Committee for a Responsible Federal Budget

The Better Budget Process Initiative:

Strengthening Statutory Budget Enforcement

June 25, 2015

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Introduction

In 2010 and 2011, policymakers enacted two important budget process improvements: statutory caps on discretionary spending and the statutory pay-as-you-go (PAYGO) law to prevent tax cuts or mandatory spending increases that are not offset by other changes. Although neither of these laws will prevent the unsustainable growth of the debt, both are designed to prevent policymakers from worsening the overall fiscal situation. Unfortunately, policymakers have negated these rules' effectiveness by finding ways to circumvent them on many occasions.

The experience with the discretionary spending caps and PAYGO requirements originally enacted as part of the 1990 Budget Enforcement Act demonstrated that when lawmakers took these rules seriously, they were more likely to abide by the rules. With debt at a modern record high and projected to grow unsustainably, it is unacceptable for policymakers to avoid hard choices by relying on gimmicks and loopholes.

Congress should therefore reaffirm its commitment to strictly enforced budget rules, and enact reforms strengthening these rules to make it harder to evade the letter and spirit of the rules. We recommend several improvements to help them do so:

Strengthening enforcement of existing rules

1. *Establish a separate point of order against provisions to exclude costs from PAYGO*
2. *Prohibit legislation blocking any sequester enforcing statutory PAYGO or discretionary caps*

Restrict the use of phony offsets

3. *Prohibit the use of spending cuts with no real savings*
4. *Restrict the use of timing gimmicks to claim savings within the budget window*
5. *Prevent the use of artificially inflated baselines to claim savings*
6. *Prohibit double-counting of increased revenues and spending cuts involving trust funds*

Ensure all costs are subject to budget discipline

7. *Limit the use of Overseas Contingency Operations as a slush fund*
8. *Expand the deficit-neutrality requirement in PAYGO to apply to debt service*

Strengthening Enforcement of Existing Rules

1. Establish a separate point of order against provisions to exclude costs from PAYGO

Current Practice: The ten-year budgetary effects of legislation affecting mandatory spending and revenues are recorded on the Office of Management and Budget's (OMB) PAYGO scorecard, and if the scorecard shows net deficit increases at the end of the year, OMB must issue a "sequestration" cut to offset these costs.

Problem: Although OMB is supposed to record costs on the PAYGO scorecard, Congress can and often does exclude costly legislation from the scorecard. For example, Congress excluded from PAYGO both the $141 billion fix to the Medicare Sustainable Growth Rate passed this year and the $42 billion extension of various tax breaks enacted last year. Although a point of order can be raised against such an exclusion under current law (Section 306 of the Budget Act), sustaining that point of order would take down the entire bill instead of just the PAYGO exemption. As a result, Members who support the underlying bill but are forced to choose between killing a bill entirely or allowing it to proceed exempt from PAYGO rules.

Proposal: Congress should create a separate point of order against provisions in legislation exempting costs from PAYGO that would strike only the exemption if upheld. The point of order should require 60 votes to waive in the Senate. This sort of surgical point of order, which would resemble the rule for emergency spending in Budget Control Act, would allow Congress to remove the PAYGO exemption without killing legislation with broad support, making it easier for Members who wish to enforce the PAYGO rule. Striking the PAYGO exemption while allowing the rest of the bill to go forward would effectively require that the costs be offset by subsequent legislation.

2. Prohibit legislation blocking any sequester enforcing statutory PAYGO or discretionary caps

Current Practice: If OMB determines that discretionary spending limits have been exceeded or legislation subject to PAYGO has increased the deficit, OMB is required to issue a sequester to bring spending within the cap or offset the deficit increase.

Problem: Congress can avoid enforcement of discretionary spending limits and PAYGO requirements by enacting legislation to prevent sequestration from taking effect. In the 1990s and early 2000s, Congress often included a provision blocking a sequester in omnibus appropriations bills or other must-pass legislation at the end of the year, making it difficult to block the provision "turning off" sequestration.

Proposal: Congress should create a separate point of order in the House and Senate against provisions that prohibit OMB from implementing sequestration, eliminate a negative balance on the PAYGO scorecard, or otherwise block a sequester to enforce Statutory PAYGO or discretionary spending limits. The point of order should require 60 votes to waive in the Senate and strike only provisions blocking sequestration, allowing Members to strike the offending provision without blocking the entire bill.

Background on Statutory Budget Enforcement Provisions

There are two primary budget enforcement tools currently in law. Statutory Pay-As-You-Go (PAYGO), which limits changes to mandatory spending and revenue, and discretionary spending caps, which set limits on defense and non-defense discretionary spending. These two tools were an important part of the 1990 budget agreement and ultimately helped policymakers balance the budget in the late 1990s but were allowed to expire in 2002. They were reinstated in 2010 and 2011, respectively.

PAYGO: The Statutory PAYGO Act of 2010 established requirements to ensure that over the course of a given fiscal year, the net effect of new laws affecting mandatory spending or revenues does not add to the debt. In other words, policymakers must balance laws that increase deficits with other laws that produce savings of equal or greater value.

The Office of Management and Budget (OMB) enforces PAYGO through a "PAYGO Scorecard" that sums up all of the costs and all of the savings incurred by new laws in a given year, averages the costs over the first five and first ten years after enactment, and places that amount on the five-and ten-year scorecard respectively.

If Congress adjourns for the year with a negative balance on either the five- or ten-year scorecard (resulting from costs exceeding savings), then the President is required to issue a sequester order that uniformly cuts non-exempt mandatory spending by an amount that offsets the deficit shown on the scorecard.

Discretionary Caps: The Budget Control Act of 2011 established annual discretionary spending caps, limiting the amount appropriators could spend in budget authority each year through 2021. The initial caps allowed for about $1.043 trillion in total budget authority in 2012, and $11.3 trillion over the ten-year period – about $840 billion (budget authority) below projections at the time.

The caps are adjusted to accommodate any spending designated as Overseas Contingency Operations (OCO,) also known as war spending, or emergency spending as well as specified adjustments for certain program integrity funding. If total appropriations enacted by Congress exceed the spending limit in a given fiscal year, the President is required to order an across-the-board sequester of all discretionary spending in that category.

The original caps established separate limits on security and non-security spending. However, the law adjusted these caps to instead apply to defense and non-defense spending upon the failure of the Joint Select Committee on Deficit Reduction (the Super Committee) to put forward recommendations. Failure of the Super Committee also led to a multi-year "sequestration," which effectively reduced discretionary caps by about $90 billion per year – though subsequent laws reversed some of that reduction for FY2013, FY2014, and FY2015.

Restrict the Use of Phony Offsets

3. Prohibit the use of spending cuts with no real savings

Current Practice: While statutory discretionary spending caps limit the total amount Congress can appropriate in budget authority each year, the law allows Congress to appropriate budget authority (BA) in excess of spending limits as long as it offsets the excess spending with reductions in previously enacted budget authority. These reductions can take the form of rescissions to discretionary spending but can also come from changes in mandatory spending included in appropriations bills (CHIMPS).

Problem: Often, Congress will rescind budget authority that would never have been spent, reducing "empty BA" that produces no savings to pay for real increases in government spending. Because limits on budget authority are often more binding than outlay limits, these reductions in budget authority allow spending bills to comply with budget limits on paper despite having no real budgetary effect. Even more egregiously, Congress will sometimes achieve savings by simply delaying spending into the future, taking advantage of the single-year budget window used for determining discretionary spending limits. This practice has become particularly pervasive with regards to CHIMPs; indeed, FY2015 spending levels relied on about $20 billion of CHIMPs to comply with the budget caps, but those CHIMPs will produce less than $1 billion of total outlay savings (see Senate Budget Takes Issue with CHIMPs).

Proposals: Congress should exclude savings from rescinding budget authority either on the discretionary side or from CHIMPs that result in no net outlay savings in the first fiscal year from appropriations estimates for the purpose of enforcing discretionary limits, which would prevent Congress from claiming savings from rescinding empty BA. Congress should also phase out CHIMPs that simply delay obligations to a future year by gradually reducing the amount of savings that can be counted from delays in obligation of mandatory spending that have no net outlay savings over ten years and ultimately completely cancelling mandatory spending authority that is routinely delayed.

Given the current heavy reliance on CHIMPs to comply with discretionary spending limits and the amount that discretionary appropriations would need to be reduced below current levels without savings from CHIMPs, changes to the treatment of CHIMPS could be phased in gradually and/or included in a sequester relief package that adjusted discretionary limits to account for the elimination or reduction in CHIMP savings.

4. Restrict the use of timing gimmicks to claim savings within the budget window

Current Practice: Current budgetary rules and statutory PAYGO apply to the estimated costs of legislation over the first five and ten years of budget windows. Statutory PAYGO excludes the impact of timing shifts which move collection of revenues from year eleven into year ten or delays spending from year ten to year eleven in calculating the effects over the ten-year window.

Problem: Although Statutory PAYGO excludes the effects of the most explicit timing shifts, it does not exclude more subtle timing shifts – such as pension smoothing and the expansion of Roth-style retirement accounts — that produce savings within the ten-year window while increasing future deficits. In addition, the existence of sequestration creates additional opportunities for timing shifts that were not anticipated in the timing shift rule in Statutory PAYGO because the timing shift provision in Statutory PAYGO does not prevent lawmakers from taking credit for accelerating the timing of spending cuts currently scheduled to take effect to occur within the budget window.

Proposal: Congress should amend statutory PAYGO and other budget enforcement rules to exclude savings from provisions, which CBO projects will significantly increase deficits beyond the ten-year window. This rule would preclude the use of offsets that produce savings within the ten year window at the expense of larger deficits beyond the ten year window such as pension smoothing and Roth IRA conversions, as well as more blatant timing gimmicks like accelerating sequester cuts or changing tax payment schedules. At a minimum, Congress should strengthen the current timing shift prohibition in PAYGO to close the loophole regarding sequester timing.

5. Prevent the use of artificially inflated baselines to claim savings

Current Practice: The CBO baseline assumes discretionary spending continues at the current year's level adjusted for inflation, including spending for Overseas Contingency Operations and emergency spending. When discretionary spending caps are in place, the rules have been interpreted to assume appropriations will be at the levels in the caps and then increase for inflation and other factors from the level set by the caps in the last year the caps are in place.

Problem: Policymakers can exploit baseline rules to claim savings relative to an artificially inflated baseline that overstates likely discretionary spending or take credit for reductions in temporary spending, which were already scheduled to decline or end.

For example, policymakers have attempted to claim savings by imposing limits on OCO spending that simply reflected the gradual reduction in temporary OCO spending that was already scheduled to occur as a result of the troop drawdown. More recently, the President's FY2016 budget claimed savings of $230 billion from extending discretionary spending caps through 2025 by measuring them relative to an inflated baseline that assumes discretionary spending will "snap back" to the pre-sequester BCA cap level in 2022 and beyond, even though discretionary spending levels in the budget are higher than they would have been if spending were assumed to increase with inflation from the post-sequester caps that will be in place under current law in Fiscal Year 2021.

Proposal: Reductions in projected spending not subject to the BCA caps should not be scored as achieving savings that can be used to offset other costs. It is inappropriate to claim savings from limiting the ability to continue one-time or temporary spending that was not originally subject to spending limits because it was supposed to be temporary spending.

In addition, Congress should clarify rules for calculating the baseline to use the FY 2021 sequester-level spending limit as the current law level used as the starting point to calculate discretionary spending levels for FY 2022 and beyond. This clarification should also provide that any increase in the discretionary spending limits for FY 2021 would automatically increase the discretionary spending baseline for FY 2022 and beyond and possibly scored with costs that should be offset. This clarification is consistent with current CBO practice.

6. Prohibit double-counting of increased revenues and spending cuts involving trust funds

Current Practice: Current scorekeeping conventions assume that spending on programs funded through trust funds with dedicated revenues will continue at current law levels regardless of whether the trust fund has sufficient revenues and assets to finance such spending. This convention means that depositing more money in the Highway Trust Fund (HTF) to allow spending above what current law allows does not increase spending relative to the CBO baseline.

Problem: Because the baseline assumes spending continues after trust fund depletion, general revenue transfers to a trust fund, such as the Highway Trust Fund or increases in dedicated revenues into a trust fund to prevent depletion, are not scored as increasing spending, even though they allow spending to be higher than what would otherwise be allowed. This loophole allows policymakers to transfer revenue to bail out the HTF without offsets. It also allows policymakers to double-count revenues dedicated to a trust fund such as an increase in the gas tax or reductions in spending from a trust fund to offset increased spending or reduced revenues elsewhere in the budget in addition to financing trust fund spending and extending solvency.

Proposal: The treatment of spending for programs funded through trust funds should be modified to reflect the limits on the amount of spending allowed under the law when trust fund assets are depleted. This change would mean that legislation increasing trust fund balances through general revenue transfers or increases in dedicated revenues would be scored with a cost for the increased spending, and legislation reducing trust fund spending would not be scored with savings that could be used to offset costs elsewhere in the budget. This would effectively require general revenue transfers bailing out a trust fund to be offset, and would prohibit any new revenues dedicated to a trust fund from being double-counted and used to offset other costs.

An alternative approach would be to adopt a rule requiring all general revenue transfers to be offset, and banning the use of increased revenues dedicated to a trust fund or reductions in spending from a trust fund as an offset for other purposes.

Ensure All Costs Are Subject to Budget Discipline

7. Limit the use of Overseas Contingency Operations as a slush fund

Current Practice: Under the Budget Control Act (BCA), statutory caps on defense and non-defense spending are adjusted to accommodate funding designated as spending for Overseas Contingency Operations (OCO, or war spending), effectively exempting any spending with the OCO designation from the discretionary spending caps.

Problem: Because spending designated as OCO is not subject to any spending limits, and there are no restrictions or limits on what spending can be designated as OCO, Congress has used this OCO designation as a "slush fund" for non-war defense and international affairs spending to circumvent the spending caps. The temptation to use OCO as a slush fund for other spending will increase as the amount of spending needed for legitimate OCO expenses decline.

Proposal: Congress should establish statutory caps on OCO spending. Caps could be established through a process in which the President is required to submit a plan for OCO spending consistent with military plans, with Congress considering, on an expedited basis, legislation setting limits based on that plan. Capping OCO would restrict the ability of Congress to use it to fund non-war projects because it would require reducing funding for legitimate OCO expenses. Importantly, setting a cap on OCO spending below the baseline, which assumes OCO spending continues at current levels adjusted for inflation, should not be scored as achieving savings that can be used to offset other costs. Alternatively, Congress could establish a point of order limiting the amount of spending that can be designated as OCO for purposes of BCA caps at the level requested by the President or another reasonable amount based on actual war-related needs.

In addition to or instead of establishing a limit on OCO spending, Congress should restrict abuse of OCO designation by codifying criteria for discretionary spending that can be designated as Overseas Contingency Operations (OCO) funding exempt from discretionary spending limits. OMB has published criteria for OCO spending which include: operations and maintenance resulting from transport to, from, and within the theater of operations; additional pay as required for personnel in the theater, procurement costs for losses incurred; military construction costs in the theater; and finally, required R&D for projects that can be delivered within a year. All spending designated as OCO would be required to include certification by Congress and President that it meets the criteria. This would make the OCO designation more honest.

8. Expand the deficit-neutrality requirement in PAYGO to apply to debt service

Current Practice: The PAYGO scorecard applies to direct increases in the deficit from changes in revenues or mandatory spending programs, but not the associated debt service, or interest costs, from increased borrowing.

Problem: Legislation with near-term costs and offsets later in the ten-year window may comply with PAYGO but still increase debt because of debt service from increased borrowing to cover the short-term costs. As a result, such legislation, which is officially "deficit-neutral" for purposes of PAYGO, actually results in higher debt.

Proposal: The definition of "budgetary effects" subject to Statutory PAYGO should be modified to include net interest costs or savings on the PAYGO scorecard. CBO would be required to provide an estimate of the debt service associated with legislation. This estimate would then be entered onto the PAYGO scorecard for sequestration enforcement. This proposal would force Congress to take a closer look at the timing of costs and offsets and would help stabilize the debt.

Conclusion

Budget gimmicks and other maneuvers to evade budget rules weaken the credibility of budget enforcement and undermine the transparency of fiscal policy. If Congress believes the budget enforcement rules are too strict, they should honestly acknowledge the costs of relaxing the rules and modify them as part of an overall fiscal plan instead of relying on gimmicks and evasions to circumvent budget rules. Any agreement providing sequester relief or otherwise relaxing the requirements of budget rules should be accompanied by measures strengthening enforcement to ensure strict compliance with the revised requirements.

About the Better Budget Process Initiative

There is a growing consensus that the budget process is broken. The *Better Budget Process Initiative* will put forward specific options to reform and improve the budget process in a wide range of areas, including increasing focus on the long-term fiscal outlook, improving the process for dealing with the debt limit, strengthening statutory budget enforcement, revising the content and structure of the budget resolution, moving to biennial budgeting, and addressing treatment of tax expenditures in the budget process.

Other papers:
Improving the Debt Limit
Improving Focus on the Long-Term
The Budget Act at 40: Time for a Tune Up?