EFFECTS OF CHANGES IN TAXES AND BENEFIT PAYMENTS PROPOSED IN THE ADMINISTRATION'S 1983 BUDGET FOR HOUSEHOLDS IN DIFFERENT INCOME CATEGORIES

Staff Memorandum

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Pursuant to the Request of
Senator Ernest F. Hollings
Ranking Minority Member
Senate Committee on the Budget

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SUMMARY

This memorandum, prepared at the request of Senator Ernest F. Hollings, examines the impact on households in different income categories of the revenue and spending changes directly affecting individuals that were proposed in the Administration's fiscal year 1983 budget. It extends a memorandum of February 1982, prepared at the separate requests of Senator Hollings and Representative Jones, Chairman of the House Committee on the Budget, that estimated the distributional effects of the tax and benefit reductions enacted in 1981.

This analysis, like that in the earlier memorandum, is limited by the complexity of the tax and expenditure programs involved and by the lack of complete data about them. As in that memorandum, the estimates presented here reflect only the proposed changes in federal taxes and benefits that directly affect specific households. Thus, for example, changes in spending in areas such as defense have not been included, since the benefits arising from these expenditures are not directly allocable to specific households. Additional details concerning the methods used to prepare these estimates, and a discussion of several cautionary points regarding their interpretation, may be found in the CBO's earlier analysis.

In addition, this analysis does not include any possible macroeconomic impacts of the proposed tax and benefit changes. If the budget proposals taken together significantly raised the rate of economic growth and reduced unemployment, then they could provide higher incomes that would offset the reductions in benefits.

The fiscal year 1983 budget includes only small proposed changes in direct taxes, so the estimates presented here focus primarily on the proposed changes in benefit payments. The major findings of this analysis are:

- If the Administration's proposed benefit reductions and direct tax increases were enacted, total savings in calendar year 1983 would be about $11.6 billion, and they would rise to about $23.2 billion by 1985. About half of this amount would come from reductions in means-tested programs.

- Over half of the savings that would result from the proposals--about $6.2 billion in calendar year 1983--would come from benefit reductions and tax increases affecting households with incomes below $10,000.

- The average loss as a result of the proposals would be about $320 in 1983 for households with incomes below $10,000. This is almost three times the average reduction for households in all other income categories.

- The average dollar loss generally declines as income rises. Households with incomes over $80,000, however, would lose roughly $100, or about the same amount as those with incomes between $10,000 and $20,000.

The table below summarizes these findings for calendar year 1983.

SUMMARY TABLE. PROPOSED CHANGES IN DIRECT TAXES AND BENEFIT PAYMENTS FOR HOUSEHOLDS IN DIFFERENT INCOME CATEGORIES: Calendar Year 1983

		Household Income (in 1982 dollars)				
	All Households	Less Than $10,000	$10,000–20,000	$20,000–40,000	$40,000–80,000	$80,000 and over
1. Proposed Changes in Total Direct Taxes and Benefits (in millions of current dollars)						
Reduction in cash benefits	4,710	3,200	630	570	270	40
Tax increases	830	70	160	420	180	10
Sum	5,540	3,270	790	990	450	50
Reduction in in-kind benefits	6,060	2,960	1,530	1,140	390	60
Sum, including in-kind benefits	11,600	6,230	2,320	2,130	840	110
2. Proposed Changes in Direct Taxes and Benefits per Household (in current dollars)						
Reduction in cash benefits	50	170	30	20	20	40
Tax increases	10	a	10	15	15	5
Sum	60	170	40	35	35	45
Reduction in in-kind benefits	70	150	70	40	30	60
Sum, including in-kind benefits	130	320	110	75	65	105

SOURCE: Congressional Budget Office.

NOTE: Components may not add to totals due to rounding.

a. Less than $5.

INTRODUCTION

This memorandum discusses the impact upon households in different income categories of the changes in taxes and in benefit payments for individuals proposed in the Administration's fiscal year 1983 budget. It extends a Congressional Budget Office (CBO) memorandum dated February 1982, which estimated the distributional impact of the tax and benefit reductions enacted in 1981. A more detailed presentation of general definitions and limitations, along with further discussion of the methodological problems associated with such estimates, may be found in that memorandum.

Like the earlier one, this memorandum concentrates on those changes in taxes and benefits that would directly affect household incomes. Thus, proposed changes in direct taxes--such as the income and Social Security payroll tax--and in benefit payments for individuals are estimated for households in various income categories, but changes in business taxes and in federal expenditures other than benefits to households are not. In addition, no attempt has been made to take into account the possible macroeconomic effects of the proposed tax and benefit changes.

The estimates presented here focus primarily on the proposed changes in benefit payments, since only small changes in direct taxes were proposed in the Administration's 1983 budget. A brief

discussion of proposed tax changes is presented in the next section, however. The third section outlines the impact of the proposed changes in benefit payments for households in five income categories, and the last section discusses the combined effects of the budget proposals.

REVENUE INCREASES PROPOSED IN THE 1983 BUDGET

Few of the proposed revenue increases in the fiscal year 1983 budget would directly affect households. The only policy option of this type estimated here would make federal government employees subject to the payroll tax for Medicare. Currently, federal employees do not contribute to the Hospital Insurance trust fund while they are employed by the federal government, but many are eligible for Medicare upon reaching retirement age because they have contributed enough to Social Security at some time during their lives. The budget includes a proposal to tax federal workers at the same Medicare payroll tax rate (currently 1.3 percent) that applies to workers who are employed in jobs covered by the system. The tax would apply to the same maximum taxable earnings as for workers now covered by Social Security ($32,400 in 1982). The expected revenue increase would be about $0.8 billion in 1983, half of which would be paid by those with incomes between $20,000 and $40,000, as shown in Table 1. Though the tax would be substantial for many of those affected, it would represent only a small amount per household when distributed among the entire population, as is shown Table 2.

TABLE 1. PROPOSED TAX INCREASE[a] BY INCOME CATEGORY, CALENDAR YEARS 1983-1985 (in millions of current dollars)

Calendar Year	All Households	Household Income (in 1982 dollars) Less Than $10,000	$10,000-20,000	$20,000-40,000	$40,000-80,000	$80,000 and over
Tax Increase						
1983	830	70	160	420	180	10
1984	870	70	170	440	180	10
1985	970	80	190	490	210	10
Percentage Distribution of Tax Increase						
1983	100	8.4	19.3	50.6	21.7	1.2
1984	100	8.0	19.5	50.6	20.7	1.1
1985	100	8.2	19.6	50.5	21.6	1.0

SOURCE: Congressional Budget Office.

NOTE: Components may not add to totals due to rounding.

a. The proposed tax increase shown in this table is the imposition of the Medicare portion of the Social Security tax on federal employees.

TABLE 2. PROPOSED TAX INCREASE[a] PER HOUSEHOLD BY INCOME CATEGORY, CALENDAR YEARS 1983-1985 (in current dollars)

Calendar Year	All Households	Household Income (in 1982 dollars) Less Than $10,000	$10,000-20,000	$20,000-40,000	$40,000-80,000	$80,000 and over
1983	10	b	10	15	15	5
1984	10	b	10	15	15	5
1985	10	b	10	15	15	5

SOURCE: Congressional Budget Office.

a. The proposed tax increase shown in this table is the imposition of the Medicare portion of the Social Security tax on federal employees.

b. Less than $5.

Another revenue enhancement proposal pertaining to individuals would implement withholding of federal income taxes on interest and dividends. No attempt has been made here to distribute this revenue increase, however, for several reasons. For example, the most substantial tax increases due to withholding would be imposed on those who evade tax in the absence of withholding, and on whom there are therefore no data. In addition, some low-income taxpayers would be able to request exemption from withholding, but the operation of the exemption system is not yet clear. The total additional revenues to be collected would be about $2 billion in fiscal year 1983.

Most of the remaining revenue initiatives proposed in the 1983 budget pertain only to the corporate income tax, and therefore are not reflected in Tables 1 and 2. The largest proposed revenue increases are from the corporate minimum tax ($2.3 billion in fiscal year 1983), the prohibition of modified coinsurance arrangements ($1.9 billion), and the prohibition of the completed contract method of accounting ($1.9 billion). Other revenue enhancements would bring the total of additional tax revenues to $12.8 billion in fiscal year 1983.

Further revenue increases would stem from new and increased user fees of $2.5 billion in fiscal 1983. Most of these user fees would be paid by businesses, though some (including increased fees

for use of federal recreation facilities and new fees for Coast Guard services) might bear upon households. These fees were not included in Tables 1 and 2 because the amount that would be paid by households is not known.

PROPOSED CHANGES IN BENEFIT PAYMENTS FOR INDIVIDUALS

Substantial reductions are proposed in the Administration's 1983 budget in most of the federal programs that provide benefit payments for individuals. Proposed reductions would be particularly large for means-tested programs, which would account for about half of the estimated 1983 savings, in comparison to about one fifth of estimated outlays. No reductions are proposed in Social Security cash benefits, which account for over half of all benefit payments for individuals. The CBO estimates that the proposed reductions in outlays for benefit payments would total about $11 billion in calendar year 1983, and would grow substantially over time, to about $22 billion in 1985.[1] Proposed reductions in

1. The estimates of outlay savings presented here are the differences attributable to proposed legislative changes relative to the level of spending that would otherwise occur. The "baseline" from which the savings are measured assumes that program authorizations would be extended into the future and that, in the case of entitlement programs (encompassing most benefits for individuals), spending would otherwise have risen consistent with current CBO economic assumptions and with anticipated demographic changes. In the case of appropriated accounts, the baseline assumes that, except where capped by legislation, appropriations would otherwise have risen at the rate necessary to provide the base year's level of services for each year thereafter.

benefit payments for individuals would account for about 30 percent of total proposed outlay reductions over the next three years.

Not all reductions in benefit payment programs have been included in these estimates. Those that would affect only state administrative costs, for example, have been excluded. In the Food Stamp, Aid to Families with Dependent Children (AFDC), and Medicaid programs, the Administration has proposed the consolidation of the federal share of administrative payments into a block grant funded at reduced levels, and the elimination of federal payments resulting from erroneous benefit payments by the states. The enactment of these proposals could substantially increase states' costs but would not directly affect benefit payments, and so these cuts have been excluded from the savings estimates presented here.[2]

Two programs, Medicare and food stamps, account for almost half of the savings from proposed benefit reductions, as Table 3 shows. Proposed Medicare cuts include both benefit changes affecting covered services and patient liability, and reductions in

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2. A complete list of the proposed changes excluded from these estimates, and a discussion of the effects of their exclusion, is given in the appendix.

TABLE 3. PERCENTAGE DISTRIBUTION OF PROPOSED REDUCTIONS IN OUTLAYS FOR BENEFIT PAYMENTS FOR INDIVIDUALS, BY PROGRAM: CALENDAR YEARS 1983-1985

Programs	1983	1984	1985
Total Reduction in Benefits (in billions of dollars)	10.8	17.0	22.2
Reductions in Benefits as a Percentage of Total	100	100	100
Cash Benefit Programs	44	37	34
Social Security Retirement, Survivors', and Disability Benefits and Railroad Retirement	0	0	0
Civil Service Retirement	7	9	11
Military Retirement	1	1	1
Unemployment Insurance	a	a	a
Trade Adjustment Assistance	1	a	a
Food Stamps	19	13	11
Aid to Families with Dependent Children	6	4	3
Supplemental Security Income	3	3	3
Low Income Energy Assistance	5	3	3
Veteran's Pensions and Compensation	3	3	3
In-Kind Benefit Programs	56	63	66
Medicare	29	34	39
Medicaid	8	7	7
Guaranteed Student Loans	2	4	4
Pell Grants	5	8	8
Food and Nutrition Programs, other than Food Stamps	8	7	6
Housing Assistance Programs	4	3	3

NOTE: Components may not add to totals due to rounding. Estimates may differ from other CBO estimates because of changes in technical estimating procedures and economic assumptions and because these estimates are for calendar rather than fiscal years.

a. Less than 0.5 percent.

hospital and physician reimbursement. The latter would probably result in higher medical care costs for Medicare recipients.[3] The proposed food stamp cuts that would affect benefits paid to individuals include the elimination of the earnings deduction, an increase in the rate at which benefits are reduced when other income is received, and the counting of low income energy assistance payments as income in determining benefit levels.

In addition to Medicare and food stamps, large reductions are also proposed for several other programs. The three largest remaining cuts would be in Medicaid, Civil Service Retirement, and Pell Grants (previously known as Basic Educational Opportunity Grants). In Medicaid, co-payments would be imposed on beneficiaries. Cost-of-Living Adjustments (COLAs) for civil service and military retirees would be limited to the lower of the percentage increase in federal pay and in the Consumer Price Index (CPI). In

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3. Reductions in physician reimbursement account for about 20 percent of Medicare savings and reductions in hospital reimbursement account for about 25 percent. Physicians are allowed to pass these cuts in reimbursements on to beneficiaries. For example, lowering the reimbursement rate for radiologists and pathologists to 80 percent (from 100 percent) will directly increase beneficiaries co-insurance under Medicare Part B. Hospitals might be able to shift the costs of lower reimbursements onto patients with private insurance. See the appendix for further discussion.

the Pell Grant program, which provides grants to low-income college students, the maximum payment would be reduced and the number of recipients would be cut by about one third.

Distribution of Federal Outlay Savings from Proposed Reductions in Benefit Payments for Individuals

This section first examines separately the proposed reductions in cash benefit payments and in benefits paid in kind. The combined effects of the proposed benefit reductions and the average effects for households in different income categories are then discussed.

Proposed Reductions in Cash Benefits. Reductions in cash benefit programs would account for about 40 percent of total outlay savings from proposed cuts in benefits for individuals. These reductions would affect some recipients in all income categories, but about 60 percent of the savings would come from reductions affecting households with incomes below $10,000, as Table 4 shows. Less than 20 percent of the proposed savings in 1983, rising to about 30 percent by 1985, would come from reductions in cash benefits received by households with incomes over $20,000.

The major cuts in cash benefits affecting households in the lowest income category are those in the Food Stamp, AFDC, Supplemental Security Income (SSI), and Low Income Energy Assistance

TABLE 4. TOTAL PROPOSED REDUCTIONS IN OUTLAYS FOR BENEFIT PAYMENTS FOR INDIVIDUALS, BY INCOME CATEGORY OF BENEFICIARIES, CALENDAR YEARS 1983-1985 (in millions of current dollars)

		Household Income (in 1982 dollars)				
Calendar Year	All Households	Less Than $10,000	$10,000-20,000	$20,000-40,000	$40,000-80,000	$80,000 and over
<u>Cash Benefits</u>						
1983	4,710	3,200	630	570	270	40
1984	6,270	3,720	950	1,030	520	80
1985	7,560	4,080	1,210	1,420	730	110
<u>Benefits In Kind</u>						
1983	6,060	2,960	1,530	1,140	390	60
1984	10,690	4,950	2,910	2,140	620	80
1985	14,620	6,860	3,980	2,830	840	110
<u>Total Benefits</u>						
1983	10,770	6,160	2,160	1,710	660	100
1984	16,960	8,670	3,860	3,170	1,140	160
1985	22,180	10,940	5,190	4,250	1,570	220
<u>Percentage Distribution of Total Benefit Reductions</u>						
1983	100	57	20	16	6	1
1984	100	51	23	19	7	1
1985	100	49	23	19	7	1

SOURCE: Congressional Budget Office.

NOTE: Components may not add to totals due to rounding.

programs. The largest single reduction is that in food stamps, which results from several changes in the program, as described above. The AFDC and SSI cuts are smaller on average than those in food stamps, but would affect many of the same households. Included in the AFDC cuts are proposals to count low income energy assistance payments as income in determining benefits, to pro-rate shelter and utility costs included in the need standard for AFDC filing units that are part of larger households, and to count the incomes of certain other household members who are not part of the filing unit in setting benefit levels. In SSI, the Administration proposes to eliminate the $20 income disregard in computing benefits for new beneficiaries, and to tighten eligibility requirements for benefits based on disability. The Administration also proposes to combine Low Income Energy Assistance with Emergency Assistance (currently funded as part of AFDC) in a block grant to be funded at about 70 percent of the level now authorized for 1983.

The proposed food stamp cuts would also affect some households with incomes over $10,000, but the bulk of the cuts affecting such households would be in the Civil Service Retirement and Military Retirement programs, and in benefits for veterans. More than 70 percent of the savings from limiting COLAs for civil service and military retirees would come from reductions in benefits received by households with incomes over $20,000, and almost 30

percent would come from benefits received by those with incomes over $40,000. Reductions in veterans' benefits, which would include the elimination of students' benefits and reductions in some benefits for those who are less than 100 percent disabled, would be fairly evenly distributed over the lowest three income categories.

Proposed Reductions in Benefits In Kind. Cuts in programs providing subsidies for goods and services rather than cash account for about 60 percent of the total savings arising from the proposed reductions in benefit payments.[4] The largest proposed reductions in in-kind benefits would be those in Medicaid and Medicare, although reductions in Pell Grants and in nutrition programs would also produce substantial savings.

These reductions would have the most effect on households with incomes below $10,000, with almost half of the savings coming from in-kind benefits received by such households. Another one fourth of the savings would result from reductions in benefits received by those with incomes between $10,000 and $20,000, and

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4. Reductions in benefits in kind are valued at the reduction in the federal government's cost of providing these benefits, which may not equal the reduction in the value of these benefits for their recipients. In addition, some states may institute programs to replace some of the lost benefits.

most of the remaining savings would come from cuts for those in the $20,000 to $40,000 income category.

For the lowest income category, the bulk of the savings would come from the Medicare and Medicaid programs, although proposed cuts in Pell Grants, housing assistance, and the Department of Agriculture's feeding program for Women, Infants, and Children (WIC) would also affect these households. Households with incomes over $10,000 would be particularly affected by the proposed reductions in Medicare and in the Guaranteed Student Loan (GSL) program.

Total Benefit Reductions. In summary, as the bottom section of Table 4 shows, more than half of the total savings from proposed benefit reductions would come from benefits received by households in the lowest income category, and almost three fourths of the savings would stem from reductions in benefits received by those with incomes less than $20,000. The proportion of the total cuts affecting each income category declines as income rises, with about 8 percent of total savings coming from benefits received by the highest two income groups.

Distribution of Reductions in Federal Outlays Per Household

The average reductions in outlays resulting from the Administration's proposals would follow much the same pattern as the

total reductions (see Table 5). The average reduction in benefits would be more than twice as large for households with incomes below $10,000 as for households in other income categories, and the size of the average cut would generally decline with income. The one exception is the relatively large decline in average benefits that would be experienced by those in the $80,000 and over category. This decline largely results from the cuts in Civil Service and Military Retirement and in Medicare.

Table 5 should be interpreted with some caution. In particular, these figures represent the average reduction in federal outlays per household, which is not necessarily equivalent to the average reduction in the value of the benefits received. Further, these figures are averages over all households in each income category and include many households that receive no benefits from the programs that would be cut--and therefore no reductions. Average reductions for only those households that receive benefits would be larger. Unfortunately, however, such averages cannot be computed because of the lack of data on the extent to which the households participate in more than one of the affected programs.[5]

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5. Several other cautionary points with regard to the interpretation of such estimates are presented in the CBO's earlier analysis of the distribution of tax and benefit reductions, of which this memorandum is an extension. See that analysis for detailed discussion of these points.

TABLE 5. AVERAGE PROPOSED REDUCTIONS PER HOUSEHOLD IN OUTLAYS FOR BENEFIT PAYMENTS BY INCOME CATEGORY OF RECIPIENTS: CALENDAR YEARS 1983-1985 (in current dollars)

		Household Income (in 1982 dollars)				
Calendar Year	All Households	Less Than $10,000	$10,000-20,000	$20,000-40,000	$40,000-80,000	$80,000 and over
Cash Benefits						
1983	50	170	30	20	20	40
1984	70	190	40	30	40	70
1985	80	200	50	40	50	100
Benefits In Kind						
1983	70	150	70	40	30	60
1984	120	250	130	70	40	70
1985	160	340	180	90	60	100
Total Benefits						
1983	120	320	100	60	50	100
1984	190	440	180	100	80	150
1985	250	540	230	130	110	200

SOURCE: Congressional Budget Office.

NOTE: Components may not add to totals because of rounding.

COMBINED EFFECTS OF THE PROPOSED TAX AND BENEFIT CHANGES

Since the proposed tax increases are small, the combined effects of the proposed tax and benefit changes would be similar to the effects of the cuts in benefits alone, as Tables 6 and 7 show. The total impact of the changes would be a loss to households of about $12 billion in 1983, rising to about $23 billion in 1985. About half of this amount--about $6 billion in 1983 and about $11 billion in 1985--would come from reductions in benefits and increases in taxes for those in the lowest income category.

The inclusion of the tax changes also has little effect on the average loss per household that would result from these proposals. Average total losses--including reductions in both cash and in-kind benefits and tax increases--for those with incomes of $10,000 or less would be about $320 in 1983, rising to about $540 in 1985. These amounts are more than twice the average loss for any other group.

TABLE 6. TOTAL PROPOSED CHANGES IN TAXES AND BENEFITS BY INCOME CATEGORY: CALENDAR YEARS 1983-1985 (In millions of current dollars)

		Household Income (in 1982 dollars)				
Calendar Year	All Households	Less Than $10,000	$10,000-20,000	$20,000-40,000	$40,000-80,000	$80,000 and over
1983						
Reduction in cash benefits	4,710	3,200	630	570	270	40
Tax increases	830	70	160	420	180	10
Sum	5,540	3,270	790	990	450	50
Reduction in in-kind benefits	6,060	2,960	1,530	1,140	390	60
Sum, including in-kind benefits	11,600	6,230	2,320	2,130	840	110
1984						
Reduction in cash benefits	6,270	3,720	950	1,030	520	80
Tax increases	870	70	170	440	180	10
Sum	7,140	3,790	1,120	1,470	700	90
Reduction in in-kind benefits	10,690	4,950	2,910	2,140	620	80
Sum, including in-kind benefits	17,830	8,740	4,030	3,610	1,320	170

(Continued)

TABLE 6. Continued

Calendar Year	All Households	Less Than $10,000	$10,000-20,000	$20,000-40,000	$40,000-80,000	$80,000 and over
		Household Income (in 1982 dollars)				
1985						
Reduction in cash benefits	7,560	4,080	1,210	1,420	730	110
Tax increases	970	80	190	490	210	10
Sum	8,530	4,160	1,400	1,910	940	120
Reduction in in-kind benefits	14,620	6,860	3,980	2,830	840	110
Sum, including in-kind benefits	23,150	11,020	5,380	4,740	1,780	230

SOURCE: Congressional Budget Office.

NOTE: Components may not add to totals due to rounding.

TABLE 7. PROPOSED CHANGES IN TAXES AND BENEFITS PER HOUSEHOLD BY INCOME CATEGORY: CALENDAR YEARS 1983-1985 (In current dollars)

		Household Income (in 1982 dollars)				
Calendar Year	All Households	Less Than $10,000	$10,000-20,000	$20,000-40,000	$40,000-80,000	$80,000 and over
<u>1983</u>						
Reduction in cash benefits	50	170	30	20	20	40
Tax increases	10	a	10	15	15	5
<u>Sum</u>	60	170	40	35	35	45
Reduction in in-kind benefits	70	150	70	40	30	60
<u>Sum, including in-kind benefits</u>	130	320	110	75	65	105
<u>1984</u>						
Reduction in cash benefits	70	190	40	30	40	70
Tax increases	10	a	10	15	15	5
<u>Sum</u>	80	190	50	45	55	75
Reduction in in-kind benefits	120	250	130	70	40	70
<u>Sum, including in-kind benefits</u>	200	440	180	115	95	145

(Continued)

TABLE 7. Continued

Calendar Year	All Households	Household Income (in 1982 dollars) Less Than $10,000	$10,000-20,000	$20,000-40,000	$40,000-80,000	$80,000 and over
1985						
Reduction in cash benefits	80	200	50	40	50	100
Tax increases	10	a	10	15	15	5
Sum	90	200	60	55	65	105
Reduction in in-kind benefits	160	340	180	90	60	100
Sum, including in-kind benefits	250	540	240	145	125	205

SOURCE: Congressional Budget Office.

NOTE: Components may not add to totals due to rounding.

a. Less than $5.

APPENDIX. PROPOSED CHANGES IN BENEFIT PAYMENT PROGRAMS NOT INCLUDED IN SAVINGS ESTIMATES

The Administration's 1983 budget proposals include several proposals to shift certain costs from the federal government to states and localities. Such proposals would particularly affect the AFDC, Food Stamp and Medicaid programs. The savings arising from these proposals have not been allocated to households in the various income categories, since in the absence of information on state responses it is difficult to predict the distributional effects of these proposals. If states responded to these cuts by reducing benefits, the total effects of the cuts could be larger than the estimates given in the text would indicate. On the other hand, states could decide to increase their own expenditures to make up for the federal reductions, which might impose additional costs on state taxpayers but which would not result in reductions in benefits. The distributional implications of these two types of response would be very different. Thus, the following proposals have been excluded from the estimates:

<u>AFDC</u>

- o Combined Welfare Administration block grant
- o Phase-in of zero error rate tolerance
- o Restructured matching rates for Child Support Enforcement (CSE)
- o 6 percent matching fee for non-AFDC CSE cases

Food Stamps

- o Combined Welfare Administration block grant
- o Phase-in of zero error rate tolerance
- o Transfer of work registration costs to states
- o Food stamp block grant for the territories

Medicaid

- o Combined Welfare Administration block grant
- o Phase-in of zero error rate tolerance
- o Elimination of federal matching for Medicare part B "buy-in" for Medicaid recipients
- o Reduced federal matching rates for optional coverage, optional benefits, and administrative costs

In general, it is difficult to know how to distribute spending reductions that would affect programs providing individual benefits, but which would not translate directly into benefit cuts. This is particularly a problem for spending reductions that would probably result in fewer benefits or services for individuals, but where the total size or the distribution of the effects cannot be known with any certainty. Examples of such spending reductions are the cuts in federal matching rates for state Medicaid expenditures for optional coverage and optional benefits and cuts in Medicare reimbursement rates for physicians and hospitals.

The estimates presented in this memorandum generally exclude such reductions in spending if they would affect federal payments to states, but include them if they would affect other federal payments, such as those made to physicians and hospitals. In

general, the assumption has been that states are somewhat more likely to absorb part or all of the cuts. The Medicaid reductions cited above are an example of the first type, while the Medicare cuts are an example of the second.

Neither the inclusion of the Medicaid matching rate reductions nor the exclusion of the Medicare reimbursement cuts would have substantially changed the overall estimates. Inclusion of the Medicaid cuts would have increased the total estimated savings by about 6 percent in 1983, and would have increased the benefit reduction experienced by those in the lowest income category by about 10 percent, if the full reductions were assumed to be passed on to Medicaid recipients. The total loss in benefits experienced by those in the second and third income categories would also have increased slightly.

Exclusion of the reductions in Medicare hospital reimbursement rates would have reduced total savings by about 6 percent in 1983. Cuts in Medicare benefits are distributed over the income categories in approximately the same proportions as are all other benefit cuts combined, so the average reduction in benefits in each category would also be about 6 percent. If both the hospital and physician reimbursement rate reductions had been excluded, total savings would have been reduced by about 10 percent.