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Analyzing the President's New Budget Framework
April 21, 2011

Last week, President Obama gave a speech outlining his plan to reduce the deficit and stabilize the debt in the coming years. This new budget framework was in many ways a revision of his February budget, and outlined $4 trillion worth of deficit reduction through 2023. This framework represents a positive step forward, both because of the substance of the deficit reduction and because it represents the President's willingness to engage in negotiations to address our mounting debt.

While the new framework (hereafter the "President's Framework") is a substantial improvement over the President's February FY 2012 budget request, it still falls short of the total debt reduction proposed by the Fiscal Commission (which we believe should be seen as a minimum to strive for) as well as short of the House budget resolution, which is based on House Budget Committee Chairman Paul Ryan's (R-WI) proposal.

This paper attempts to compare the President's Framework on an apples-to-apples basis to the two other plans and the President's February budget. Over ten years, the President's Framework saves about $2.5 trillion. Using CBO rather than OMB numbers, we estimate that the plan is unlikely to result in a declining debt-to-GDP ratio, and would thus rely on the proposed "Debt Failsafe" to achieve further savings.

Fig. 1: Comparison of Budget Projections and Savings

	President's Framework^	President's Budget	House Budget	Fiscal Commission
10-Year Savings (billions)				
From Adjusted Baseline*	**$2,480**	**$0**	**$4,020**	**$4,060****
From Current Law	-$250	-$2,730	$1,290	$1,420
2021 Debt (% of GDP)				
Claimed Level	N/A	77%	67%	<65%
CRFB Re-estimate	77%	87%#	69%	68%
2021 Deficit (% of GDP)				
Claimed Level	~2.0%	3.1%	1.6%	<1.2%
CRFB Re-estimate	~3.0%	4.9%	1.9%	1.6%

Note: Negative numbers represent costs as opposed to savings.
*Adjusted baseline assumes Congressional Budget Office estimates for extended tax cuts for all but top earners, declining war costs, and annual doc fixes.
**Excludes savings from assuming lower war costs than in the adjusted baseline.
#As re-estimated by the Congressional Budget Office.
^Assumes Debt Failsafe is not activated.

Understanding the President's Framework[1]

In the President's Framework released last week, the President calls for $4 trillion of deficit reduction over 12 years with savings stemming from almost all areas of the budget. About half of the proposed savings would come from spending cuts, including reductions in security and non-security discretionary spending, new health care savings, and cuts to a number of mandatory spending programs. Another quarter of the deficit reduction would come from cutting tax expenditures as part of comprehensive tax reform. The remaining savings would come from the reduced interest payments resulting from lower debt levels. In addition to these measures, the President calls for a "Debt Failsafe," which would kick in if debt projections by 2014 were not stabilized or declining in the second half of the decade.

The Administration estimates that its plan would reduce the deficit to about 2.5 percent of GDP in 2015, and closer to 2 percent of GDP by the end of the decade.

Discretionary Spending

On non-security spending, the President proposes building on the discretionary cuts from the recent Continuing Resolution that defines spending levels for the remainder of FY 2011 in order to generate savings similar to what was recommended by the Fiscal Commission. Though the President does not specify how he would achieve this, locking in this year's spending levels and then growing them a bit below the rate of inflation would likely accomplish that goal. On security spending, the President calls for holding growth below the level of inflation. The Administration estimates these changes would save nearly $1.2 trillion over 12 years.

Health Care Spending

The President proposes a number of reforms meant to reduce federal health spending. On Medicaid, the President's Framework proposes replacing the current set of federal matching formulas with a uniform matching rate and working with state governors to enact additional efficiency-improving reforms. In addition, the Framework includes various reforms to the Medicare prescription drug program, along with a number of anti-fraud and anti-abuse measures. The President's Framework also touts a new patient safety initiative meant to reduce preventable medical complications. The Administration estimates these changes would save $480 billion over 12 years.

In order to reduce long-term health care spending growth, the President's Framework would strengthen the Independent Payment Advisory Board (IPAB) created under the health care reform legislation by reducing its target for Medicare cost growth from GDP

[1] Estimates in this section are as reported by the Administration. All savings judged against the Administration's "adjusted baseline," and in some cases build on savings outlined in the President's FY 2012 budget request while in other cases the recommended savings are new.

plus one percent per beneficiary to GDP plus 0.5 percent per beneficiary beginning in 2018. To make these targets more achievable, IPAB would be given more flexibility in determining benefit design, and savings would be enforced with an automatic sequester if policymakers (including IPAB) fail to act to control cost growth.

Social Security Reform

On Social Security, the President largely punts as he did in his February budget, but does voice his support for "bipartisan efforts to strengthen Social Security for the long haul." The President reiterated the principles of Social Security reform which he laid out in his February budget, calling for reform that restores long-term solvency, avoids privatization, does not "slash" benefits, maintains the base benefit for current beneficiaries, and strengthens retirement security for the vulnerable and maintains robust disability and survivors benefits.

Other Mandatory Spending

The President proposes a target of finding $360 billion over 12 years in savings from non-health, non-Social Security mandatory programs. The President's Framework highlights some of the proposals in the President's February budget (unemployment reform, cuts to farm subsidies, changes to PBGC, etc.) and the Fiscal Commission's plan, but does not specify precisely where the savings should come from – other than to say that reforms should protect the most vulnerable.

Tax Reform

The President calls for new revenue on top of what would be raised by allowing the upper-income tax cuts to expire. Though his proposal is vague, the President's Framework calls for "reducing tax expenditures so that there is enough savings to both lower rates and lower the deficit," and suggests that reform should protect the middle class and promote economic growth. He also calls for reducing corporate tax expenditures in order to lower the corporate tax rate. The Administration calls for these changes to save $1 trillion over 12 years (in addition to revenues from letting the upper income tax cuts expire).

Budget Enforcement

The President calls for a "Debt Failsafe" to enforce debt reduction efforts. The failsafe would require that, by 2014, debt be projected to be on a stable or declining path for the latter half of the decade. Should that not be the case, the failsafe would trigger an across-the-board spending cut to a number of federal programs, as well as to tax expenditures. Social Security, Medicare benefits, and low-income programs would not be hit by the trigger. (Read more about the debt target and trigger idea at http://crfb.org/document/peterson-pew-debt-targets-and-trigger-central-presidents-proposal.)

Re-Estimating the Savings in the President's Framework

President Obama claims that his framework saves $4 trillion. But in order to judge that claim, one must answer the questions "over what time period?" and "compared to what?"

Breaking with general convention, the President's Framework measures its savings over a 12-year period – through 2023 instead of 2021. As is more common, the Administration calculates savings for the President's Framework by comparing it to an "adjusted baseline," which assumes lawmakers act as expected and continue to extend a number of expiring policies that would increase deficits.

CRFB has constructed a similar adjusted baseline using projections from the Congressional Budget Office (CBO) rather than the Office of Management and Budget (OMB) as the starting point for comparison.[2] This baseline assumes the permanent continuation of the 2001/2003/2010 tax cuts for income below $250,000 per year, continued AMT patches, an estate tax at 2009 levels after 2012, the $50 billion per year war spending plugs in the President's February budget, and annual "doc fixes." Using CBO's baseline in place of OMB's projections is particularly important for measuring the impact of discretionary cuts, which change substantially depending on baseline projections. In order to flesh out the recommendations, we also make a number of our own assumptions to approximate what we believe is the intent of the President's Framework.[3]

Our analysis finds that:

- The Administration estimates that the President's Framework would save **$4 trillion** over 12 years when compared to an adjusted baseline that assumes tax cut extensions for those making below $250,000 per year, lower war costs, and annual doc fixes.
- Because much of the savings would come in the last years of the 12-year period, the Administration assumes **$2.9 trillion** in savings over the standard 10-year period using OMB projections.
- However, when using CBO numbers to construct an adjusted baseline, we find savings would be **$2.5 trillion** over 10 years.

[2] The President's adjusted baseline may make small adjustments that we do not, such as for Pell grants.
[3] For example, with regards to proposals from the President's February budget not addressed in this framework, we generally assume the President would enact changes either on a pay-as-you-go basis or else not at all. Note that we also had to take some liberties in re-estimating the Fiscal Commission recommendations – which only go through 2020 and were originally estimated based on an adjusted version of CBO's August 2010 baseline. In addition, we made one adjustment to the House Budget Resolution, fully charging it for annual "doc fixes" in order to put it on level ground with other estimates.

- Compared to current law (which assumes the expiration of all the 2001/2003/2010 tax cuts as well as the expiration of other current policies), the President's Framework would actually increase deficits by **$250 billion** over 10 years.

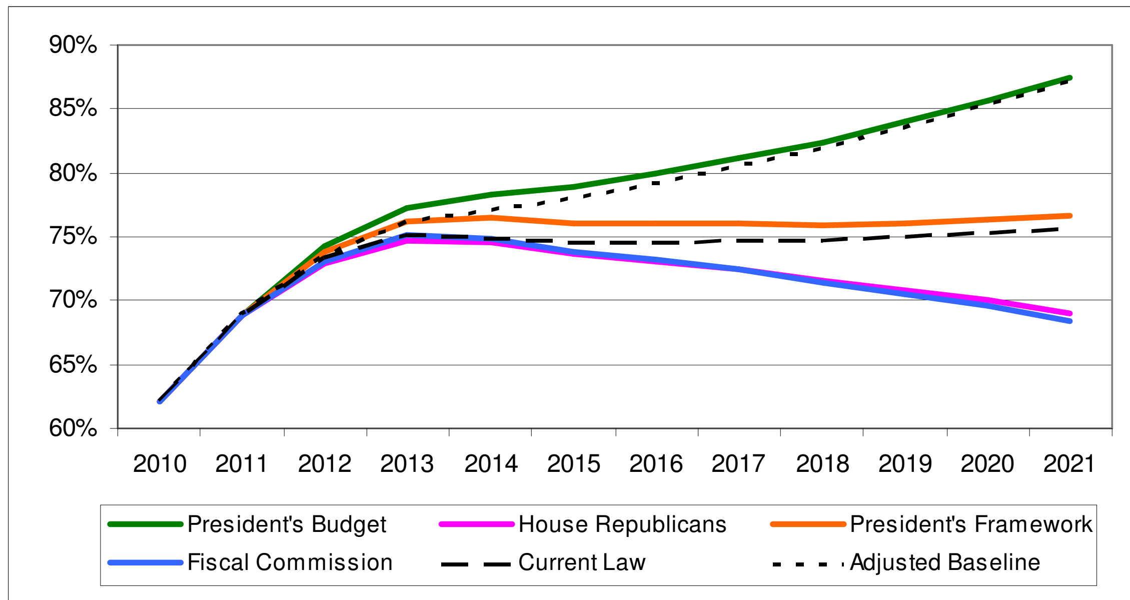
Fig. 2: Savings under the President's Framework (Billions)

	Administration Estimates		CRFB Estimates	
	12-Year Savings	10-Year Savings	10-Year Savings from Adjusted Baseline	10-Year Savings from Current Law
Security	$400	$290	$130	$1,170*
Non-security	$770	$620	$450	$450
Health	$480	$340	$340	$40
Other Mandatory	$360	$290	$290	$30
Revenue	$1,000	$760	$760	-$1,980
Interest	$990	$620	$510	$40
Total	**$4,000**	**$2,920**	**$2,480**	**-$250**

Note: Negative numbers represent costs as opposed to savings.
*Incorporates President's assumed reductions in war spending.

Measured against CBO assumptions, it does not appear that the $2.5 trillion of deficit reduction in the President's Framework would be sufficient to reduce the deficit to 2.5 percent of GDP in 2015 or 2 percent in 2020, as claimed. Using reasonable phase-in assumptions, we estimate that unless the debt failsafe is employed (as it would be in this circumstance), deficits would remain at or above 3 percent of GDP throughout the decade. As a result, debt would continue to slowly increase as a share of the economy, reaching 77 percent of GDP by 2021.

Fig. 3: Debt Projections under Various Fiscal Reform Plans (Percent of GDP)



Note: Estimates for President's Framework assume Debt Failsafe not employed.

Comparing the President's Framework to Other Plans

The $2.5 trillion in deficit reduction in the President's Framework represents a substantial improvement from the President's February budget – which essentially includes no deficit reduction relative to the adjusted baseline (and therefore increases the debt to 87 percent of GDP). However, the President's Framework falls short of both the Fiscal Commission recommendations and those from the House Budget Committee, both of which would reduce the deficit by over $4 trillion and reduce the debt to below 69 percent of GDP by the end of the 10-year period.

The House budget saves substantially more from non-security discretionary, health care, and other mandatory spending than does the President's Framework, while the Fiscal Commission plan saves more from security discretionary, health care, Social Security, and tax reform. However, the President's Framework and the Fiscal Commission both propose special processes for ensuring debt is at least stabilized – or falling, under the President's Framework – as a share of the economy in the second half of the decade.

Fig. 4: 10-Year Savings under Various Plans (Billions, vs. Adjusted Baseline)

	President's Framework	President's Budget	House Budget	Fiscal Commission
Security Spending Changes	$130	-$350	-$90	$750
Non-Security Discretionary Cuts	$450	$250	$1,680	$460
Social Security Reform	N/A	N/A	N/A	$300#
Repeal of Select Provisions of Health Reform	N/A	N/A	$590#	-$90+
Other Health Spending Reductions	$340	$50	$800	$490
Other Mandatory Spending Cuts	$290	-$200	$980	$290
Tax Reform & Revenue Changes	$760#	$300#	-$610#	$1,220#
Interest Savings	$510	-$50	$650	$640
Total Deficit Reduction	**$2,480**	**$0**	**$4,020**	**$4,060***
Memorandum:				
Total Deficits	***$6,990***	***$9,470***	***$5,450***	***$5,320***

Note: Negative numbers represent costs as opposed to savings. Totals may not add due to rounding. All numbers estimated by authors, using data from CBO, the Fiscal Commission, and the Administration. Estimates should be considered rough, and are subject to considerable uncertainty.
#Includes revenue and outlay effects.
+Commission recommends "reforming or repealing" the CLASS Act. Repeal would cost $90 billion over the next decade, since funds from premiums come in advance of benefit payouts.
*Excludes savings from assuming lower war spending, which are included in total deficits.

Conclusion

By presenting his own framework for deficit reduction, the President has done a substantial service in moving the ball forward. Not only is the President's Framework a significant improvement over his February budget proposal – to the tune of $2.5 trillion – but it also represents a balanced approach to begin improving the nation's finances. This is a move we strongly praise.

At the same time, we believe the deficit reduction achieved by the President's Fiscal Commission – $4 trillion over ten years – is the appropriate standard to strive for. Using CBO assumptions, it appears unlikely that the policies proposed in the President's Framework would be sufficient to reduce debt to a manageable level – at least not without further action spurred by the proposed Debt Failsafe. Thus, we believe the President should work with Congress to offer additional savings on top of what he has already proposed.

To the Administration's credit, they do propose a budget process to ensure a stable debt-to-GDP ratio even if their policies do not achieve this. A well designed Debt Failsafe such as the one they have proposed could be a powerful and useful tool to help ensure the debt remains under control and to help encourage policymakers to propose additional deficit reduction policies.

Recent warnings from the Standard & Poor's credit agency and others have made it clear that the United States has limited time to prove to the markets that we are serious about putting our fiscal house in order. The President should work with leaders of both parties and both chambers to put in place a legitimate plan to shore up the nation's finances this year.

Deficit Reduction Proposals under Each Plan

	President's Framework	President's Budget	House Budget	Fiscal Commission
Discretionary Spending	Holds non-security spending to levels consistent with Fiscal Commission (real 2008 levels). Identifies additional security savings in order to hold defense growth below inflation.	Freezes non-security spending through 2015 and holds the growth of defense spending to near inflation as recommended by Secretary Gates.	Reduces non-security spending to nominal 2006 levels in 2012, and holds the growth of defense spending to near inflation as recommended by Secretary Gates.	Freezes both security and non-security spending in 2012 and returns them to real 2008 levels in 2013.
Health Care Spending	Proposes $340 billion in savings from standardizing the Medicaid matching rate, prescription drug reforms, patient safety initiatives, and anti-fraud measures. Strengthens IPAB by broadening its mandate and limiting Medicare growth to GDP+0.5% per beneficiary instead of GDP+1%.	Identifies $50 billion in health savings from reducing state Medicaid gaming, prescription drug reforms, and various others. Assumes but does not identify an additional $315 billion in unspecified savings.	Saves nearly $800 billion from block granting Medicaid and nearly $600 billion from repealing the tax and coverage provisions of health reform. Transforms Medicare into a premium support program, and limits per beneficiary growth of premium support and block grants to inflation.	Saves $400 billion from increasing Medicare cost sharing, reducing various provider payments, limiting state Medicaid gaming and making other changes. Establishes a long-term budget for total health care spending to limit health care cost growth to GDP+1%.
Social Security	Makes no changes but calls for reform to restore solvency without privatization, "slash[ing]" benefits, or reducing the base benefit of current retirees.	Makes no changes but calls for reform to restore solvency without privatization, "slash[ing]" benefits, or reducing the base benefit of current retirees.	Proposes a process where the President and Congress must put forward plans to restore solvency if the program is projected to be insolvent.	Enacts a comprehensive solvency plan which relies on making the benefit formula more progressive, indexing the retirement ages to longevity, raising the taxable maximum, and other changes.
Other Mandatory	Aims to save $290 billion, building on savings identified in the President's February budget.	Reforms farm subsidies, student loans, PBGC, unemployment insurance, and other programs. Reinvests the bulk of the savings into new programs.	Saves over $900 billion from reforming civil service retirement, reducing farm subsidies and student loans, block granting food stamps, and other changes.	Saves nearly $300 billion by indexing programs to chained CPI, reforming civil service and military retirement, reducing farm subsidies, and other changes.
Tax Reform	Calls for raising $760 billion by cutting tax expenditures (on top of letting the upper income tax cuts expire). Calls for further reduction in tax expenditures to finance cuts to individual and corporate rates.	Proposes $300 billion of new net revenue (on top of letting the upper income tax cuts expire), mainly from limiting itemized deductions for high earners and reducing various corporate tax breaks.	Calls for revenue neutral tax reform that cuts tax expenditures and lowers the top individual and corporate rates to 25% or lower. (Reform loses money relative to the adjusted baseline used in this paper).	Raises $1 trillion from tax reform by cutting tax expenditures which allows the reduction of the top individual and corporate rates to 29% or lower. Also increases the gas tax and indexes tax provisions to chained CPI.
Budget Process	Includes a "debt failsafe" which automatically reduces spending and tax expenditures if, in 2014, debt is projected to increase as a share of the economy.	Renews statutory PAYGO and proposes enhanced rescission authority (modified line-item veto).	Caps total spending as a share of the economy and establishes a regular review process for mandatory programs.	Establishes a debt stabilization process to fast-track deficit reduction if debt grows in any year after 2015.

Note: All numbers measured over 10 years, relative to adjusted baseline used in this paper.