy Assistance Program (LIHEAP)
- Child Care and Development Block Grant (CCDBG)
- Tenant Based Rental Assistance
- Project Based Rental Assistance
- Public Housing Capital Fund
- Public Housing Operating Fund
- Affordable Housing Trust Fund
- Section 8 Housing Vouchers

Function 700: Veterans Benefits and Services (10% plus-up)

- Veterans & Military Families
- Wounded Warriors K-9 Corps

Function 750: Administration of Justice (5% plus-up)

- State and Local Law Enforcement
- Juvenile Justice
- DOJ Administrative Review and Appeals



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THE PEOPLE'S BUDGET

A TECHNICAL ANALYSIS

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INTRODUCTION

The Congressional Progressive Caucus has drafted a progressive budget, titled the *People's Budget*, as an alternative to the House Republican 2012 budget and President Barack Obama's 2012 budget request. The Economic Policy Institute (EPI) has analyzed and scored the specific policy proposals in the *People's Budget* and modeled their cumulative impact on the federal budget over the next decade. The policies in the *People's Budget* reflect the decisions of the Congressional Progressive Caucus leadership and staff, not that of the Economic Policy Institute.¹ The *People's Budget* Department of Defense proposals were crafted by Congressional Progressive Caucus staff in conjunction with Congressional Research Service staff; budgetary scores were provided to the Economic Policy Institute but independent verification is beyond our area of expertise. All other policy proposals have been independently analyzed and scored by EPI based on a variety of other sources, notably data from the Congressional Budget Office, Joint Committee on Taxation, Office of Management and Budget, Tax Policy Center, and Citizens for Tax Justice.

This Working Paper will explain the budget baseline assumptions, the policy choices, policy impacts, and budgetary modeling used in analyzing the *People's Budget*.

A Credible Baseline

The Congressional Budget Office (CBO) March 2011 baseline is the starting point for this analysis, however, we make several adjustments to the current law baseline, which underestimates outlays and overestimates revenue relative to the current policies that will almost certainly be continued beyond their present statutory limits. There are several major differences between current law and current policy baselines, including: the possible continuation beyond their scheduled expiration on December 31, 2012 of some or all of the 2001 and 2003 tax cuts, as modified by the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (H.R. 4853); a continuation of the annual patch of the Alternative Minimum Tax (AMT); prevention of a steep reduction in Medicare physicians payments currently scheduled under the

¹ Many of the policies included in the budget, however, overlap with policies in *Investing in America's Economy: A Budget Blueprint for Economic Recovery and Fiscal Reasonability*, a progressive budget plan released by Our Fiscal Security (OFS), a partnership of The Century Foundation, Demos, and the Economic Policy Institute.

Medicare sustainable growth rate (SGR) formula (i.e., maintaining the “doc fix”); and an extension of some or all of the business tax “extenders” (annually renewed corporate tax credits).

The baseline for our analysis of the *People’s Budget* in this Working Paper indexes the 2011 parameters of the AMT for inflation for the full 10-year budget window at a cost of \$683.0 billion (excluding debt service) over 2012-21 relative to the CBO’s current-law baseline.² The baseline for our analysis also maintains the “doc fix” for the full 10-year budget window at a cost of \$297.6 billion (excluding debt service) over 2012-21.³ These two policy adjustments add \$202.1 billion to debt service over 2012-21.⁴ Beyond the AMT patch, the budget baseline assumes no revenue modifications (specifically no extension of the 2001 and 2003 tax cuts).

Based on these two adjustments, our budget baseline (hereafter referred to as the adjusted CBO baseline) shows deficits falling from \$1.1 trillion (7.0% of GDP) in 2012 to \$581.5 billion (3.4% of GDP) in 2014 and then trending upward.⁵ By 2021, the deficit under our adjusted CBO baseline is projected to reach \$944.9 billion (4.0% of GDP). The budget is never projected to reach primary budget balance (revenue less outlays, excluding debt service), and debt as a share of GDP is projected to gradually trend upward over this entire budget window, from a projected 68.9% of GDP in 2011 to 80.6% of GDP in 2021. All policies presented below are scored against this adjusted CBO baseline.

Composition of the People’s Budget

The policy options that make up the *People’s Budget* fall into five broad categories: public investment, Social Security, health care reform, Department of Defense spending, and tax reform. What follows is a detailed description of the policy choices included in the *People’s Budget* and the outlay or revenue impact of those policies.

² Joint Committee on Taxation, JCX-19-11, Provision I. All years referring to budget windows and budget scores are fiscal years.

³ Provided by House Budget Committee minority staff.

⁴ Ibid.

⁵ All GDP forecasts are in fiscal years as projected in the CBO January 2011 Budget and Economic Outlook: Fiscal Years 2011-21 (see p. 129).

BUDGET PRIORITIES AND POLICY CHOICES

INVESTING IN JOB CREATION AND ECONOMIC GROWTH

The *People's Budget* finances \$1.7 trillion worth of public investment over the coming decade. Specifically, it budgets for a \$212.9 billion for a surface transportation reauthorization bill, including \$30 billion as start-up costs for a national infrastructure bank that would leverage private financing to help rebuild America's public capital stock. These proposals reflect, in part, proposals in the president's 2012 budget. Additionally, the plan budgets for \$1.45 trillion in general public investment over the next decade. The general public investment is front-loaded to put Americans back to work, budgeting for an additional: \$350 billion in 2012; \$300 billion in 2013; \$250 billion in 2014; \$150 billion in 2015; \$125 billion in 2016; \$100 billion in 2017; \$100 billion in 2018; \$50 billion in 2019; and \$25 billion in 2020. All told, \$1.2 trillion would be spent over the next five years. Specific investment proposals for rebuilding the national infrastructure are identified below.

Physical Infrastructure, Particularly Transportation

The *People's Budget* adopts the six-year surface transportation reauthorization proposal in the president's 2012 budget. The plan would rebuild and modernize the national surface transportation infrastructure and expand investments in highways, highway safety, passenger rail, and high-speed rail, among other projects. The proposal includes an up-front investment of \$50 billion above current law for 2012, which the administration estimates will generate hundreds of thousands of jobs over the next few years. The administration's proposal would also allocate \$53 billion for high-speed rail over the next six years.

To help finance these long-term infrastructure improvements, the *People's Budget* plan calls for a National Infrastructure Bank (I-Bank) to leverage private capital and direct investment toward projects of national importance. The *People's Budget* adopts the six-year plan to establish the I-Bank as presented in the president's 2012 budget (part of the six-year surface transportation reauthorization proposal).⁶ The I-Bank would provide loans and grants to support individual projects and broader activities of significance to our Nation's economic competitiveness. For example, the I-Bank could support improvements in road and rail access to a West Coast port

⁶ OMB, Budget of the United States Government, Fiscal Year 2012, Department of Transportation, p. 123.

that benefits farmers in the Midwest, or it could fund a national effort to guarantee private loans made to help airlines purchase equipment in support of the Next Generation Air Transportation System (NextGen). A cornerstone of the I-Bank's approach would be a rigorous project comparison method that transparently measures which projects offer the biggest value to taxpayers and our economy. This marks a substantial departure from the practice of funding projects based on more narrow considerations. Over the 2012-17 period, \$5 billion a year is invested to cover the start-up costs of an I-Bank, which would eventually become self-financing.

According to the CBO, these increased investments in our national transportation would cost \$212.9 billion over the 2012-21 period, relative to current law.⁷ Additional transportation investments could be drawn from the \$1.45 trillion pool of general public investment.

Recapitalizing the Highway Trust Fund

The *People's Budget* proposes raising the motor fuel excise tax by 25 cents as a direct funding mechanism to recapitalize the Highway Trust Fund and finance this surface transportation reauthorization proposal. This policy would increase the federal excise tax on gasoline to 43.4 cents and on diesel fuel to 49.4 cents per gallon. CBO estimates that raising the motor fuel tax by 25 cents would generate \$140.2 billion over the 2012-16 period and \$290.9 billion over the next decade.⁸ The current tax on motor fuels is insufficient to fund today's level of highway spending, which is already inadequate. This policy would also help to correct for the negative social costs (particularly pollution, greenhouse gas emissions, and dependence on foreign oil) of consuming petroleum.

(The president's budget assumed \$328 billion of "Bipartisan financing for Transportation Trust Fund," which the Joint Committee on Taxation did not score because the proposal lacked specifications.⁹)

⁷ CBO, Preliminary Analysis of the President's Budget for 2012, p. 17.

⁸ CBO, "Reducing the Deficit: Spending and Revenue Options," p. 191.

⁹ JCT, JCX-19-11, Provision XIV.

Background: Impact of Public Investments

Ample evidence exists arguing that there is a large deficit in needed physical infrastructure investments in the U.S. economy. Even stronger evidence exists arguing that human capital investments, like universal high-quality pre-kindergarten educational programs, would yield enormous returns that would not only make the overall economy richer. Lastly, the looming threat of global climate change argues for significant resources to be spent to mitigate GHGs and put the economy on a low-GHG track in decades to come.

Furthermore, the more front-loaded these investment efforts are, the better it is for an American economy that looks saddled with a high unemployment rate for years to come. Debt-financed public investments in the next few years will greatly help efforts to drive down joblessness, and the cost of this debt—measured by the long-term costs of borrowing—is historically low. Not only can we afford to front-load public investments today rather than tomorrow, but it also makes absolute economic sense to do so.

Even after the jobs-crisis inflicted by the Great Recession recedes and chronic joblessness begins fading, the case for public investment on its own terms remains strong and needs to be accommodated in our nation’s budgeting.

The Economic Payoff to Ramped-up Public Investment

The research relating public investment to overall economic growth gives us a useful range of estimates about the expected payoff for the public investments financed by the *People’s Budget*.

As noted earlier, the *People’s Budget* finances \$1.7 trillion worth of public investment over the next decade. A quick calculation of the growth impacts of this public investment can be made by comparing this level of investment effort to that contained in *Investing in America’s Economy: A Budget Blueprint for Economic Recovery and Fiscal Responsibility* (OFS 2010). The OFS budget blueprint contained almost \$2.5 trillion in public investments over a 10-year span. Using the results from the research literature as a foundation, OFS estimated that this level of investment effort should be expected to boost growth rates by 0.5% per year.¹⁰ Since the

¹⁰ OFS, “Investing in America’s Economy: A Budget Blueprint for Economic Recovery and Fiscal Responsibility.” Appendix G, p. 68.

People's Budget calls for an investment effort that is roughly two-thirds as large, a rough estimate would be that the investment effort in the *People's Budget* would boost growth by 0.3% annually. Though there is likely to be a growth impact of this investment, the budgetary scores included in the rest of this report are static—that is, they do not include any budgetary impact of expected increases in growth.

It should also be noted that the vast majority of estimates from the research literature examine the effects of investment in public *physical* capital. While this kind of estimate generates large social and economic returns, there are, as noted earlier, even larger potential gains to be had from investment in human capital.

Furthermore, the Council of Economic Advisors have similarly noted that reforms to the health care sector (say, perhaps, those aided by investments in health information technology) that even knock 0.5% off the projected long-run growth rate of health care costs (or just 7% of projected growth rates) would lead to GDP that is nearly 1% higher in 2020 than without this restraint of costs, with payoffs that would just snowball over time.

In short, even outside the traditional investments in physical public capital that yield high returns, there are numerous potential areas for intelligently directed public investments to make the economy much, much richer (and more equitable) in the future that should not be sacrificed to a program of budget austerity.

STRENGTHENING SOCIAL SECURITY

Background: Social Security

Millions of elderly Americans rely on the economic security that comes from the Social Security system. While poverty has risen dramatically as a result of the Great Recession, poverty rates among seniors have actually edged down, largely because of the economic security afforded by the Social Security System; the Census Bureau estimates that Social Security kept 20.5 million Americans, including 14 million seniors and 1.1 million children, out of poverty in 2009.¹¹

¹¹ See “Income, Poverty, and Health Insurance Coverage: 2009,” http://www.census.gov/newsroom/releases/pdf/09-16-10_slides_plot.pdf

The *People's Budget* does not propose any reductions in benefits. The *People's Budget* raises the taxable maximum to include 90% of economy-wide earnings, and eliminates the maximum that employers pay on behalf of their high-income employees. The CBO estimates that increasing the share of total earnings subject to the payroll tax to 90% would require raising the maximum taxable amount to \$170,000 in 2012, up from \$106,800 in 2011.¹² The increase in the taxable maximum on the employee side is gradually phased in over five years. The increase in employer contributions for high earners (those employees earning more than \$106,800) would be phased in immediately. This option maintains the benefits structure as is, and benefit computations would reflect all earnings up to the new taxable maximum on the employee side, although increased employer contributions would not affect benefit computations. This policy raises \$445.0 billion over five years, and around \$1.2 trillion over 10 years. Social Security outlays would increase by \$2.8 billion over 10 years.

Under the current system, income above a taxable maximum is not subject to any Social Security tax, meaning that high-income individuals pay less as a share of their income than everyone else. As income inequality has widened, a greater share of income has fallen outside of the taxable maximum, with the percent of earnings covered by the program slipping from 91% in 1983 to just 83% in 2009.¹³

Our estimates are modeled off of two policy options from the Office of the Chief Actuary. The first option is to “raise the taxable maximum amount (the contribution and benefit base) to include 90% of total OASDI covered earnings. Phase in this increase gradually between 2011 and 2016. Benefit computations would reflect all earnings up to the new taxable maximum,” which is used to calculate the employee side of the policy. The second option would, beginning in 2010, “make all earnings subject to the payroll tax (but retain the current-law taxable maximum for benefit calculations),” which is used to calculate the impact of eliminating the cap on the employer side.¹⁴ Our hybrid option marries these two Social Security Administration policies together, averaging the income rate from both options in our calculations. This score converts income rate, cost rate, and annual balance into dollars using payroll projections from the 2010 Trustees Report and associated tables. The net change in revenue is calculated as the difference between these projections and the original projections.

¹² CBO, “Reducing the Deficit: Spending and Revenue Options,” p. 169.

¹³ Ibid.

¹⁴ See policies E2.1 and E2.5: <http://www.ssa.gov/oact/solvency/provisions/payrolltax.html/>

BUILDING ON HEALTH CARE REFORM

Background: Health Care Reform

Access to quality, affordable health care is necessary for a strong middle class, but spiraling health care costs have strained the budgets of working-class families in recent decades. Health care excess cost growth (growth in per capita national health care expenditure exceeding per capita GDP growth) poses a grave challenge for families, businesses, state and local governments, as well as the federal government. Consequently, policies that merely shift costs from the federal budget to consumers, businesses, and state and local budgets are nothing but “band aid” solutions masking an underlying ailment. Beyond avoiding cost shifting, budget policy should also acknowledge that the current health insurance system suffers from numerous market failures and government purchasing power is one of the few checks available for price containment in a scattered, often uncompetitive industry.

The *People’s Budget* adopts policies that build on the health care reform laws passed last year in order to assure access to affordable, quality care and expand coverage to Americans. The CBO estimates that health care reform will increase the number of nonelderly Americans with health insurance by roughly 34 million by 2021, allowing greater risk pooling and decreasing uncompensated costs that are passed along via insurance premiums.¹⁵ The CBO also estimates that recent health care reform legislation will reduce deficits by \$210 billion over the 2012-21 period and decrease budget deficits by roughly half a percent of GDP in the following decades, saving literally trillions of dollars.¹⁶

Offer a Public Insurance Plan to the Health Insurance Exchanges

Beginning in 2014, national health insurance exchanges will be established (as a result of health care reform) through which individuals and families may purchase private coverage, increasing competition in largely fragmented, regional insurance markets. Under this option, the Secretary of the Department of Health and Human Services would administer a public health insurance plan to be offered alongside private plans through the exchanges. The public plan would exploit economies of scale to negotiate payment rates for prescription drugs, would pay physicians

¹⁵ CBO, “CBO’s Analysis of the Major Health Care Legislation Enacted in March 2010,” p. 1.

¹⁶ CBO, “CBO’s Analysis of the Major Health Care Legislation Enacted in March 2010,” p. 2, 28.

roughly 5% more than Medicare reimbursement rates, and would pay hospitals and providers comparable rates as paid under Medicare. Based on the potential for administrative and other savings, the CBO estimates that insurance premiums for the public plan would be roughly 5-7% lower than private plans offered in the insurance exchanges.¹⁷

According to the CBO, this option would lower deficits by \$17.4 billion from 2012 to 2016, and by \$88.0 billion from 2012 to 2021. Over the next decade, outlays would fall by \$26.7 billion (a reduction in targeted subsidies for the purchase of insurance in the exchanges) and a \$61.2 billion increase in revenue (largely resulting from interactions with the tax exclusion for employer-sponsored health insurance).

Negotiate Drug Prices With Pharmaceutical Companies

Background: Pharmaceutical Rebate

When enacted, Medicare Part D (the prescription drug benefit) failed to harness the purchasing power of the federal government to negotiate wholesale prices for pharmaceutical drugs. This proposal applies the Medicaid approach to negotiating drug prices to Medicare Part D, increasing the rate of rebate from pharmaceutical companies to the federal government by around 15 percentage points. Currently, individual insurance plans with considerably less market power negotiate prescription drug rebates; consequently, Medicare Part D rebates averaged only 8.1% in 2006.¹⁸ By comparison, health care reform increased the Medicaid rebate rate for single-source drugs from 15.1% to 23.1%.

The Bipartisan Policy Center's (BPC) report, *Restoring America's Future*, estimated that negotiating drug prices would save \$100 billion over the 2012-18 period. The BPC report proposed ending guaranteed Medicare in 2019 (changing the program to a premium support system similar to vouchers), ending the ability of the government to harness economies of scale to negotiate pharmaceutical drug prices. The budgetary impact of this proposal is extrapolated beyond 2018 by indexing savings to projected per capita health expenditure.¹⁹ Based on this

¹⁷ CBO, "Reducing the Deficit: Spending and Revenue Options," p. 33.

¹⁸ Bipartisan Policy Center, "Restoring America's Future," p. 54.

¹⁹ CBO estimates that per capita national health care expenditure will average nearly 5% over the next 75 years. See letter to Congressman Paul Ryan, January 27, 2010, p. 3. <http://www.cbo.gov/ftpdocs/108xx/doc10851/01-27-Ryan-Roadmap-Letter.pdf>

extrapolation, negotiating drug prices with pharmaceutical companies would save an estimated \$157.9 billion over the 2012-21 period.

Centers for Medicare and Medicaid Services Program Integrity Savings and Other Medicare and Medicaid Savings in the President's Budget

The *People's Budget* adopts a series of health care savings included in the president's 2102 budget request that are meant to compliment and strengthen health care reform (proposals intended to offset the "doc fix" through 2013 in the president's budget). Major proposals include reducing the Medicaid provider tax threshold in 2015, tracking high prescribers and utilizers of prescription drugs in Medicaid, strengthening Medicaid third-party liability, and recovering erroneous Medicare Advantage payments. According to the Office of Management and Budget (OMB), these proposals would collectively save \$17.2 billion over the 2012-16 period and \$62.2 billion over the 2012-21 period.²⁰

As noted in the discussion of baselines, the budget includes the cost of maintaining the "doc fix" for a full decade; the combined health savings in the *People's Budget* more than offset the cost of maintaining the doc fix over a decade.

REALIGNING DEPARTMENT OF DEFENSE PRIORITIES

Background: Recent Defense Spending

Base funding for the Department of Defense more than doubled in nominal terms from 2000 to 2009. While the Pentagon has largely operated with loose budget constraints for well over a decade, the wars have been conducted without any semblance of a budget constraint or, until recently, honest budgeting. Additional funding for military operations for Afghanistan, Iraq, and other combat missions has totaled \$1.3 trillion over the 2001-11 period, of which \$1.1 trillion went to the Department of Defense.²¹ These overseas contingency operations (OCOs) have been financed almost entirely off-budget in emergency supplemental appropriations bills. The president's budget requested \$126.5 billion for OCOs in 2012 and includes a \$50 billion annual placeholder thereafter, for total costs of \$576.5 billion over from 2012 through 2021.²²

²⁰ OMB, Budget of the United States Government, Fiscal Year 2012, Summary Tables S-8, p 196.

²¹ CBO, January 2011 Budget and Economic Outlook: Fiscal Years 2011-21, p. 77.

²² OMB, Budget of the United States Government, Fiscal Year 2012, Summary Tables S-10, p 198.

Over the last two years, a rare consensus has emerged among a wide range of Washington policymakers: any deficit reduction plan must tackle Department of Defense spending. Budget proposals ranging from the president's budget request to reports from the National Commission on Fiscal Responsibility and Reform, the Bipartisan Policy Center, and Our Fiscal Security, among others, all agree that defense spending needs downward adjustment. Other proposals have stressed that overseas contingency operations should be placed on budget or financed by a war tax.²³ Along with this newfound political resolve, specific plans have emerged for realigning our defense priorities. Notably, the Sustainable Defense Task Force (SDTF), a bipartisan group of defense experts, released a report in June 2010 that detailed a series of options, which, if taken together, would save \$960 billion over a decade.²⁴

Responsibly End the Wars in Iraq and Afghanistan

The *People's Budget* accounts for an end to the wars in Iraq and Afghanistan. As noted above these operations have cost \$1.3 trillion, excluding debt service. The *People's Budget* provides \$161.4 billion in OCO funding for 2012 (the funding level in the CBO baseline), after which all OCO funding is ended. The Congressional Research Service estimates that this sum would be more than sufficient to safely and deliberately withdraw American soldiers from Afghanistan and Iraq. Responsibly ending the wars in Afghanistan and Iraq will save \$1.6 trillion over the 2013-21 period, relative to the CBO baseline. Relative to the highly uncertain costs budgeted for in the president's 2012 budget, this withdrawal would save \$415.1 billion.²⁵

Reduce Base Department of Defense Spending

Specific proposals for conventional forces include: reducing active duty Army personnel strength to 427,000 by 2014 (a decrease of 120,000); reducing the Marine Corps personnel strength by 30% to a force of 145,000 by 2014; reducing the Navy by 20% to a fleet of 230 ships; and reducing the Air Force by 15%, reducing the number of squadrons by 18 of 60. These force structure savings would total \$593.7 billion over the 2012-21 period. Specific proposals for strategic capabilities include reducing the U.S. nuclear arsenal, cancelling the Trident II missile, limiting modernization of nuclear weapons infrastructure and research, and selectively curtailing

²³ Galston, Bill and Maya MacGuineas. "The Future is Now: A Balanced Plan to Stabilize Public Debt and Promote Economic Growth," 2010, p. 8.

²⁴ Sustainable Defense Task Force. "Debt, Deficits, and Defense." June 2010.

²⁵ OMB, Budget of the United States Government, Fiscal Year 2012, Summary Tables S-11, p 200.

missile defense and space programs. No savings are assumed from TRICARE, the military health care program for active duty personal, military retirees, and their dependents.

These proposals and their respective budgetary impact were compiled by Congressional Progressive Caucus staff in conjunction with Congressional Research Service staff and provided to EPI. Overall, these policy proposals would gradually reduce defense appropriations by \$692.2 billion over the 2012-21 period, relative to the CBO baseline. Relative to higher spending levels in the president's budget request, they would represent \$816.7 billion in savings over the next decade. In both cases, the savings are well within the bounds of the savings identified as reasonable by the SDTF report.

Taken in conjunction with ending the wars in Afghanistan and Iraq, the realignment of conventional and strategic forces would result in \$2.3 trillion worth of savings relative to the adjusted CBO baseline.

TAX REFORM AND MODERNIZATION

Reforming Taxation on Individual Income and Wealth

Transparently Budget for Alternative Minimum Tax Relief

As noted in the discussion of the adjusted CBO baseline, the *People's Budget* indexes the 2011 parameters of the AMT to inflation.

Allow the Bush-era Tax Cuts to Expire but Extend Marriage Relief, Credits, and Incentives for Children, Families, and Education

Background: Bush-era Tax Cuts

The Bush-era tax cuts were and continue to be costly and ineffective at fostering economic growth. Of all the post-war business cycles, the economic expansion of 2001-07 saw the worst growth in gross domestic product, investment, employment, total compensation, wages and salaries, and labor force participation (measured trough to peak: 2001Q4 to 2007Q4).²⁶ The Bush-era tax cuts were also objectively regressive, conferring a disproportionate benefit to high

²⁶ Bivens, Josh and John Irons. "A Feeble Economic Recovery: The fundamental weakness of the 2001-07 expansion." Economic Policy Institute, December 9, 2009, p. 7.

earners capturing a majority of new income.²⁷ According to the CBO, extending all the Bush-era tax cuts (as modified by December’s tax deal) would decrease revenue by \$2.5 trillion over 2012-21 and add \$3.0 trillion to deficits accounting for additional debt service, relative to current law. Because the Bush-era tax cuts reduced income tax liability without making corresponding adjustments for the AMT, the cost of extending the Bush tax cuts and patching the AMT is much higher than either proposal calculated separately. According to the CBO, extending the Bush tax cuts and indexing the 2011 parameters of the AMT would decrease revenue by \$3.8 trillion over 2012-21 and add \$4.6 trillion to deficits (accounting for additional debt service, relative to current law).²⁸

The *People’s Budget* allows the Bush tax rate cuts to expire on schedule on December 31, 2012. The *People’s Budget* does, however, selectively continue a handful of provisions helping middle-class families. Specifically, the *People’s Budget* maintains marriage-penalty relief, the expanded child tax credit, education incentives, and other incentives for children and families that would add \$261.7 billion to deficits over the 2012-16 period and \$698.5 billion over the 2012-21 period.²⁹

Specifically, marriage penalty relief expanding the standard deduction for joint-filers, the extension of the 15% tax rate for joint-filers, and the \$5,000 extension of the EITC phase-out for joint-filers is continued at a cost of \$355.1 billion. The higher \$1,000 child tax credit and the lower \$3,000 earnings threshold for the refundable portion of the child tax credit are extended at a cost of \$317.5 billion over the 2012-21 period. The dependent care credit, adoption credit, and employer-provided child care credit are extended at a cost of \$8.8 billion over the 2012-21 period. Lastly, education incentives—including preferential tax treatment of Coverdell Education Savings Accounts, employer provided education assistance, student loan interest, select tax free scholarships, and tax exempt bonds for school construction—are extended at a cost of \$17.0 billion. The scores for all of these proposals are taken from the Joint Committee for Taxation’s *Estimated Budget Effects of the Revenue Provisions Contained in the President’s Fiscal Year*

²⁷ Leiserson, Greg and Jeff Rohaly. “Distribution of the 2001-2008 Tax Cuts: Updated Projections, July 2008.” Urban-Brookings Tax Policy Center, July 2008.

²⁸ CBO, January 2011 Budget and Economic Outlook: Fiscal Years 2011-21, Table 1-7.

²⁹ Excluding interaction effects.

2012 Budget Proposal.³⁰ With the exception of the extended 15% tax rate for joint filers (i.e., marriage-penalty relief), the tax structure would revert to Clinton-era rates in 2013.

Rescind the Upper-Income Tax Cuts in December's Tax Deal

As noted above, the *People's Budget* would allow the Bush tax rate structure to expire on schedule when last December's tax deal expires on December 31, 2012. The *People's Budget* would, however, immediately rescind the upper-income tax cuts, instead maintaining only those tax cuts for individuals earning less than \$200,000 and joint-filers earning less than \$250,000. Specifically, the budget would let the 33% and 35% tax brackets revert to 36% and 39.6%, respectively; reinstate the limitation on itemized deductions and personal exemption phase-out; and end all capital gains and dividends tax cuts.³¹ Collectively, these upper-income tax costs are projected to cost \$94.9 billion over 2012-14 (the revenue impact from capital gains tax cut spills into 2014). The scores for these proposals are taken from JCT's *Estimated Budget Effects of the "Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010."*³² This proposal would also increase revenue for 2011 (before the 10-year budget window), but the related interest effects from lower borrowing costs this fiscal year are ignored.

Enact a Progressive Estate Tax

Background: Recent Estate Tax Cut

December's tax deal increased the estate tax exemption to \$5 million (\$10 million for married couples) and reduced the maximum tax rate above that exemption to 35% through December 31, 2012. Relative to then-current law, which would have seen the exemption amounts fall back to \$1 million (\$2 million for married couples) and a maximum tax rate of 55%, this tax cut cost \$68.1 billion. Relative to the estate and gift tax cuts proposed in the president's budget, this represented a tax cut that benefited only the wealthiest one-quarter of one percent of households.

³⁰ JCT, JCX-19-11, Provisions II: B. Marriage Relief, C. Child Tax Credit, D. Family Incentives, and F. Education Incentives.

³¹ Truly holding harmless all tax filers below the \$200,000/\$250,000 threshold would require slightly extending the 28% tax bracket, as proposed in the president's 2011 budget request, but this proposal does not extend the 28% bracket because of data limitations for the revenue impact.

³² JCT, JCX-54-10, Provisions I. A.1.c.d. and B.1,2.

The *Peoples' Budget* would rescind the estate tax cut in December's deal and replace it with Senator Bernie Sanders' (I.-Vt.) Responsible Estate Tax Act (S. 3533).

The policy would include a \$3.5 million exemption (\$7 million for married couples), leaving 99.75% of all estates fully exempt. The taxable portion of estates beyond these exemptions would be subject to a progressive series of marginal tax rates as follows: a 45% rate up to \$10 million; a 50% rate up to \$50 million; a 55% rate up to \$500 million; and a 65% rate on the portion of estates worth over \$500 million.³³ Combined with rescinding the estate tax cuts in December's tax deal, this progressive estate tax would generate \$173.0 billion over the 2012-16 period and \$330.1 billion over the 2012-21 period.³⁴

Enact the Fairness in Taxation Act

The *People's Budget* would adopt Representative Jan Schakowsky's (D.-Ill.) Fairness in Taxation Act (H.R. 1124), which would create several new tax brackets for high-income earners: \$1-10 million would be taxed at 45%; \$10-20 million, 46%; \$20-100 million, 47%; \$100 million to \$1 billion, 48%; \$1 billion and over would pay 49%. The bill would also tax capital gains and dividend income as ordinary income for those taxpayers with income over \$1 million. Citizens for Tax Justice (CTJ) estimate that the Fairness in Taxation Act would generate \$748.2 billion over the 2011-20 period.³⁵ Extrapolating from this score, Rep. Schakowsky's Fairness in Taxation Act is projected to generate \$401.5 billion in revenue over the 2012-16 period and \$872.5 billion over the 2012-21 period.³⁶

Tax Capital Gains and Qualified Dividends as Ordinary Income

Background: Tax Preference for Investment Income

The tax code gives preferential rates to investment income relative to earned income. The Bush-era tax cuts lowered the rate on long-term capital gains and qualified dividends to 15%—a full 20 percentage points below the reduced top marginal tax rate. High-income individuals are

³³ Press Release: Sanders Bill Restores Estate Tax on Billionaires, June 24, 2010, Office of Senator Bernie Sanders, for more details.

³⁴ This score is based on a JCT score of S. 3533 that was not made publicly available. The base policy proposal would generate revenue of \$225.4 billion over 2010-20. The revenue impact for 2021 is extrapolated by adjusting the 2020 revenue level for nominal GDP growth.

³⁵ This score is not publicly available.

³⁶ The revenue impact for 2021 is extrapolated by adjusting the 2020 revenue level for nominal GDP growth.

currently able to shift their form of compensation from ordinary income to capital gains, and as a result, the lower rate on capital gains allows the very wealthy to avoid paying their fair share. In this way, the tax code favors income derived from wealth rather than income from work and “human capital.” Even Ronald Reagan recognized the value of treating income from work the same as income from wealth when he signed the Tax Reform Act of 1986, calling the bill a “sweeping victory for fairness.” Prior to the Bush-era tax cuts, dividends were still taxed as ordinary income, and are scheduled to be taxed as ordinary income when last December’s tax deal expires on December 31, 2012.

The *People’s Budget* would eliminate the preferentially low rates on long-term capital gains and qualified dividends, and it would tax all capital income as ordinary income under the marginal tax rate structure. The Tax Policy Center (TPC) estimated that taxing capital gains and qualified dividends as ordinary income would generate \$989.8 billion over the 2007-17 period, relative to then-current law (the Bush-era tax cuts would have expired for all years in the 2012-21 budget window).³⁷ Extrapolating from this score, taxing capital income as ordinary income is projected to generate \$1.0 trillion in savings over the 2012-21 period.³⁸

In order to harmonize tax rates between capital and ordinary income, the Medicare Hospital Insurance (HI) 0.9% surcharge on earned income and the 3.8% surcharge on investment income for high earners (included in the Patient Protection and Affordable Care Act (PPACA) of 2010) must also be repealed. The PPACA surcharges were estimated to generate \$201.3 billion over the 2012-19 period.³⁹ Extrapolating from this score, the repeal of the PPACA surcharges would decrease revenue by \$292.4 billion over the 2012-21 period. Adjusting the TPC score for eliminating the PPACA surcharges, this policy is projected to generate \$736.7 billion over the 2012-21 period.

As noted earlier, however, Rep. Schakowsky’s Fairness in Taxation Act would also tax capital gains and qualified dividends as ordinary income for individuals earning over \$1 million. The *People’s Budget* intends to tax all investment income as ordinary income, so this score is only meant to tax investment income as ordinary income for tax filers earning less than \$1

³⁷ TPC, T07-0212 - Tax Capital Gains and Qualified Dividends as Ordinary Income, Static Impact on Individual Income Tax Liability and Revenue (\$ billions), 2007-17.

³⁸ Relative to then-current law and irrespective of rescinding the capital gains tax cuts in December’s tax deal.

³⁹ JCT, JCX-17-10, Title I.15.

million. The \$736.7 billion over 2012-21 estimate of taxing capital gains and dividends at a top rate of 39.6% (relative to the current law baseline for this estimate) is adjusted accordingly to avoid double counting. According to TPC, tax units earning over \$1 million account for 55.9% of the share of total taxes on capital gains and qualified dividends.⁴⁰ Correspondingly, our revenue estimate is adjusted to reflect the 44.1% share paid by tax units earning less than \$1 million. With this adjustment, taxing capital gains and qualified dividends as ordinary income for those tax filers unaffected by the Fairness in Taxation Act is projected to generate \$324.9 billion over 2012-21.

Limit the Benefit on Itemized Deductions for High Earners

Background: Regressivity of Itemized Reductions

Itemized deductions tend to be regressive because their value is larger for those in higher tax brackets and because they do not benefit tax filers claiming the standard deduction (typically lower-income workers). For example, the mortgage interest deduction—the second most costly tax expenditure—is worth 35 cents on the dollar to someone with an income of \$1 million, but just 15 cents on the dollar to an itemizing married couple earning \$60,000. It has no value at all for a family taking the standard deduction.

The *People's Budget* would decrease the regressivity of itemized deductions while maintaining incentives built into the tax code by limiting the rate at which itemized deductions can reduce tax liability to a maximum of 28%. This policy would only affect itemizing tax filers currently in the top two income brackets. The president's budget also proposed limiting the value of itemized deductions to 28%. This policy would generate \$293.3 billion over 2012-21 period.⁴¹

⁴⁰ TPC, "T09-0483 - Distribution of Taxes on Long-Term Capital Gains and Qualified Dividends by Cash Income Level, 2010, Baseline: Current Law," December 14, 2009. The baseline for this distributional analysis assumes current law with no tax on long-term capital gains that would be subject to lower rate.

⁴¹ JCT, JCX-19-11, Provision XI.

Replace the Tax Exclusion for Interest Income on State and Local Bonds With a Direct Subsidy for the Issuer

Background: Tax Preference for Municipal Bonds

Bonds issued by state and local governments receive preferential tax treatment. Interest from public purpose state and local government bonds can be excluded from a bondholder's adjusted gross income. According to OMB, the exclusion on interest from public purpose state and local bonds will result in forgone revenue of \$230.4 billion over the 2012-16 period, making this preference one of the most expensive tax expenditures.⁴² This preferential tax treatment acts as an indirect subsidy, reducing borrowing costs for state and local governments. The current tax treatment also confers a disproportionately larger tax benefit for upper-income earners.

The *People's Budget* would replace the tax exclusion for interest with a direct subsidy to borrowers (i.e., state and local governments), which would be a more cost-effective way of reducing their borrowing costs. Under this policy, state and local governments would make taxable interest payments to borrowers and receive a 15% subsidy from the federal government for the interest paid on those bonds. This would simplify the tax code, increase budgeting transparency, and more cost-effectively subsidize borrowing by state and local governments. According to the CBO, this policy would generate \$30.5 billion over 2012-16 and \$142.7 billion over 2012-21.⁴³

Corporate Tax Reform and Responsibility Fees

Financial Crisis Responsibility Fee

The *People's Budget* would impose a fee on large financial institutions. Specifically, the budget would impose a leverage tax (0.15% of covered liabilities) on large banks with more than \$50 billion in assets (as proposed in the president's budget request). According to the CBO, imposing such a tax could generate \$31.3 billion over the 2012-16 period and \$70.9 billion over the full 2012-21 period, recouping more than three-fold the net taxpayer cost of the Troubled Asset

⁴² OMB, Budget of the United States Government, Fiscal Year 2012, Analytical Perspectives, Federal Receipts, p. 244.

⁴³ CBO, "Reducing the Deficit: Spending and Revenue Options," p. 163.

Relief Program (TARP).⁴⁴ The fee would provide an incentive for large firms to decrease their liabilities, helping to rectify the problem of “too big to fail” financial institutions that was made all too apparent during the financial crisis. The proposal would also help to level the playing field between small financial institutions (which do not benefit from an implicit government guarantee because they are not viewed as “systemically important” by credit markets) and larger financial institutions.

Derivatives and Speculation Tax

The *People’s Budget* would impose a small tax on transactions of exotic financial products. Assuming a 25% behavioral reduction in transactions resulting from a tax, Dean Baker and Robert Pollin estimate that various taxes on financial derivative products (financial instruments deriving their value from some other underlying asset, such as a stock, currency, or index) could generate upwards of \$63.5 billion annually.⁴⁵ Specifically, a tax on swaps (taxed at 0.01% per year to maturity and assuming an average life to maturity of 1.5 years)—including credit default swaps—could generate roughly \$34.8 billion. A tax of 0.01% on each side of futures and forwards transactions could generate roughly \$10.7 billion. A 0.5% tax on option premiums (the right to purchase a stock at a set price at a future date) could generate roughly \$6.3 billion. Additionally, a 0.01% tax on all foreign exchange spot transactions could generate roughly \$11.7 billion annually (this latter option is a proper “Tobin tax,” rather than a derivatives tax). Their revenue estimate, calculated on 2008 transactions volumes, is assumed for 2012 and held constant as a share of the economy.

The behavioral response to such a tax is uncertain. Evidence from the United Kingdom, which imposes a 0.5% “stamp duty” on registration and ownership of stocks and bonds, suggests that the behavioral effects are relatively muted. Econometric studies of the U.K. transactions tax suggest that “a 10% increase in transactions costs reduces turnover by 10% to 17% in the long run.”⁴⁶ Similarly, Hawkins and McCrae (2002) estimate that halving the stamp duty would

⁴⁴ CBO estimates the total subsidy cost of TARP will total \$19 billion. See “Report on the Troubled Asset Relief Program—March 2011,” p. 4. See CBO “Reducing the Deficit: Spending and Revenue Options,” p. 201.

⁴⁵ Baker, Dean, Robert Pollin, Travis McArthur, and Matt Sherman. “The Potential Revenue from Financial Transactions Taxes,” December 2009, p. 2.

⁴⁶ Campbell, John and Kenneth Froot. 1994. “International Experiences with Securities Transactions Taxes.” NBER

increase turnover on U.K. stock exchanges by roughly 20%.⁴⁷ The tax rates on derivative and speculative financial products proposed by the *People's Budget* would represent a smaller relative increase in transactions costs, so a 25% reduction in transactions seems reasonable, if not conservative. A larger behavioral response would decrease revenue relative to projected levels, but would conversely further the policy goal of taming speculation and encouraging more productive investment. Assuming a larger 50% reduction in transaction, Baker and Pollin estimate that these speculation taxes would raise \$43.2 billion annually.

Eliminate Fossil Fuel Tax Preferences

The president's budget requests have repeatedly proposed eliminating a handful of tax preferences carved out for fossil fuel producers over the years. Eliminating this tax code spending would help level the playing field between renewable energy sources and fossil fuels. The *People's Budget* would eliminate fossil fuel tax preferences as detailed by the president's budget. Specifically, this policy would repeal exploration and development expensing, preferential tax treatment of royalties, and domestic manufacturing deductions, among other tax preferences, for oil, natural gas, and coal producers.⁴⁸ Repeal would save \$21 billion over the 2012-16 period and \$41 billion over the 2012-21 period.⁴⁹

Reinstate Superfund Taxes

The Environmental Protection Agency's Superfund program, once largely funded by dedicated taxes, is now largely funded by general revenue. Having a stable source of funding, rather than relying on year-to-year appropriations, would help plan multi-year cleanup of hazardous chemical waste.

The *People's Budget* would reinstate the Superfund excise taxes that expired in 1995 in order to finance cleanup of hazardous waste. Specifically, this policy would re-impose an excise tax of \$0.22 to \$4.87 per ton on various chemicals, an excise tax of 9.7 cents per barrel of crude or refined petroleum, and a corporate income tax of 0.12% on modified alternative minimum

⁴⁷ Hawkins, Mike and Julian McCrae. 2002. "Stamp duty on share transactions: is there a case for change?" Institute for Fiscal Studies.

⁴⁸ JCT, JCX-19-11, Provision VIII.A,B.

⁴⁹ OMB, Budget of the United States Government, Fiscal Year 2012, Analytical Perspectives, Federal Receipts, p. 177.

corporate income above \$2 million. According to the CBO, this policy option would generate \$19.4 billion over the 2012-21 period.⁵⁰

Tax U.S. Corporate Foreign Income as It Is Earned

The tax deferral on earnings from U.S.-controlled foreign subsidiary corporations enables firms to indefinitely avoid repatriating foreign earnings, because firms are taxed only when foreign earnings are received by the U.S. parent company as dividends. Consequently, U.S. firms have parked more than \$1 trillion in profits overseas.⁵¹ In 2004, a repatriation holiday allowed firms to bring overseas profits back subject to a tax rate of just 5%—30 percentage points below the normal corporate tax rate.

The *People's Budget* would eliminate the deferral of income from U.S.-controlled foreign subsidiary corporations and instead tax all foreign earnings as earned. Foreign tax credits (reducing U.S. tax liability by the amount of tax paid to foreign governments) would still be allowed, although the credit limits would be treated differently. The U.S. parent corporation would no longer split domestic and foreign expense activities, so the credit would only be allowed against tax liability to foreign governments. Additionally, because all earnings would be treated identically, the differentiation between active and passive foreign income would no longer matter (the “active financing” exception for U.S.-controlled foreign financing subsidiaries would be closed). According to the CBO, this policy would generate \$49.7 billion over the 2012-16 period and \$114.2 billion over the 2012-21 period.⁵²

ADDING IT ALL UP

Based on the policy adjustments noted above, the *People's Budget* would reduce primary spending by \$868.9 billion, increase general revenue by \$2.8 trillion, and increase payroll tax receipts by \$1.2 trillion over a decade relative to the adjusted CBO baseline. Responsibly ending the wars in Afghanistan and Iraq and recalibrating Department of Defense priorities would save \$2.3 trillion. Roughly \$1.7 trillion would simultaneously be invested for general public investment and a surface transportation reauthorization bill, including an I-Bank. Health care

⁵⁰ CBO “Reducing the Deficit: Spending and Revenue Options,” p. 203.

⁵¹ Rubin, Richard and Steven Sloan, Bloomberg, “Republican Tax Chiefs Cool to Cisco, EMC Offshore Proposal,” March 24, 2011.

⁵² CBO, “Reducing the Deficit: Spending and Revenue Options,” p. 186.

savings would decrease deficits by \$308.1 billion from 2012 to 2021, more than offsetting the 10-year cost of maintaining the current rate of Medicare physician reimbursements, adjusted for inflation. Based on all of these policy adjustments, net interest payments are projected to fall by \$856.3 billion over 2012-21.⁵³ In total, the *People's Budget* would reduce deficits by \$5.6 trillion over 2012-21 relative to the adjusted CBO baseline.

The *People's Budget* is projected to turn from budget deficit to budget surplus in 2021, with a surplus of \$30.7 billion (0.1% of GDP) in that year. That surplus compares with a deficit of 3.1% of GDP under the CBO baseline and 4.0% of GDP under the adjusted CBO baseline (see **Figure 1**). The budget would hit primary surplus (revenues less non-interest outlays) in 2014. The budget is projected to run a primary surplus of 2.9% of GDP by 2021, compared with a primary surplus of 0.3% of GDP under the CBO baseline and a primary deficit of 0.4% of GDP under the adjusted CBO baseline (see **Figure 2**). After climbing to 73.9% of GDP in 2013, debt as a share of the economy would trend downward after reaching primary budget balance. By 2021, debt as a share of GDP would fall to 64.1%, down from 75.6% of GDP under the CBO baseline and 80.6% of GDP under the adjusted CBO baseline (see **Figure 3**).

The *People's Budget* is projected to run lower deficits and place public debt on a more sustainable trajectory than either the House Republican Budget or the president's budgets. The projected surplus in 2021 (0.1% of GDP) compares with a deficit of 1.6% of GDP under the House Republican Budget⁵⁴ and 4.9% of GDP under the president's budget (see **Figure 4**). The *People's Budget* is projected to bring debt as a share of GDP in 2021 to 64.1%, compared with debt at 67.5% of GDP under the House Republican Budget and 87.4% of GDP under the president's budget (see **Figure 5**).

MECHANICS OF BUDGET MODELING

The Economic Policy Institute has modeled the impact of the *People's Budget* to adjust for lower borrowing needs and decreased debt-service costs. The March 2011 CBO baseline—including revenue, outlays, deficits, debt, and net interest payments—are first adjusted for the “doc fix” and the AMT patch, as described in the discussion of the adjusted baseline. The budget

⁵³ See Mechanics of Budget Modeling for an explanation of net interest calculations.

⁵⁴ See “The Path to Prosperity: Fiscal Year 2012 Budget Resolution,” Table S-1, p. 63. These reflect the analysis of the House Budget Committee majority staff, which may overstate the impact on deficits. See Horney, Jim. 2011. “Ryan Budget Plan Produces Far Less Real Deficit Cutting than Reported,” CBPP.

estimation first calculates the net impact of all policies for a given year, excluding net interest effects (later estimated as a residual of other parameters). Growth in public debt is then adjusted accordingly, with subsequent interest payments calculated from downwardly adjusted public debt levels.

Specifically, net interest is calculated on a year-by-year basis from adjusted total public debt and the effective interest rate for the U.S. Treasury Department. The effective interest rate (net interest/public debt) represents an average borrowing cost weighted across the average maturity of debt. Based on the March 2011 CBO baseline, this effective nominal borrowing cost is projected to trend upwards from 2.2% in 2012 to 4.5% by 2021. This is a static model in the sense that borrowing costs are fixed, ignoring expected changes in economic projections that would result from the deficit reduction policies in the budget. Everything else being equal, reducing the debt-to-GDP ratio by more than 16 percentage points by 2021 would likely result in a lower borrowing cost than assumed here. In other words, these are somewhat conservative estimates.

For 2012, adjusted CBO baseline debt in 2011 is again adjusted for the baseline loan expansion for 2012 and the net impact of policies in 2012, excluding net interest effects. Then for 2013, we calculate an adjusted debt-service cost based on our alternate debt level for 2012 and the baseline effective interest rate. Netting out the baseline interest outlays, we generate an adjustment to total interest outlays for 2013. For 2013, we adjust our alternative debt path for policy adjustments excluding debt service, the previously calculated interest adjustment, and the baseline loan expansion. Continuing in this fashion, we generate an interest adjustment that compounds policy choices over time and correspondingly a dynamic alternative debt path. Finally, we combine the net interest adjustment with the policy-adjusted deficit excluding net interest effects to estimate bottom line-budget deficits for the *People's Budget*.

This is admittedly a less sophisticated model for interest costs than employed by the CBO. We have reason to believe, however, that these net interest estimates are on the conservative side. Net interest adjustments of \$856.3 billion under this model total 17.9% of the \$4.8 trillion worth of non-interest deficit adjustments. By way of contrast, the ratio of debt-service costs to non-interest deficit adjustments averages 20.6% across the eight policies scores in “Budgetary Effects of Selected Policy Alternatives Not Included in CBO’s Baseline” (Table 1-7) of the CBO January 2011 baseline.

Finally, it should be noted that possible interaction effects between tax policies are not taken into consideration in this budget model; running the combined tax policies through a micro simulation model was beyond the scope of our technical support for budget modeling.

Figure 1. Deficits Relative to Baseline Projections

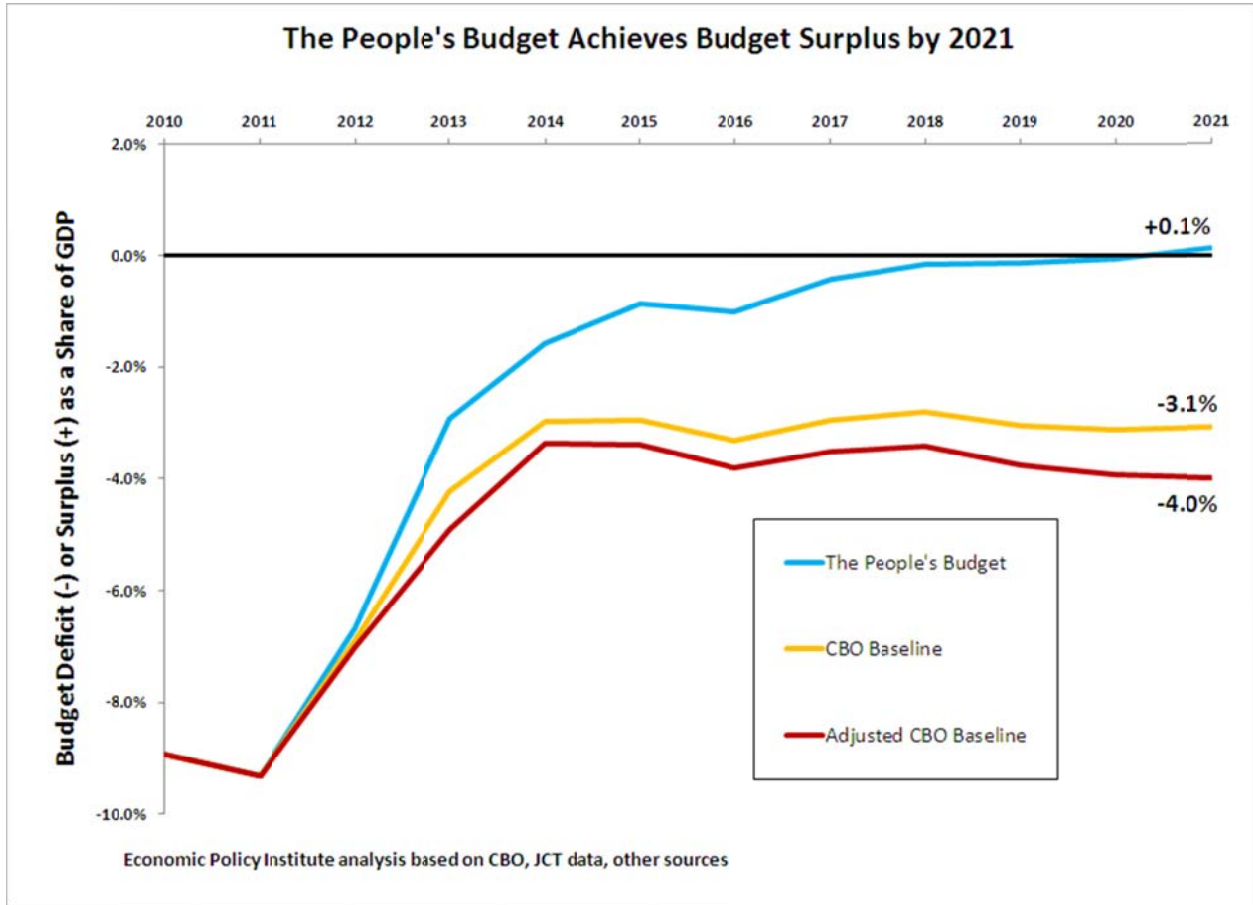


Figure 2. Primary Budget Deficit Relative to Baseline Projections

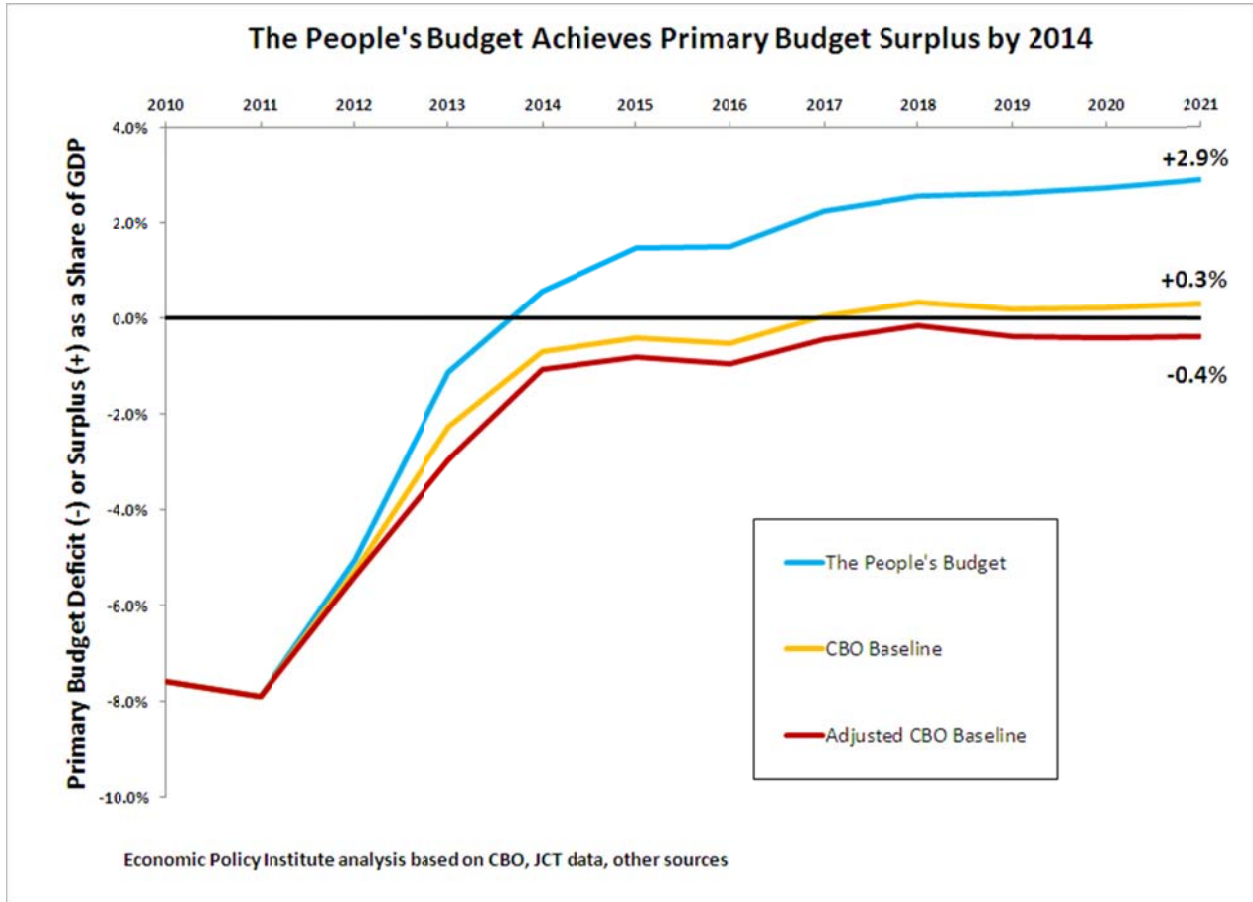


Figure 3. Debt Relative to Baseline Projections

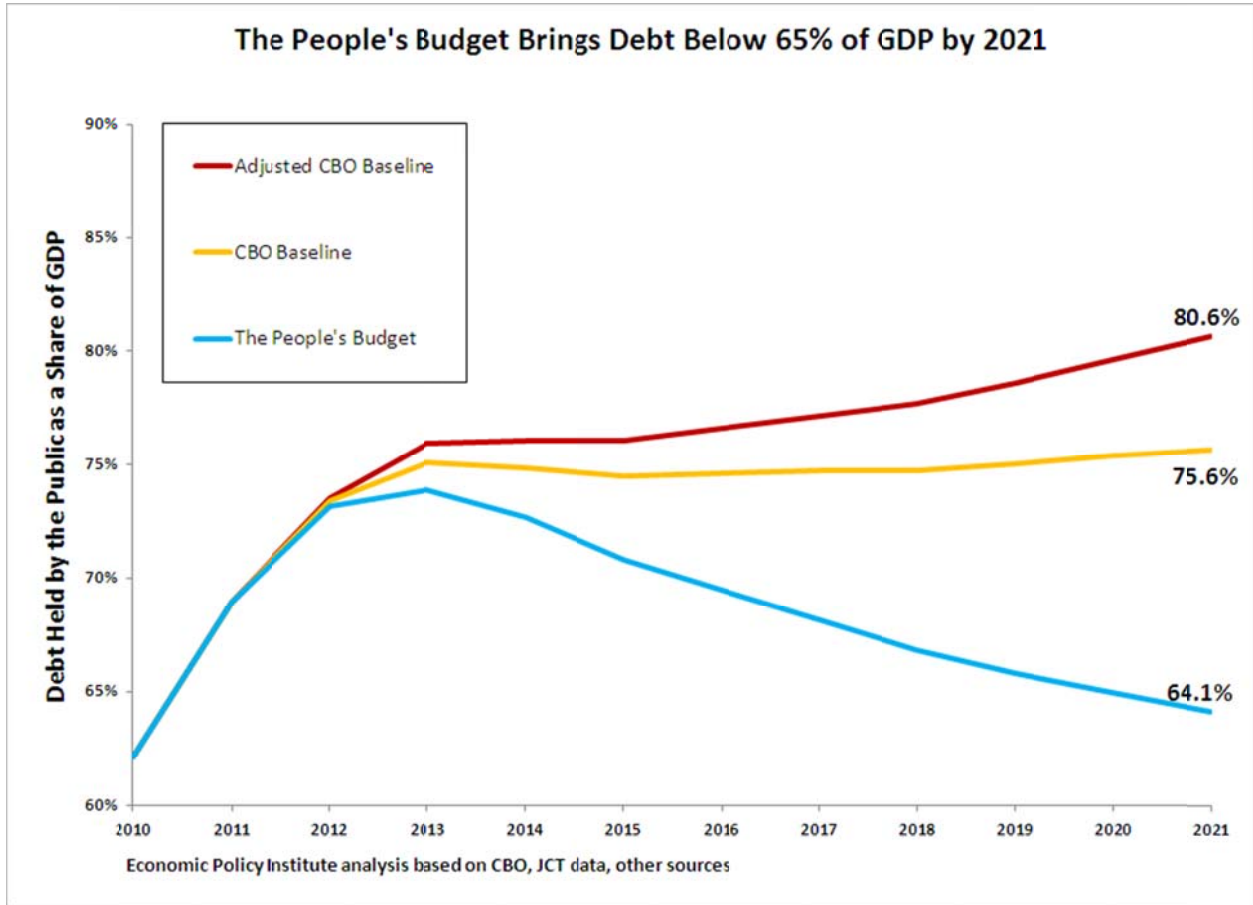


Figure 4. Deficits Relative to House Republican Budget and President's Budget

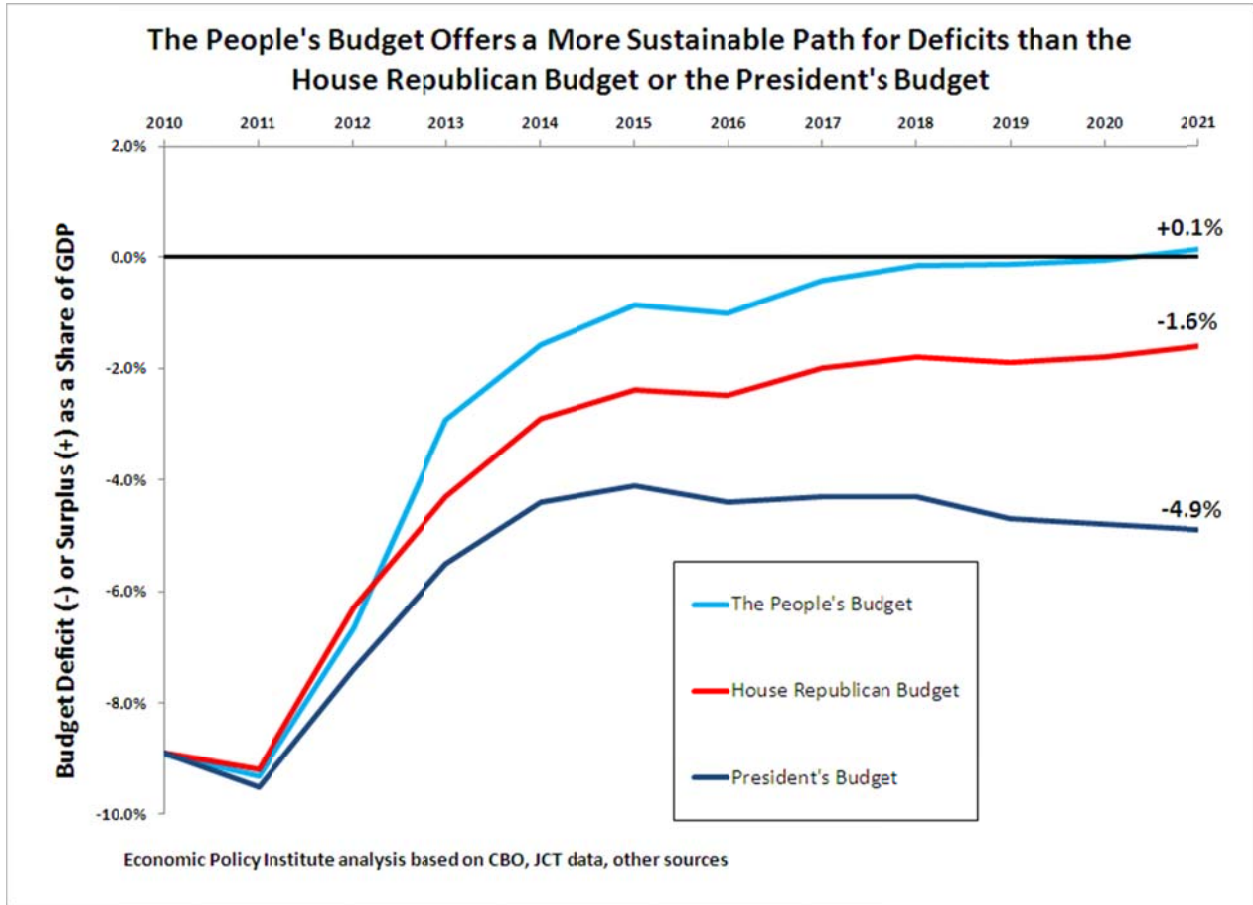


Figure 5. Debt Relative to House Republican Budget and President's Budget

