Policy Matters Ohio

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Principles for a better budget deal

President Obama and Congress have the chance to make smart budget decisions that can stabilize families, raise resources from those most able to pay, and keep in place important programs that reduce poverty and build the middle class. As we navigate those choices, here are two novel ideas to keep in mind: don't make a deal that increases inequality and don't make a deal that impoverishes more children.

Key findings

- Federal policy must not increase poverty or inequality.
- Tax rates on the wealthiest are among the lowest since the 1930s; they should go back to levels in the high-growth 1990s.
- We can't allow cuts – to education, extended unemployment, safety net programs, or the Earned Income Tax Credit – that would hurt millions of Ohioans.
- Spending caps in the Budget Control Act of 2011 already dramatically reduce the deficit.
- Smart choices will improve our economy, reduce poverty, and build the middle class.

What the pundits have begun referring to as a "fiscal cliff" refers to a set of automatic tax increases and spending cuts that will begin to take place if a deal is not reached by January 2. Tax rates on the wealthiest are almost as low as they've ever been since the 1930s. These are due to go back to the still-low rates that prevailed in the high growth 1990s and they should. Tax rates on the middle class are also due to increase without action. Those rates should be kept low.

Congressional leaders are promoting an approach to taxes and spending that would get rid of unemployment insurance for thousands of Ohio families, create deep cuts in programs that support individuals, families and communities, and eliminate cuts that have reduced taxes for middle class and poor families.

As they move toward an agreement to avert the so-called "fiscal cliff," policymakers must ensure that deficit reduction:

- Includes significant revenues, raised from the wealthiest;
- Does not increase poverty or inequality;
- Supports economic growth and job creation;
- Does not shift costs to states;
- Preserves tax cuts for the middle class.

A bad deal – one that would hurt families and children, deepen poverty and hardship and increase inequality – is worse than no deal at all. Policymakers must take the time to craft a plan that will strengthen economic growth and protect Ohio families.

The following recommendations would reduce the deficit without sacrificing economic growth.

Deficit reduction must be balanced

We need a balanced plan that restores significant revenues from those most able to pay and supports economic growth and well-being for all Americans.

The first step: let the high-income tax cuts expire. Marginal tax rates on the wealthiest are almost as low as they've ever been since the 1930s. Marginal taxes are only paid on the additional earnings above a certain threshold. These are due to go back to the still-low rates that prevailed in the high growth 1990s and they should. No deal would mean that marginal tax rates returned to these levels. Allowing the high-end income tax cuts to expire and the estate tax to revert to the (still-generous) rules of 2009 would generate an additional $1 trillion. A balanced plan, however, must raise more revenue to shrink the deficit without starving the government of resources needed to support economic growth, help with education, protect public health, assist the less fortunate, and promote opportunity.

It is also important that we raise additional revenue, beyond just that generated by letting the high-income tax cuts expire. Both President Obama's plan and the conservative Simpson-Bowles commission[1] plan would raise about $1.6 trillion more, over ten years, than generated by restoring the top rates alone. The new deal should raise at least as much as those efforts to reach a compromise.[2]

Deficit reduction must not make poverty worse

As Congress and the president shape deficit reduction legislation, they should reject any proposal that would increase poverty or reduce opportunities for families to climb out of poverty. Annually appropriated domestic programs (also known as non-defense discretionary funding) should not be hit by additional cuts. This part of the budget is slated for deep cuts as a result of the spending limits imposed by the Budget Control Act of 2011. By the end of the decade, the cuts already required by that act will shrink this funding to the lowest level, as a share of the economy, since 1962.[3]

Eliminating further cuts is essential. In addition to the spending limits, the Budget Act includes automatic cuts in discretionary funding will start in January of the coming year unless Congress replaces them with a more responsible deficit reduction package. This is known as the sequester, shorthand for across the board budget cuts to all discretionary spending. Ohio stands to lose $316 million in 2013 – and each year thereafter, through 2021 (K-12 education stands to lose $126 million in 2013, for example; Head Start, almost $10 million).[4] Fully one-quarter of overall non-defense discretionary funding goes directly to states and local governments for a wide array of services ranging from classroom teaching to clean-water infrastructure. These cuts, and other ones that Congress is discussing, would hurt economic growth by significantly constraining public investments

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[1] The 2010 National Commission on Fiscal Responsibility and Reform, established to develop: "…policies to improve the fiscal situation in the medium term and to achieve fiscal sustainability over the long run," is commonly referred to by the names of the bipartisan co-chairs, Erskine Bowles and Alan Simpson. This group had conservative leanings.

[2] Chye-Ching Huang, Chuck Marr, and Joel Friedman, "Restraining Tax Expenditures Should Complement, Not Replace, Letting High-Income Bush Tax Cuts Expire," (11/29/12) Center for Budget and Policy Priorities at http://bit.ly/WbIgyn.

[3] Richard Kogan, "Non-Defense Discretionary Programs Will Face Serious Pressures Under Current Funding Caps," Center for Budget & Policy Priorities at http://www.cbpp.org/cms/index.cfm?fa=view&id=3869

[4] Wendy Patton, "The Budget Control Act of 2011: Impact on public services in Ohio," Policy Matters Ohio at http://www.policymattersohio.org/budget-control-act-march2012.

– such as public education, access to college, and investments in basic science – that are critical to maintaining our global competitiveness, as well as many programs that assist low-income families.

Programs that help families through hard times are also at risk in upcoming budget negotiations. These programs include – but aren't limited to – core safety net programs such as Medicaid, Supplemental Nutrition Assistance Program (formerly known as food stamps), Supplemental Security Income, and subsidies that would enable people to afford health coverage and to access health care through the new health insurance exchanges. All major deficit reduction packages enacted in recent decades have protected core safety net programs; this year's framework for deficit reduction must adhere to this principle.

Deficit reduction must not deepen inequality

We need to raise tax rates on the wealthiest Americans, preserve tax cuts for middle-income families, and protect the Earned Income Tax Credit (EITC) and the low-income component of the Child Tax Credit (CTC) from cuts.

The federal EITC is the nation's largest poverty relief program for working families. Created by President Gerald Ford in 1975 and expanded under every presidential administration since, the EITC is lauded for its direct impact in lifting families with children above the poverty line, making work pay, and sending federal dollars to local communities.

The 2009 Recovery Act temporarily expanded the EITC for families with three or more kids, and also helped married couples with children. In 2010, these two expansions together lifted an estimated 500,000 people out of poverty and reduced the severity of poverty for approximately 7.3 million people living in poverty. These improvements are set to expire at the end of 2012.[5]

In Ohio, the federal EITC benefits more than 979,000 families (17 percent of all tax filers) and brings more than $2 billion to local communities. The average federal EITC refund is $2,211, often equaling three months of pay for a low-wage working family. Empirical research shows that families use refunds for basic needs, to pay for child-care expenses and for savings.[6]

The child tax credit, a different credit, was enacted 15 years ago, and expanded with bipartisan support over the past decade. Worth up to $1,000 per eligible child, it helps working families offset the cost of raising children. The 2001 and 2003 Bush tax cuts expanded the CTC from $500 per child to $1,000. The 2009 Recovery Act expanded eligibility and boosted the credit for many who were receiving only a partial credit, lifting one million people above the poverty line in 2010. Unless policymakers act, at the end of 2012 the CTC will revert to its pre-2001 structure, reducing the benefit to a $500-per-child nonrefundable credit.[7]

Failure to maintain these improvements would push many low-income parents and children below the poverty line and many others deeper into poverty. For example, a mother raising two children on a full-time, minimum wage job (which pays just $14,500 a year) would lose her entire credit – a total cut of $1,725. Even if policymakers extend the pre-2009 CTC improvements while allowing the

[5] David Rothstein, Ohio needs a state earned income tax credit at www.policymattersohio.org/eitc-april2012.
[6] Ibid.
[7] Center for Budget and Policy Priorities: "Policy Basics: Child Tax Credit." cbpp.org/cms/index.cfm?fa=view&id=2989.

Recovery Act improvements to expire, many working-poor families will be hurt. Working families earning less than about $13,350 would be ineligible for any child credit, and families with two children wouldn't qualify for the full credit until their earnings surpass $26,683.[8]

In addition, reducing the federal child tax credit would impact the Ohio child and dependent care tax credit. Currently Ohio's Child and Dependent Care tax credit is coupled to the federal benefit, set at 25 percent of the federal child tax credit for families making $20,000 to $40,000 and 100 percent for those making less than $20,000 annually. Elimination of the federal benefit would eliminate the Ohio benefit.[9]

The principle that tax changes enacted to reduce the deficit should not make the tax code less progressive or cut critical tax credits that help low-income working families make ends meet was a key element of a bipartisan Senate deficit reduction proposal – referred to at the time as the "Gang of Six" plan – modeled after the Simpson-Bowles plan.

Maintain extended unemployment benefits until economy strengthens

Tens of thousands of Ohioans who have been out of work and unable to find a job for more than six months will be affected if Congress fails to extend unemployment insurance (UI) benefits. Families and communities need an additional leg up when the economy is weak and it is difficult to find a job. As had been done in previous recessions, in 2008, President George W. Bush and Congress approved extended benefits for jobless workers who exhaust regular state unemployment compensation, which lasts up to 26 weeks in Ohio and most states. Though unemployment has declined, it remains high, and long-term unemployment remains at sky-high levels. In the year ended in September, the average Ohioan without a job was unemployed for 33.5 weeks, according to data from the U.S. Bureau of Labor Statistics.[10]

More than 48,000 Ohioans have relied on federally supported benefits each week; the bulk of them will have their benefits cut off if the program is not continued after Dec. 29.[11] These benefits help families, but they also provide vital support to communities. Jobless workers are likely to spend nearly all of their benefits, with positive effects for local economies. During the first nine months of 2012, the federal program paid more than $788 million to unemployed Ohioans.[12] Congress should continue federal support for UI benefits to avoid the loss of benefits for Ohioans and the negative effects that would have on their families and communities.

[8] Ibid.
[9] "Tax Credits for Working Families" fact sheet at http://www.taxcreditsforworkingfamilies.org/state/ohio/
[10] Ohio Department of Job & Family Services, Claim Trends report, ohiolmi.com/uc/Weekly/UCTRENDS_1248.pdf.
[11] Ibid.
[12] Policy Matters Ohio analysis of data available from the U.S. Department of Labor at http://1.usa.gov/X6GT7s.

Some clear choices

The Coalition for Human Needs outlines the clear choices we face in the so-called fiscal cliff.[13]

- We could maintain favorable tax treatment for hedge fund managers at the cost of $21 billion over ten years, and pay for it by eliminating housing vouchers and cutting deeply into the Women, Infants and Children nutrition program. (The WIC program helped the families of slightly more than half of all infants in Ohio in 2010, a high-poverty year.)
- We could keep the federal estate tax low, giving a bigger inheritance to the heirs of 7,400 high-income families nationally, very few of whom are in Ohio. Or, for the same cost, we could preserve refundable child tax credits that would assist 13 million families and 25.7 million children across the country (including 500,000 working Ohio families with nearly a million children).
- We could spend $156 million for two V-22 Osprey helicopters (expensive yet not as effective as hoped) or we could provide childcare to 22,000 children of families with low incomes.

The choices are fairly clear. We must raise marginal tax rates on those most able to pay, to the still-low levels we had in the high-growth 1990s. We should keep in place middle-class tax cuts, as middle-income families are struggling in our economy. We need to retain important spending that helps us educate our children, train our workforce, protect our communities and provide a basic safety net. Smart choices now will mean less poverty, a stronger and larger middle class, and a healthier economy in Ohio and all over the nation.

Policy Matters Ohio is a non-partisan, non-profit research institute
with offices in Cleveland and Columbus.

[13] Coalition for Human Needs, in slides provided for Advocates for Ohio's Future webinar on the Fiscal Cliff at http://www.slideshare.net/Advocates4OH/aof-fiscal-cliff-webinar-14790536#btnNext