# Federal and State Revenue Rises Much Touted, But All Smoke

by Paul Gallagher and Mary Jane Freeman

Tax revenues of the Federal government in 2005 remain considerably *below* their level of four years ago, despite the considerable fanfare the George W. Bush Administration gave to its July 13 announcement of a "shrinking budget surplus" and "rising Federal tax revenues." The high-profile announcement by Office of Management and Budget (OMB) director Joshua Bolton reflected a number of frauds—including the clearly too-high estimate of the FY 2006 deficit that OMB made in February, which made it easy to show a substantially lowered deficit estimate now. Also, OMB used a record Social Security surplus, over $160 billion, to make the deficit estimate "shrink" to $333 billion. In all, it was basically a fraudulent "intelligence estimate," reminiscent of those of Dick Cheney.

At the same time, a number of Federal states around the country have been announcing "a return to revenue surpluses" after three to four years of repeated gaping budget shortfalls, brutal budget cuts, and exhaustion of rainy-day funds, tobacco settlements, and so on.

At both the Federal and state levels, the frauds of the revenue jumps share common elements. They do not represent withholding-tax increases, which indicate rising employment and/or wages; but rather, they reflect the much higher real-estate-bubble-driven corporate and capital gains taxes in 2004. As one Maryland legislator put it, concerning the newly projected $1 billion FY 2005 surplus in that state, "No government official had anything to do with this; it was the real estate market."

The Federal and state increases involve many one-time-only factors, especially with regard to corporate taxes; they represent tax revenue levels still well below those of the late 1990s through 2000; and they represent the underpayment by government of rapidly rising costs from the decay of the underlying real economy. On the state level, this means, above all other factors, the upward spiral of Medicaid costs—the result of falling real wages and benefits in employment—which are tending to overwhelm the "surpluses" which have briefly appeared.

The OMB raised its Federal tax revenues estimate for FY 2005 by $87 billion on July 13. George W. Bush, and other Republicans, like Budget Committee chairman Rep. Jim Nussle (R-Iowa), immediately trumpetted the claim—hardly challenged anywhere in the media—that the Bush tax cuts have produced *increases* in Federal tax revenues. In the same July 13 report, the OMB also immediately raised its Federal tax revenue projections for each of the next five years, by roughly the same amount—a nonsensical step.

## Historically Low Tax Revenue

But the claim is a fraud. Economic collapse and tax cuts have *reduced* total tax revenues during Bush's term in office.

Despite the Federal tax revenue increase from Fiscal Year 2004 to FY 2005, this year's currently projected revenue remains 2-3% *lower* than the Federal tax revenue collected in FY 2001, which ended just before the Bush/Cheney tax-cut binge began to go into effect. (The Federal fiscal year ends with each Sept. 30.) Federal tax revenue fell for three straight years, FY 2002-04, an extremely unusual occurrence; and in FY 2004, it reached the lowest level since 1959, as a percentage of GDP.

Federal tax revenue for FY 2005 is now, with the OMB's latest revision, projected to equal 18% of GDP; in contrast, Federal tax revenue remained in the range of 21-22% of GDP from 1960-1999.

In dollar figures, the changes in Federal tax collections from year to year since FY 2001 are as follows: 2001-02, down $60 billion; 2002-3, down $27 billion; 2003-4, down $49 billion; 2004-5, up $91 billion (projected); 2001-05 as a whole, down $45 billion (projected).

There is another way to look at this revenue collapse: The *projection* of FY 2005 Federal tax revenue made by the Congressional Budget Office (CBO) in January 2002—after the 9/11 attacks, and after the biggest Bush tax cuts had already been enacted—was $2.342 trillion. But this week's new OMB projection for FY 2005 is $2.140 trillion, almost 10% less than what the CBO projected three and a half years ago.

Higher corporate income tax collections account for $51 billion of the $87 billion increase in Federal revenue estimated by the OMB. The reasons for the FY 2005 increase over 2004 are primarily three: First, corporate taxes have risen substantially with the expiration of an accelerated depreciation business tax cut at the end of 2004. Second, a one-time, large tax break rewarding businesses that bring overseas profits back into the United States, is in effect in 2005. Instead of 30%, firms are paying only 5.25% on these repatriated profits, so they are bringing that income back in large amounts in order to be lightly taxed.

Third, rising stock prices in 2004 produced rising capital gains taxes; but stock prices have not risen in 2005.

Nonetheless, looking at corporate tax revenues only, the changes from year to year since FY 2001 are as follows: 2001-02, down $35 billion; 2002-03, down $7 billion; 2003-04, down $20 billion; 2004-05, up $51 billion (projected); and 2001-05 as a whole, down $11 billion (projected).

## An Example: 'Chiselling' Veterans

An important component in the fraud of the improved budget situation is Administration chiselling on vital services and infrastructure on a mass scale. To wit, the current scandal around the budget for veterans health care, which was found to be billions short for both fiscal 2005 and 2006. These shortfalls were discovered only after the most intense grilling of Veterans Affairs Secretary Jim Nicholson by Congressmen of both parties, which revealed an Administration attempt to sweep the shortfall under the rug by reallocating monies from reserves and capital maintenance. Even with ongoing efforts by members of Congress to pass emergency supplemental allocations, it is not clear that veterans' service will be fully funded, because Administration figures assume increases in co-pays and enrollment fees for health services which have been voted down in Congressional committees. And, veterans advocates are warning that the vital national nursing home network could remain in jeopardy whatever the funding levels voted. (See interview with Alfie Alvarado, this issue.)

## The States' 'Good News'

Many states report "good news" as revenue surpluses have arisen as they closed out Fiscal Year 2005, which, for most states, ended June 30. This revenue up-tick is the first time in four years any surpluses have accumulated, after severe shortfalls which led to state governments slashing services and programs.

In reality, the news is superficial and likely not to last long, as the spurt was not the result of job growth or newly created physical economic growth. (See, for example, accompanying interview with Vermont state legislator.) Rather, the surpluses resulted as states cut spending, imposed tax and fee increases, and reaped revenues from corporate tax amnesties, or taxes on capital gains incomes—the latter largely buoyed by the overheated housing bubble—or oil revenues, as in Texas and Alaska.

Maryland, for example, reports a $1 billion surplus, which GOP Governor Robert Ehrlich crowed was because he exercised "fiscal restraint" without "raising the sales or income tax." Not reported by Ehrlich was the 5 cents per $100 assessed value on state property taxes, which generated more than half the new-found surplus. Nor did he mention the double-digit increase in college tuition that occurred, or program cuts, including some in health care.

Maryland state Delegate Richard Madaleno, Jr. (D) likened Ehrlich's bragging to "watching George Bush under the 'Mission Accomplished' sign" on the aircraft carrier over a year ago, declaring the 'victory' in Iraq. "It's a little premature to declare victory," he said.

The "good news," announced in early July by agencies which monitor states' revenues and spending, was qualified with caveats: "Revenue is improving, but not enough to eradicate persistent budget gaps," as "half the states are facing [new] gaps" for Fiscal Year 2006, which began July 1. Another remarked that the revenue surge "is not overwhelming, especially considering the extent to which states have cut their budgets recently."

Exploding growth of Medicaid costs, as more people are laid off from high-paying jobs and employers halt health-insurance programs, is a key factor too. "Enrollment increases continue to play a major role in increased Medicaid spending [for states], with enrollment increases of 40 percent over the past five years," the National Association of State Budget Officers (NASBO) reports.

The April 2005 "State Budget Update" by the National Conference of State Legislatures (NCSL) showed that "rising health-care costs and utilization are driving Medicaid and other health-care programs over budget. Through the first eight months of FY 2005, Medicaid and other health care spending [exceeded] appropriations in 23 states." By June it was 24 states, NASBO reported, "despite extensive cost containment."

NCSL economist Arturo Perez told *EIR,* "much of the growth in revenues will be tapped for additional Medicaid expenditures" and other health-care costs, so "there will be a tremendous need for those new-found dollars." NASBO reported the "good" revenue picture is "tempered by a backlog of expenditure demands," including "Medicaid [which is] the most costly."

Another critical element showing the weakness of the recent revenue surge is the "growth" in personal income tax (PIT) revenue. In the January-March, 2005 period, PIT grew by 11.2% nationally. PIT accounts for about one-third of states' revenues. But the total for withholding tax on wages was the smallest part of the increase, whereas the estimated tax portion grew by 21.5% compared to 2004, reports the Rockefeller Institute of Government. These taxes derive mostly from investments and capital gains. New jobs did not cause the revenue growth.

Although the revenue up-tick enabled many states to adopt their Fiscal 2006 budgets with less pressure to reduce programs and spending, it failed to erase the last four years of under-investment in people and government.

Twenty-six states had a combined $26.9 billion shortfall as they moved to adopt 2006 budgets. To close those gaps, they made cuts to programs along with increases in borrowing or taxes or fees. So this new budget year already begins with hundreds of thousands of people losing Medicaid benefits, property taxes continuing to climb, and states indebting themselves without initiating capital investment in goods and services for desperately needed infrastructure, which benefits the nation's general welfare.