# COMMITTEE FOR A RESPONSIBLE FEDERAL BUDGET

**Corrected Version of Congressional Action Update**

Memo to: Board and Members, and Friends
From: Carol Wait
Date: April 5, 2000

Subject: Budget Issue Update
Budget Comparisons—
A Different Point of View

**Tax Cuts**

Contrary to what you may have heard, the real threat to fiscal discipline this year does not lie in the Republican Congress' proposed tax cuts.

First, the tax cuts in the House Passed Budget (and the very similar resolution before the Senate this week) simply are not large enough to threaten budget discipline or the economy. They never approach one-half of one percent of GDP in any year. Second, the President is unlikely to sign into law tax cuts that aggregate even to the amounts permitted by the Congressional Budget Resolutions.

Differences between Congressional Republicans and the Administration go beyond the question of how big tax cuts should be. Last week the *Richmond Times Dispatch* quoted Secretary of the Treasury Lawrence Summers, on the Administration views, "…the administration thinks the most important objectives of tax law deal with helping taxpayers through 'key moments of their lives,' such as home buying, educating their children and preparing for retirement". By contrast, Republicans in Congress tend to favor broad based cuts that return money to people more or less proportionately to the amounts they pay in taxes—without strings attached requiring specific purchases or behavior to take advantage of the tax reductions.

**Spending**

By contrast, there is a very real risk that large and growing surplus projections will spawn a spending spree that could threaten fiscal discipline.

220 ½ E Street, N.E. Washington, DC 20002*Tel. (202) 547-4484*Fax (202) 547-4476*CRFB @ aol.com

Taking the President's Budget and the Congressional Budget Resolutions at face value, spending will go up at least $300 billion per year over the next five years. That is twice the cost of tax cuts in the Congressional Budgets. And the actual increase likely will be considerably larger than any of these budget proposals suggest. (See table at page 3.)

All versions of the budget tend to understate the magnitude of proposed spending increases.

The President's Budget includes $75 billion over five years in offsetting receipts, e.g., increases in receipts from proposals to transfer earnings from Federal Reserve banks, increase customs and harbor maintenance fees and Superfund taxes. Including those items as offsetting receipts, i.e., negative outlays, the Administration reduces total outlays in their budget $75 billion below the actual cost of their proposals. Congress is not likely to enact these proposals and, even if they did, the Budget Enforcement Act and traditional scorekeeping conventions (properly in our view) should prohibit using such receipts to reduce expenditures as the Administration proposes to do.

The Congressional Budget contains a $20 billion/five year "reserve fund" for Medicare prescription drugs. Democrats have argued that is not enough to pay for the program they hope to see enacted. The Senate version of the budget contemplates $5.5 billion in emergency farm support, and $11 billion for longer-term reform of agricultural programs. Even so, the Congressional budget is a billion below the President for farm support in FY 2001. Recent history suggests that position will not hold. If anything, Congress may appropriate more than the Administration request for farmer support, as even the President's budget represents a $12 billion drop in aid FY 2000-FY 2001.

The President wants $12 billion more in outlays for discretionary programs next year than the Congressional Budget would provide (even if the discretionary caps were adjusted upward as the Senate version of the Budget assumes they will be). If Congress and the President do not agree on new discretionary budget caps and write the new caps into law very early this year, we think it is entirely likely that total discretionary spending will exceed amounts contained in the President's budget for FY 2001. That certainly has been the pattern over the past two years. If they do enact new caps, history suggests the new caps generally will be observed for the first year or two.

Congress has passed, and the President almost certainly will sign, a bill to repeal the earnings limit for Social Security Recipients under 70 years of age. Social Security benefit payments will increase as a result.

Budget Comparisons
fiscal years--$ in billions--totals may not add due to rounding

| | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | Total 2010-2005 | |
|---|---|---|---|---|---|---|---|---|
| **President's Budget (CBO Re-estimate)** | | | | | | | | |
| **Revenues** | **1946** | **2026** | **2097** | **2171** | **2262** | **2352** | **10908** | |
| **Outlays** | **1778** | **1836** | **1902** | **1958** | **2033** | **2114** | **9843** | |
| Disc | 611 | 635 | 656 | 670 | 684 | 701 | 3346 | |
| Man | 1021 | 1071 | 1131 | 1204 | 1288 | 1376 | 6070 | |
| Off Rec. | -79 | -88 | -95 | -110 | -117 | -126 | -536 | |
| Net Int. | 225 | 218 | 209 | 194 | 179 | 162 | 962 | |
| **Surplus** | **168** | **190** | **196** | **213** | **228** | **238** | **1065** | |
| on-budget | 15 | 24 | 14 | 18 | 20 | 14 | 90 | |
| off-budget | 153 | 166 | 182 | 195 | 208 | 224 | 975 | |
| **Congressional Budget Resolution*** | | | | | | | | **Plus/Minus President** |
| **Revenues** | **1944** | **2003** | **2071** | **2146** | **2225** | **2318** | **10763** | 145 |
| **Outlays** | **1780** | **1826** | **1886** | **1944** | **2008** | **2081** | **9745** | -98 |
| Disc | 612 | 623 | 641 | 653 | 662 | 675 | 3253 | -93 |
| Man | 1022 | 1069 | 1126 | 1189 | 1258 | 1340 | 5982 | -88 |
| Off Rec. | -79 | -85 | -92 | -94 | -93 | -99 | -463 | -73 |
| Net Int. | 225 | 219 | 211 | 196 | 181 | 165 | 973 | 11 |
| **Surplus** | **164** | **177** | **185** | **202** | **217** | **238** | **1019** | -46 |
| on-budget | 11 | 11 | 3 | 7 | 9 | 13 | 42 | -48 |
| off-budget | 153 | 166 | 182 | 195 | 209 | 225 | 976 | 1 |

* These numbers are from the Senate Budget Committee "Chairman's Mark", as that provides more detail than any other source. There are differences between the House and Senate Budget Resolutions, but most of those differences go to items such as "emergency funding", "reserves" and budget process reforms. The numbers are substantially similar in the two versions of the budget. (In 2001, the Senate totals compare to the House as follows: Revenues -$3.2 billion; Budget Authority +$2.1 billion; and Outlays -$0.3 billion.

Some argue that the increases in discretionary spending are relatively benign, as they are controllable through appropriations every year. But the President has proposed to recalibrate caps for discretionary spending to take into account inflation; and discretionary spending increases over the last two years were larger than at any time since the mid-1960's. This seems to reflect the end of an era in which we funded increases in domestic discretionary programs from cuts in defense spending. Congress and the Administration, and both major party presidential candidates are committed to increase defense spending. It seems likely that very substantial upward pressure on discretionary spending will continue for at least as long as surplus projections continue to grow.

Perhaps the next President and the new Congress to be elected this fall will reach consensus on a fiscal policy framework budget process rules more appropriate to the surplus environment. But that won't happen this year. Recent projections show Social Security and Medicare solvency improving. Recent proposals would increase the cost of Social Security. The same is true of Medicare. If productivity growth continues, that could ease the long-term economic and budget problem, but current Social Security and Medicare benefits cannot be funded from projected payroll taxes once the baby boom generation begins to retire. Enriching benefits only makes the problem worse. Funding Social Security and Medicare from general revenues would require cuts in other popular programs. The only other alternatives are huge tax increases and/or a resurgence of very large deficits and debt. But these issues are absent from current budget debates.

Federal spending is growing, and all of the real growth is concentrated in spending for the elderly. CBO writes,[1] "By 2030, under current policies, spending for Social Security, Medicare and Medicaid is expected to rise by 75 percent as a share of GDP and will represent more than two-thirds of federal spending compared to 40 percent today. If projected surpluses do not materialize, the approaching budgetary pressures will intensify as a result of higher debt-service costs. More important, if surpluses are realized and are used to pay down debt, they will enhance the long-run prospects of the economy and help ease the burden on active workers (in the future) of supporting larger numbers of retirees."

Surpluses are not a new source of government finance. Surpluses represent tax receipts in excess of government outlays. We support using current surpluses to retire debt held by the public. Like Chairman Greenspan, we don't think there is any compelling need for large tax cuts right now. However, we also agree with the Fed Chairman that tax cuts may be preferable to large spending increases. Over twenty-five years wrestling with huge Federal deficits, we observe that it proved much easier to raise taxes than to cut spending—and it proved almost impossible to cut popular elderly entitlements. There were some restraints on the growth in Medicare, but the tide seems to be running in the opposite direction today. It will be much harder to cut elderly programs as the baby boom generation begins to retire.

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[1] Economic and Budget Outlook: Fiscal Years 2001-2010, pages 7 and 9.

## Baselines

The Congressional Budget Office published three baselines this year. The capped baseline assumes spending consistent with the discretionary caps contained in the 1997 Balanced Budget Act. The freeze baseline assumes appropriations remain frozen at the FY 2000 enacted level (adjusted for advance appropriations) through 2010. The inflation-adjusted baseline would hold discretionary spending constant for projected increases in inflation through 2010.

The three baselines are identical except for discretionary spending, debt service cost, and surplus projections. The table below shows ten year surplus projections under each scenario.

**Baseline Surplus Projections FY 2000-FY2010**

$ in billions--totals may not add due to rounding

| | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | total |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Capped | | | | | | | | | | | | |
| on-budget | 26 | 73 | 115 | 129 | 139 | 154 | 202 | 234 | 261 | 300 | 341 | 1948 |
| off-budget | 453 | 166 | 182 | 195 | 209 | 225 | 238 | 253 | 266 | 280 | 293 | 2307 |
| total | 179 | 239 | 297 | 324 | 348 | 379 | 440 | 487 | 527 | 580 | 634 | 4255 |
| Freeze | | | | | | | | | | | | |
| on-budget | 26 | 27 | 54 | 77 | 106 | 132 | 197 | 248 | 290 | 349 | 410 | 1891 |
| off-budget | 153 | 166 | 182 | 196 | 209 | 225 | 239 | 254 | 267 | 281 | 294 | 2313 |
| total | 179 | 192 | 237 | 273 | 315 | 358 | 436 | 502 | 558 | 629 | 704 | 4204 |
| Inflation-Adjusted | | | | | | | | | | | | |
| on-budget | 26 | 15 | 29 | 36 | 42 | 48 | 92 | 121 | 138 | 169 | 202 | 893 |
| off-budget | 153 | 166 | 182 | 195 | 209 | 225 | 238 | 253 | 266 | 280 | 293 | 2307 |
| total | 179 | 181 | 212 | 231 | 250 | 273 | 330 | 374 | 404 | 449 | 495 | 3199 |

Republicans in Congress used the Freeze Baseline as the basis for their budget resolution. The Administration’s current services baseline is more nearly similar to the CBO inflation-adjusted base. Nobody is using the capped base, except for comparative and informational purposes. Once again this year the President and Congress will mix baselines and policy as they discuss differences. That can be very confusing. Republicans in Congress want bigger tax cuts. The Administration wants to spend more. The Administration starts with a higher base for spending—thus limiting amounts available for tax cuts. Congress starts with lower spending in the base. If Congress agrees to spend as much or more than the President proposes in FY 2001, they must hope revenue and surplus projections continue to rise. Otherwise they would have to delay the impact of some proposed tax reductions or risk dipping into Social Security Trust fund surpluses.