Committee for a Responsible Federal Budget

Sequester Offset Solutions Plan

September 16, 2015

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October 1 marks not only the beginning of fiscal year 2016 (FY 2016), but the return of sequester-level caps that were temporarily lifted under the 2013 Ryan-Murray Bipartisan Budget Act. These sequester-level caps, which are roughly $90 billion lower than the Budget Control Act caps, will limit appropriated spending to $1,017 billion in FY 2016, only $3 billion higher than the FY 2015 limit of $1,014 billion.

In their budgets, neither Congress nor the President have supported spending exactly at the sequester levels. The President's budget would increase the defense and non-defense spending caps by $38 billion each for FY 2016 while the Congressional budget resolution would effectively do the same just for defense by circumventing the defense caps through the uncapped war category.

There is a strong case for providing sequester relief by increasing the caps because the automatic sequester cap reductions were originally put in place to encourage the "Super Committee" to enact tax and entitlement reform, and because the cuts are only temporary in nature and focus primarily on the part of the budget growing the most slowly.

However, sequester relief must be done in a fiscally responsible way. Specifically, lawmakers should abide by the following three principles:

- **Fully offset all costs of sequester relief over ten years.**
- **Focus on policies that would save increasing amounts over the long term.**
- **Strengthen budget enforcement to prevent gaming of the spending caps.**

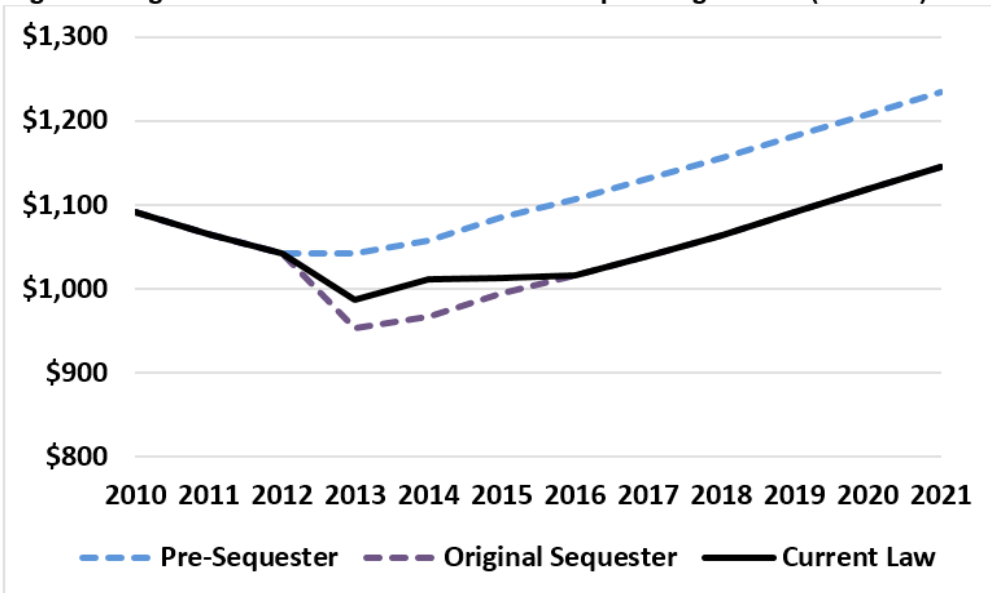
There are many ways lawmakers could do responsible sequester relief, and the Sequester Offset Solutions (SOS) plan offers one such approach. This plan would provide $300 billion of total sequester relief by restoring half of the sequester's cuts to discretionary spending over the next two years and then indexing discretionary caps to inflation through 2025. The first two years of sequester relief would be paid for through a combination of mandatory spending reductions and offsetting receipts, while more permanent changes would be paid for with the mandatory and revenue savings from adopting the chained Consumer Price Index (CPI).

Fig. 1: Summary of the Sequester Offset Solutions (SOS) Plan

Policy	10-Year Savings
Establish New Spending Caps Above Sequester Levels	**-$300 billion**
Offset 2-year relief with targeted mandatory savings and receipts	*$110 billion*
Offset further relief with chained CPI revenue and mandatory savings	*$210 billion*
Total Offsets	**$320 billion**
Net Interest Costs	***-$20 billion***
Net 10-Year Deficit Impact	**$0 billion**
Memo: Social Security impact not counted above	*$125 billion*

Background

Fig. 2: Budget Control Act and Current Law Spending Levels (Billions)



Source: CBO, OMB, House Budget Committee

The Budget Control Act (BCA), enacted in 2011, established statutory caps on discretionary spending and set up the Joint Select Committee on Deficit Reduction (or, the "Super Committee") with the goal of reaching a budget deal to achieve at least $1.2 to $1.5 trillion in savings over ten years. The Super Committee's failure set in motion the BCA's enforcement of that budget goal, commonly referred to as the sequester. These spending reductions are divided evenly between defense and non-defense spending, with most of the savings coming from reducing the BCA's original discretionary spending limits and the remainder coming from across-the-board cuts to non-exempt mandatory spending programs.[1]

The BCA's "pre-sequester" caps reduced discretionary spending significantly from their prior trajectory, but it then allowed the caps to grow in nominal terms by about 2 percent per year (roughly the rate of inflation) – from $1,043 billion in 2012 up to $1,234 billion by 2021. The failure of the Super Committee triggered reductions in these spending levels, including by scheduling a $90 billion across-the-board discretionary cut to take place in January 2013 and a reduction of future year spending caps by roughly $90 billion per year.

To date, policymakers have never allowed these sequester cuts to remain fully in effect. In early 2013, the "fiscal cliff" deal delayed and modestly reduced the size of scheduled 2013 sequester cuts. And in December 2013, lawmakers enacted the Ryan-Murray Bipartisan Budget Act, which increased FY 2014 and FY 2015 discretionary spending by nearly $65 billion. In both cases, costs were fully offset. Beginning in FY 2016, sequester-level caps are scheduled to return.

Current law calls for limiting total FY 2016 discretionary spending to $1,017 billion, only $3 billion above current levels, but neither the President nor Congress has proposed sticking to the spending levels prescribed by the sequester. The President has proposed $75 billion of sequester relief for FY 2016 – split evenly between defense and non-defense – with sustained but shrinking relief over time that would cost $370 billion through 2025. These costs would be offset by other measures in the President's budget. The FY 2016 Congressional budget resolution has called for similarly-sized increases in defense spending (though not non-defense spending), but rather than doing so by lifting the caps, it would circumvent them through the use of uncapped war accounts – a practice we have referred to in the past as the "war gimmick."

Clearly, there is an interest in lifting current law sequester level caps. Although the sequester has helped to reduce deficits, few observers believe it to be wise policy. Whereas our debt issue is more long-term in nature, the sequester makes equal-

1 Reductions do not apply to Social Security nor to means-testing programs such as food stamps or Medicaid. Although Medicare is not exempt, Medicare cuts are generally limited to 2% of the program.

sized cuts each year that are only temporary, unnecessarily harming short-term economic growth while not significantly changing the long-term trajectory of debt. Moreover, the sequester focuses almost entirely on discretionary spending, which is not a driver of the long-term debt.

Principles For Sequester Relief

If lawmakers increase the spending caps, they should abide by the following three principles to best improve our nation's fiscal situation and follow the intent of the Budget Control Act:

- **Fully offset any sequester relief over ten years.** Lawmakers should fully offset sequester relief, preferably including interest costs, without resorting to gimmicks.
- **Focus on policies that would save increasing amounts over the long term.** Lawmakers should replace short-term cuts with permanent long-term savings that significantly reduce projected deficit and debt levels in the second decade and beyond.
- **Strengthen budget enforcement to prevent gaming of the spending caps.** Lawmakers should accompany higher discretionary caps with new enforcements to make sure those caps are truly abided by and not circumvented by various gimmicks.

Fig. 3: Budgetary Effect of Sequester Offset Solutions Plan

Policy	Ten-Year Savings
Enact Sequester Relief and Extend Caps Through 2025	**-$300 billion**
Expand Ryan-Murray federal retirement reforms	$20 billion
Expand Ryan-Murray PBGC solvency measures	$10 billion
Index Ryan-Murray user fees to inflation	$10 billion
Replace Medicare sequester	$10 billion
Build on Ryan-Murray Deal	**$50 billion**
Increase Medicare means-testing	$15 billion
Enact Medicare site-of-service payment reforms	$15 billion
Streamline student loan Income-Based Repayment rules	$15 billion
Reduce farm subsidies	$10 billion
Enact oil and gas revenue reforms	$5 billion
Enact Mandatory Savings and Receipts from President's Budget	**$60 billion**
Switch to chained CPI for non-Social Security spending	$85 billion
Switch to chained CPI for the tax code	$150 billion
Enact enhancements to low-income programs	-$25 billion
Chained CPI Savings	**$210 billion**
Interest	**-$20 billion**
Total Costs	**-$320 billion**
Total Savings	**$320 billion**
Memo: Chained CPI Social Security Savings (assuming old-age bump)	*$125 billion*

Source: CBO, OMB, CRFB calculations
Note: Numbers may not add up due to rounding

The Sequester Offset Solutions Plan

The Sequester Offset Solutions plan is a four-part plan to replace a portion of the discretionary cap reductions under the sequester with more thoughtful long-term savings. Specifically, the plan would:

> **1. Establish New Spending Caps above Sequester Levels**
>
> **2. Offset Two-Year Sequester Relief with Targeted Mandatory Savings and Receipts**
>
> **3. Offset Continued Sequester Relief by Adopting the Chained CPI**
>
> **4. Strengthen Enforcement of Budget Caps**

Separately, CRFB has released plans to pay for the extension of expiring tax provisions known as the "tax extenders" with new tax revenue (largely from compliance) and a highway trust fund plan that includes spending controls and a gas tax increase.[2] One or both of these plans could be combined with the SOS plan.

2 See CRFB, The Road to Sustainable Highway Spending (May 2015) and PREP Plan: Paying for Reform and Extension Policies (November 2014).

1. Establish New Spending Caps above Sequester Levels (-$300 billion)

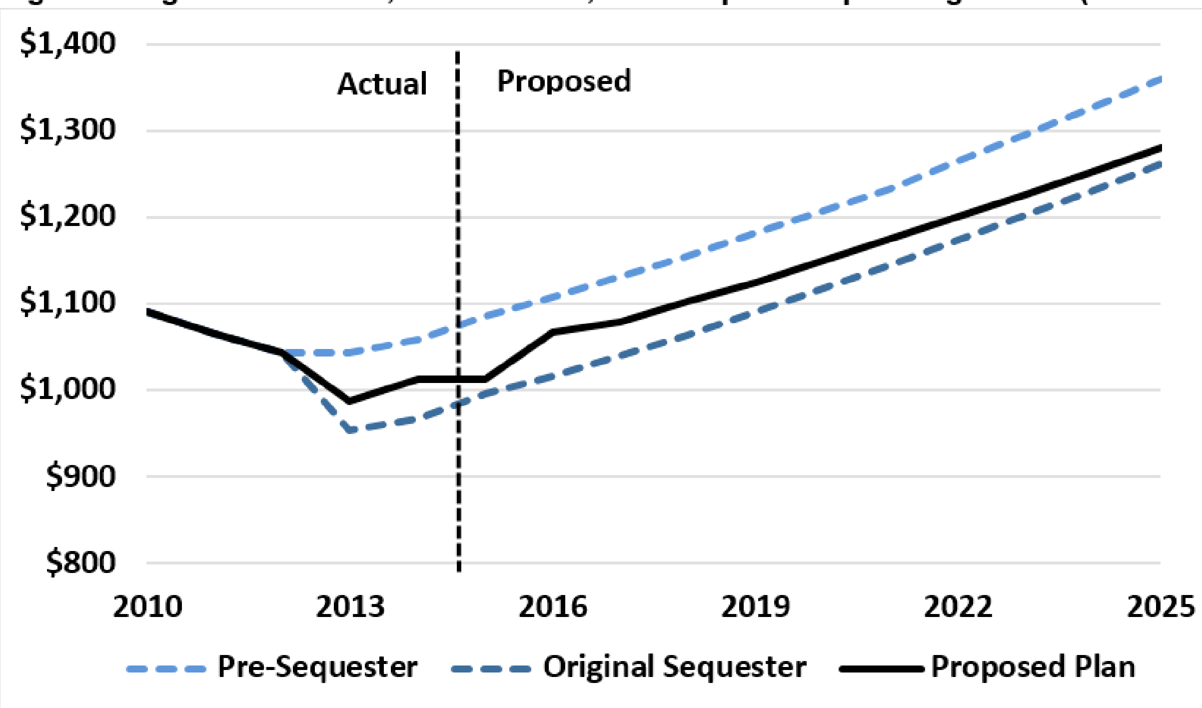
There is no one "correct" way that policymakers should modify discretionary spending caps, nor one set period of time for which sequester relief should occur (see Appendix A for options). From a budgetary standpoint, policymakers should raise caps enough so that appropriators can spend within the caps without gimmicks, but only as much as policymakers are willing to pay for.

For illustrative purposes, the SOS plan proposes to lift current sequester-level caps in two parts. First, it calls for repealing about half of the discretionary sequester cuts over the next two years, raising FY 2016 and FY 2017 caps to $1,067 billion and $1,080 billion, respectively. Next, it proposes extending the caps from expiring in 2021 through to 2025, indexing them to inflation (as measured by the chained CPI) beginning in FY 2018. As a result, discretionary spending would grow to $1.28 trillion by 2025.

2. Offset Two-Year Sequester Relief with Targeted Mandatory Savings and Receipts ($110 billion)

Reducing sequester cuts by half over the next two years will cost about $90 billion, and because of

Fig. 4: Budget Control Act, Current Law, and Proposed Spending Levels (Billions)



Source: CBO, OMB, House Budget Committee its front-loaded nature will require roughly $110 billion to offset when debt service is included. The Bipartisan Budget Act of 2013 ("Ryan-Murray") paid for two years of sequester relief with a mixture of mandatory spending reductions and receipts from user fees and other sources. Our plan would build on Ryan-Murray and include additional savings from the President's budget:

Build on Ryan-Murray Budget Deal ($50 billion):

» **Expand Ryan-Murray Federal Retirement Reforms.** Apply the Ryan-Murray retirement contribution increase for new federal workers to current workers as well *($20 billion)*

» **Expand Ryan-Murray PBGC Solvency Measures.** Allow the Pension Benefit Guaranty Corporation (PBGC) to further increase premiums to ensure solvency *($10 billion)*

» **Index Ryan-Murray User Fees to Inflation.** Allow customs fees and fees for airport security and other purposes from Ryan-Murray to grow with inflation *($10 billion)*

» **Replace Medicare Sequester.** Replace the portion of sequester that applies to Medicare – and is in effect through 2024 as a result of Ryan-Murray and subsequent legislation – with a *permanent* rebasement of Medicare payment levels to end the need for annual cuts, offer predictability to Medicare providers, and ensure permanent savings *($10 billion)*

Enact Targeted Mandatory Savings and Receipts from the President's Budget ($60 billion):

» **Increase Medicare Means-Testing.** Extend the freeze of the income thresholds for Medicare income-related premiums beyond 2019 *($15 billion)*

» **Enact Medicare Site-of-Service Payment Reforms.** Equalize Medicare payments for similar services furnished in different settings *($15 billion)*

» **Streamline Student Loan Income-Based Repayment (IBR) Rules.** Consolidate existing IBR program into a single, simple, well-targeted program *($15 billion)*

» **Reduce Farm Subsidies.** Reduce crop insurance premium subsidies *($10 billion)*

» **Enact Oil and Gas Revenue Reforms.** Make several changes to oil and gas revenue policies, including adjusting royalty rates and lease terms as well as re-prioritizing the Gulf state's revenue-sharing payments (*$5 billion)*

More information on these policies is available in Appendix B. Importantly, these represent just one set of possible offsets. Appendix C of this paper includes a table of additional options.

3. Offset Continued Sequester Relief by Adopting the Chained CPI ($210 billion)

Allowing discretionary caps to grow with inflation beyond FY 2017 from the increased levels will cost about $210 billion through 2025, as caps would remain above sequester levels through 2021 (when the current caps expire) and as a result be above CBO's baseline beyond that.

Permanent sequester relief is certainly desirable. However, it is also costly, and it is unlikely that lawmakers could identify a sufficient hodge-podge of targeted savings outside of the major entitlement programs and the tax code to offset these costs.

Therefore, we propose paying for longer-term sequester relief with a policy that has been a part of nearly every major budget discussion in recent years – the adoption of the chained Consumer Price Index (CPI) for measuring inflation throughout the budget and tax code. The chained CPI is widely regarded as a more accurate measure of inflation, which unlike the traditional CPI accounts for a problem known as upper-level substitution bias. This bias, along with a small-sample-size bias, leads the traditional measures of CPI to *overstate* inflation. Because so many provisions in the budget and tax code are linked to CPI, this overstatement leads to both over-spending and under-taxing relative to the intent of the law. (For a full discussion of chained CPI, see Measuring Up: The Case for the Chained CPI).

Adopting the chained CPI – which should be regarded as a technical improvement to ensure that spending programs and provisions in the tax code accurately keep pace with inflation rather than a spending cut or tax hike – would raise roughly $150 billion of revenue over the next decade and reduce projected spending (outside of Social Security) by $85 billion. We would dedicate about $25 billion of these savings to enhancing various benefits for low-income individuals, understanding that while chained CPI is the most accurate measure of inflation, it could result in some undesirable distributional consequences. On net, this would result in about $210 billion of savings.

The adoption of the chained CPI would also result in significant savings to the Social Security program, as annual cost of living adjustments (COLAs) are indexed to inflation. Rather than use these savings for sequester relief, we would dedicate them to strengthening the Social Security trust funds. In combination with a flat dollar bump-up in benefits for the oldest seniors, this change would yield about $125 billion of savings for the Social Security trust funds over the next decade and close one-seventh of the program's 75-year funding gap.

4. Strengthen Enforcement of Budget Caps

In the past and especially over the last couple of years, lawmakers have relied on gimmicks to circumvent the discretionary spending caps. Congress should acknowledge and offset the costs of increased spending instead of resorting to gimmicks that disguise the increase. While the Sequester Offset Solutions plan increases these budget caps, it also strengthens enforcement to demand Congress honestly abide by these higher caps.

Specifically, the plan focuses on three improvements to the current caps:

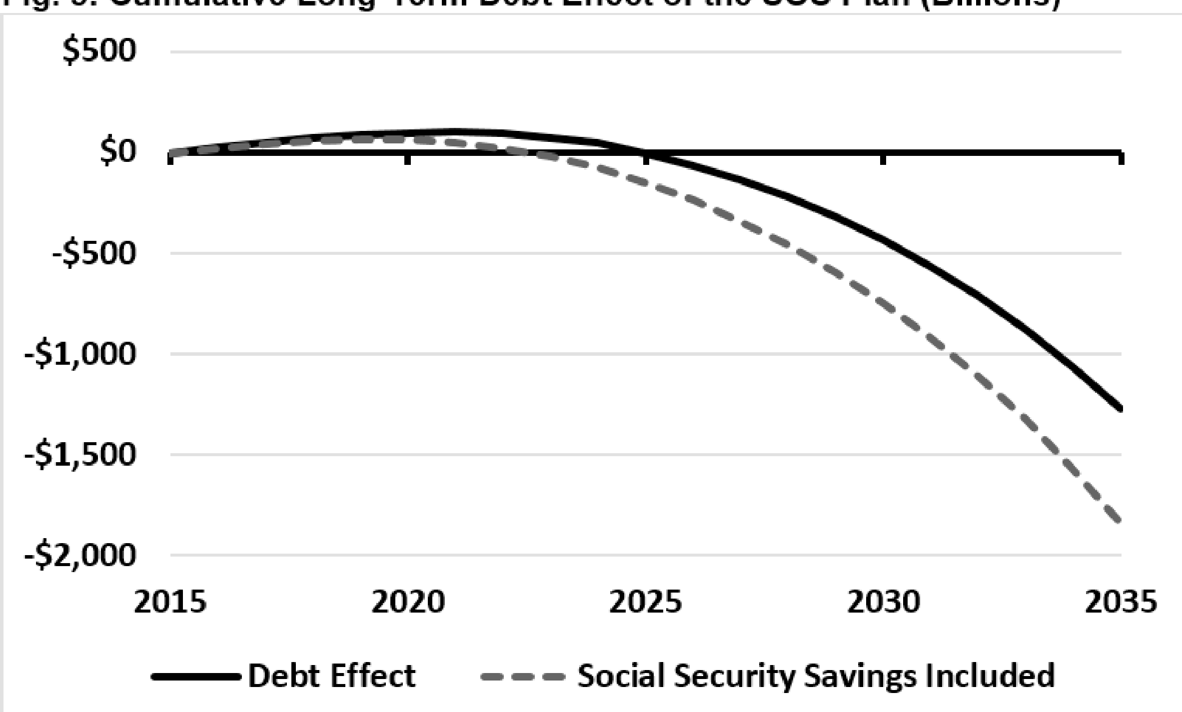
» **Limit OCO Spending.** Currently, overseas contingency operations (OCO) funding – a category meant for war spending – is not subject to budget caps. This exemption has allowed lawmakers in the past to shift a small amount of base defense spending to the OCO category to evade the defense caps. This year's budget resolution calls to expand this practice significantly, increasing OCO funding by $38 billion above the Pentagon's request. We propose limiting the amount of spending that can be designated as OCO spending to the request in the President's budget.

» **Codify Criteria for OCO Spending.** In addition to limiting the amount of OCO spending, we propose limiting which spending can be labeled as OCO and therefore exempt from the discretionary caps. Specifically, we would codify the existing criteria published by the Office of Management and Budget and prohibit OCO spending that does not meet these criteria.

» **Phase Out Misused CHIMPs and Other Phony Savings.** Currently, Congress is able to pay for discretionary spending increases with Changes in Mandatory Programs (CHIMPs) – even if those changes don't generate actual savings. In many cases, claimed CHIMP savings represent either reductions in budget authority that would not have been spent or one-year spending delays that produce savings in the first year while ignoring the costs in the second. We propose gradually phasing out this practice.

Additional information on these reforms is available in Appendix D.

Fig. 5: Cumulative Long-Term Debt Effect of the SOS Plan (Billions)



Source: CBO, OMB, CRFB calculations

Economic & Long-Term Budgetary Impact of the Sequester Offset Solutions Plan

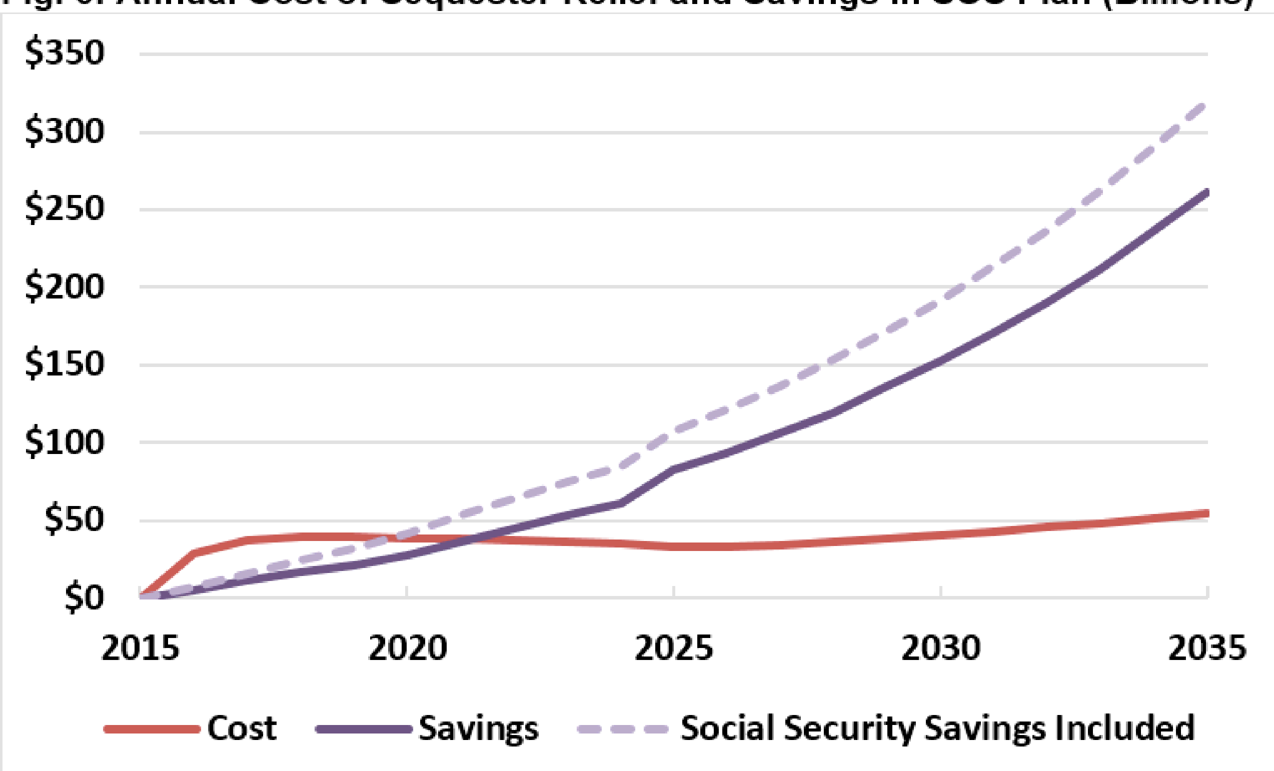
Although the Sequester Offset Solutions plan would be deficit-neutral over ten years, it would generate significant deficit and debt reduction over time. Over twenty years, the sequester relief would cost about $520 billion while the offsets would save closer to $1.7 trillion – leading to $1.2 trillion of primary savings. Including interest, these savings would total ***$1.3 trillion***, or ***$1.8 trillion i***ncluding the Social Security savings. Relative to the economy, debt in 2035 would be ***5 percent of GDP*** lower, even excluding the positive growth effects described below.

The large long-term savings stem from replacing mostly temporary and short-term cuts with permanent and growing savings. Sequester relief in our plan is quite front-loaded, reflecting the fact that the sequester itself saves the same nominal amount each year despite growing spending. Proposed offsets, on the other hand, continue to generate significant and growing savings well beyond the ten-year window. This is especially true for freezing the Medicare means-tested premium thresholds and adopting the chained CPI, both policies that compound rapidly over time.

Because the SOS plan reduces near-term cuts when the economy is weak but reduces the debt over the long-term, it would also be beneficial for both short-term and long-term economic growth.

By our estimates – based on those from the Congressional Budget Office – the fiscal impact of the plan alone would increase gross domestic product (GDP) by 0.2 percent in 2016 and by 0.3 percent by 2035. We would also expect additional growth effects as a result of replacing harsh cuts to the discretionary part of the budget – where most government investments are made – with targeted reforms in the rest of the budget.

Fig. 6: Annual Cost of Sequester Relief and Savings in SOS Plan (Billions)



Source: CBO, OMB, CRFB calculations

Conclusion

Lawmakers will have to decide on FY 2016 funding levels soon, and neither party appears content with the status quo. If lawmakers wish to increase spending above the levels set under the sequester, they should lift the caps and fully offset the cost. The upcoming deadline provides an opportunity to put in place responsible long-term deficit reduction achieving the original goal of the Budget Control Act, while setting a more reasonable and politically sustainable level of discretionary spending. This spending is already set to fall to a historic low as a share of the economy.

Appendix A: The Cost of Various Sequester Relief Options

The Sequester Offset Solutions plan provides $300 billion of front-loaded sequester relief, but there are countless paths that lawmakers could pursue, both in the level and timing of sequester relief.

For one, they could choose to repeal the across-the-board sequester on mandatory spending, which would cost $135 billion over ten years. Lawmakers so far, though, have gone in the opposite direction by extending that portion of the sequester an additional three years since its enactment.

There are also many different ways to do discretionary sequester relief. Like our plan, lawmakers could enact frontloaded sequester relief, but they could do it in different ways. The President replaced more than four-fifths of the sequester in the first two years and also had the relief decline over time. Indexing the FY 2015 cap to inflation would be frontloaded as well, but provide less relief than either our plan or the President's budget. Lawmakers could also provide roughly uniform sequester relief each year by repealing the entire discretionary sequester or a specific percentage each year.

The table below shows the cost for various sequester relief options and the ten-year cost of doing them for different periods of time.

Ten-Year Cost of Various Sequester Relief Options

	One-Year	Two-Year	Through 2021	Through 2025
Repeal Mandatory Sequester	$10 billion	$20 billion	$75 billion	$135 billion
Repeal Discretionary Sequester	$90 billion	$180 billion	$540 billion	$845 billion
Repeal Half of Discretionary Sequester	$45 billion	$90 billion	$270 billion	$425 billion
Repeal One Third of Discretionary Sequester	$30 billion	$60 billion	$180 billion	$280 billion
Index Current Caps to Inflation	$15 billion	$30 billion	$85 billion	$130 billion
Enact President's Discretionary Caps	$75 billion	$150 billion	$330 billion	$370 billion
Extend Ryan-Murray Sequester Relief	$20 billion	$35 billion	$110 billion	$170 billion

Source: CBO, CRFB calculations

Appendix B: Detailed Descriptions of Offsets in Sequester Offset Solutions Plan

Expand Ryan-Murray federal retirement reforms

Recent legislation raised the amount that federal employees must contribute to the Federal Employee Retirement System (FERS) by 1.3 percent of wages (from 3.1 to 4.4), but only applied those increases to newly-hired workers. The SOS plan would also increase the contribution of employees hired before 2014 by 1.3 percent of wages, increasing their contributions from 0.8 to 2.1 percent.

Expand Ryan-Murray PBGC solvency measures.

The Pension Benefit Guaranty Corporation (PBGC) insures the defined-benefit pension plans offered by private employers by stepping in to provide a minimum pension when those plans fail. The PBGC is financed by premiums that employers pay for the insurance, but the fund for multiemployer plans is expected to run dry in 2024. This policy would allow the PBGC to raise premiums to ensure its solvency and reflect the risks associated with each plan.

Index Ryan-Murray user fees to inflation

The federal government assesses a variety of user fees to fund operations for things like customs services, aviation security, and food and drug inspection. However, these fees are usually charged at fixed-dollar rates that are eroded by inflation over time. The plan would index all user fees to inflation.

Increase Medicare means-testing

Premiums for Medicare Parts B and D are roughly 25 and 25.5 percent of per-person costs, respectively, but beneficiaries with incomes above certain thresholds pay progressively higher premiums. Today, these higher premiums apply to about the top 6 percent of beneficiaries, which will naturally grow over time as the thresholds are indexed to inflation each year after 2019 (they are currently frozen until then).[1] This policy would continue the current freeze until one-quarter of beneficiaries are subject to the higher premiums.

Repeal Medicare sequester

The sequester enacted in 2011 makes across-the-board cuts to non-exempt mandatory spending and Medicare payments, with the Medicare cuts limited to 2 percent. The cuts originally were in effect through 2021 but were subsequently extended through 2024. This plan would replace the portion of the sequester that affects Medicare by permanently setting Medicare payments at post-sequester levels instead of having Medicare set payment rates only to be cut afterward.

Enact Medicare site-of-service payment reforms

Medicare often pays vastly different rates for similar health care services based on the setting in which they are performed. This policy would equalize these payments to reduce unnecessary disparities and to reduce incentives for hospitals to buy freestanding physician offices to claim higher rates.

Streamline student loan Income-Based Repayment rules

This provision would adopt the FY 2016 President's budget policy to consolidate repayment plans for new student loans under the Pay-As-You-Earn (PAYE) initiative and make several reforms of the PAYE program, including eliminating the standard payment cap under PAYE so that high-income, high-balance borrowers pay an equitable share of their earnings as their income rise, calculating payments for married

1 Juliette Cubanski and Tricia Neuman. "Medicare's Income-Related Premiums: A Data Note," Kaiser Family Foundation, June 2015.

borrowers filing separately on the combined household Adjusted Gross Income; and preventing payments made under non-income driven repayment plans from being applied toward Public Sector Loan Forgiveness program.

Reduce farm subsidies

The most recent farm bill enacted in early 2014 replaced direct payments for commodities with less costly coverage to insure farmers against drops in revenue. It also increased spending for crop insurance. Currently, crop insurance premiums are subsidized by having the federal government cover about 60 percent of the costs. This provision would adopt the FY 2016 President's budget proposal to reduce the premium subsidy by 10 percentage points.

Enact oil and gas revenue reforms

The President's budget includes several policies to reform oil and gas management and encourage development where leases are currently non-producing. These policies include adjusting royalty rates, repealing royalty exceptions, altering and more strictly enforcing lease terms, strengthening revenue collection, and redirecting revenue-sharing payments from offshore oil and gas leasing.

Appendix C: Other Options for Pay for Sequester Relief

The offsets used in the Sequester Offset Solutions plan are by no means the only ones available to policy-makers. The table below shows several other mandatory spending and revenue options, ranging from small policies to larger reforms, that could offset sequester relief.

Policy	Ten-Year Savings
Health Care	
Reform Medicare cost-sharing and restrict Medigap coverage	**$110 billion**
Bundle acute care and certain post-acute care Medicare payments	**$65 billion**
Phased out Medicaid provider tax threshold	**$65 billion**
Eliminate Medicare payments for bad debts	**$45 billion**
Encourage generic drugs by adjusting Medicare LIS co-pays	**$20 billion**
Extend 2018 1% post-acute care update into 2019	**$15 billion**
Limit Medicaid DME reimbursements to Medicare levels	**$5 billion**
Align employer group waiver plan payments with average Medicare Advantage plan bids	**$5 billion**
Revenue	
Limit value of certain tax expenditures to 35%	**$150 billion**
Replace Pease limitation with $250k/$500k cap on itemized deductions	**$110 billion**
Impose 30% minimum tax on millionaires ("Buffett Rule")	**$65 billion**
Provide IRS program integrity funding	**$40 billion**
Restrict inversions	**$5 to $40 billion**
Close "John Edwards/Newt Gingrich" loophole	**$10 to $25 billion**
Eliminate mortgage interest deduction for yachts and second homes	**$15 billion**
Close "carried interest" loophole	**$15 billion**
Repeal certain oil and gas tax preferences	**$10 billion**
Prevent abuse of deductions for corporate owned life Insurance	**$5 billion**
Require inherited pensions to be distributed over 5 years	**$5 billion**
Other	
Reduce interest rate yield on G-Fund in Thrift Savings Plan	**$30 billion**
Reduce Federal Reserve dividends to certain member banks from 6% to 1.5%	**$15 billion**
Sell from the Strategic Petroleum Reserve	**$5 to $10 billion**
Base military and civilian pensions on highest 5 earning years	**$5 billion**
Limit SSI benefits for children of large families and review mental health coverage	**$5 billion**
Repeal special depreciation for corporate jets	**$5 billion**

Source: CBO, JCT, CRFB calculations

Appendix D: Strengthening Enforcement of Budget Caps

More information on the three improvements to discretionary caps included in the Sequester Offset Solutions plan:

Limit Overseas Contingency Operations (OCO) Spending

Shifting normal defense spending into the OCO category, reserved for spending on the wars overseas, is an attractive method of clearing room for more spending under the caps without triggering budget enforcement. There is evidence that appropriators have shifted money on the margins in the past, and the FY 2016 Congressional budget resolution would expand that strategy dramatically by increasing OCO funding by $38 billion above the Pentagon's request.

To prevent this gaming, our plan would limit the amount of spending that can be designated as OCO spending to the request in the President's budget. This would better ensure that appropriators are not using the OCO category as a supplemental defense fund, but rather to fund actual war needs.

Codify Criteria for OCO Spending

While limiting OCO spending to the President's request would help close that gimmick, Congress might still choose to reduce funding below the requested levels if circumstances allow and instead use the extra money allowed below the new caps to backfill the base defense budget. To guard against that possibility, the plan would also codify criteria for what could qualify as OCO and require Congress and the President to certify annual OCO spending as meeting that criteria. The Office of Management and Budget has already published criteria as guidance for agency requests to have spending designated as OCO, but this can be codified to apply to those requests and appropriations bills. The combination of these criteria and the limit on spending should ensure that OCO does not become a slush fund.

Phase Out Misused CHIMPs and Other Phony Savings

Congress is able to appropriate spending above the caps offset by rescissions of budget authority that would not have been spent and through Changes in Mandatory Programs (CHIMPs). CHIMPs are changes in mandatory programs that are used to allow spending above the discretionary caps. Although this trade-off is perfectly fine in theory, it is mostly abused in practice by using CHIMPs with no savings or ones that simply shift spending into the next year. For example, in FY 2015, appropriators used about $20 billion of CHIMPs to boost discretionary spending, even though they saved less than $1 billion in reality. A simple way to prevent this gaming is to prohibit Congress from claiming savings from rescissions of budget authority that produce no actual outlay savings and phase out the use of CHIMPs that simply shift spending into the next year with no actual net savings, with a phase-out over ten years to give appropriators time to adjust. This policy would be similar to one in the FY 2016 Senate budget, which phased out fake CHIMPs over six years.