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Options for Budget Process Reform

Introduction

President Bush has proposed a FY 2005 budget that will permit less than 1-percent growth in non-defense, non-homeland-security discretionary spending. The President's budget also offers several proposals for budget process reform, designed to support the goal of cutting the deficit in half within five years.[1] These are worth careful consideration, especially in light of the declaration by the Office of Management Budget (OMB) that the projected FY 2004 deficit will exceed half a trillion dollars.

While a deficit is hardly unusual – federal spending policy has allowed outlays to exceed revenues 30 times during the past 34 years – fiscal conservatives want to reduce the deficit, and reduce it by way of reduced spending (as opposed to increased taxes). This paper describes several of the proposed budget process reforms offered by Senators, House Members, and the President, all designed to reduce the current budget deficit.

Background

The current deficit projections do raise concerns that should be addressed during this year's budget cycle, yet the situation should be viewed in proper perspective. The deficit is not projected to rise to the "out-of-control" level that critics would have the American public believe. These critics argue that the estimated deficit is the largest in history, which is correct when measured in current dollars[2]; however, as a percentage of gross domestic product (GDP) – a more appropriate standard – it is far from record levels. In fact, in 5 of the last 25 years, the percentage of the deficit relative to GDP exceeded the current level of 4.5 percent.[3] However, Federal Reserve Chairman Alan Greenspan recently warned that despite "impressive gains" in the economy, there is a long-term risk posed by rising federal budget deficits, a risk Congress should address.[4]

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[1] The Budget for Fiscal Year 2005, Historical Tables, Office of Management and Budget.
[2] Deficit arguments based on current-dollar figures arguably lack substance because they are not reflective of the figure's relevance to the overall economy.
[3] The Budget for Fiscal Year 2005, Historical Tables, Office of Management and Budget.
[4] *Congressional Quarterly*, "Greenspan Warns Deficits Pose Long-term Risk to Economy," February 11, 2004 (available at www.CQ.com.)

The Spending Problem

Last year, for the first time since the Second World War, federal outlays topped $20,000 per family (comparing inflation-adjusted dollars).[5] In 2003, mandatory spending reached its highest level in U.S. history. After remaining between $8,000 and $9,000 per household for most of the 1990s, mandatory spending surged to a record $11,144 per household in 2003, or the equivalent of 11 percent of GDP.[6]

While few would be surprised to learn that half of the spending increases since 1998 went to defense and Social Security spending, they might be surprised to learn that education, health programs, agriculture, and unemployment compensation have grown at higher rates.[7] Using inflation-adjusted dollars, since 1998: education spending has increased 78 percent, from $34 billion to $58 billion; National Institutes of Health spending has increased 81 percent, from $33 billion to $60 billion; agriculture spending has increased 76 percent to $23 billion.[8] While the above figures are not a comprehensive list of the astonishing increases that have occurred, they illustrate a congressional penchant for spending that needs restraining.

From 1998 to 2003, inflation-adjusted discretionary outlays jumped 36 percent, from $603 billion to $820 billion.[9] According to Heritage Foundation calculations, since 1998, discretionary spending on programs unrelated to defense and September 11th has increased 27 percent. This spending, combined with an economic "perfect storm" – which included the shocks of a stock-market bubble, a recession, the September 11th terrorist attacks, well-publicized corporate scandals, and the continued costs of the war on terror – contributed to the current projected deficit.

Specifically, the economic downturn was responsible for 49 percent of the current deficit.[10] Tax cuts are responsible for 27 percent; defense and homeland security spending is responsible for 13 percent; and non-defense, non-homeland-security spending is responsible for the remaining 11 percent.[11]

Even if Congress had not adopted any of President Bush's tax-relief proposals, the federal budget still would include a significant deficit. In fact, the tax policy changes enacted in 2001 and 2003 are responsible for less than one-third of the current budget

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[5] Federal outlays consist of the amount of money the federal government spends in a given fiscal year, and budget authority is the authority provided by law to incur financial obligations that will result in outlays. As such, outlays often include spending from budget authority beyond the previous fiscal year and even prior administrations.

[6] Brian M. Reidl, "$20,000 per Household: The Highest Level of Federal Spending since World War II," The Heritage Foundation, December 3, 2003 (available at www.Heritage.org).

[7] The year 1998 provides a good benchmark because it is arguably the beginning of the federal spending spree. Notably, 1998 was the first year the federal government registered a budget surplus since 1969.

[8] Reidl.

[9] Reidl (citing data provided by the Office of Management and Budget and the Congressional Budget Office).

[10] President Bush's 2005 Budget: A Brief Overview, U.S. Senate Budget Committee (February 2, 2004).

[11] President Bush's 2005 Budget: A Brief Overview, U.S. Senate Budget Committee (February 2, 2004).

deficit.[12] Moreover, those advocating the repeal of President Bush's tax cuts as a means of cutting the deficit should review historical statistics, which show that increasing taxes encourages more spending, and that action in turn only serves to increase the deficit.[13]

Budget Reform Options

How can Congress meet the President's goal of holding non-defense, non-homeland security discretionary spending to less than 1 percent? Congress in past years has turned to budget process reforms to help institute fiscal restraint.[14] Implementing such reforms this year would send an important message to the American people: Congress, like most Americans, will not spend more than it can afford.

The following is a brief catalogue of some of the major available budget process reforms:

1. Caps on Discretionary Spending

Under statutory discretionary spending caps that were in place from 1991 to 2002, the President was required to sequester funds that exceeded the statutorily defined cap.[15] More specifically, the President was required to issue an order for an across-the-board spending cut that would have reduced spending to the level permitted by the cap.

Since 1934, the federal government has run a surplus in only 12 years; however, 4 of the 12 surpluses occurred between FY91 and FY02. The significance of surpluses during this time period is that statutory spending caps were in place, which restricted discretionary spending. Unfortunately, on September 30, 2002, Congress allowed these caps to expire.

The President's FY05 budget proposes re-instituting discretionary spending caps for FY05-FY09. Under the President's proposal, all discretionary spending would come under one cap, except for a single, discretionary cap with separate "firewalls" that would be created for transportation programs.[16]

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[12] President Bush's 2005 Budget: A Brief Overview, U.S. Senate Budget Committee (February 2, 2004).
[13] Daniel J. Mitchell, "Spending Growth-Not Tax Cuts-Is The Reason for Fiscal Imbalance," February 12, 2004, (available at www.Heritage.org).
[14] The most recent examples include: P.L. 101-508, Budget Enforcement Act of 1990; P.L. 103-66, the Omnibus Budget Reconciliation Act of 1993; P.L. 105-33, the Balanced Enforcement Act of 1997.
[15] CBO defines "sequestration" as "the cancellation of budgetary resources available for a fiscal year in order to enforce the discretionary spending limits or pay-as-you-go procedures in that year." The Budget and Economic Outlook: Fiscal Years 2005 to 2014, Congressional Budget Office.
[16] A firewall prevents funds from being used for purposes that they were not intended. Thus, under the President's proposal, transportation "firewalls" would prevent funds for transportation from being used for non-transportation programs. Arguably, such a method limits the flexibility of appropriators, and forces them to fully fund the protected program.

2. Limit Spending to a Percent of GDP

Over the last 50 years, federal receipts have averaged about 18 percent of the GDP.[17] Over that same period, federal outlays have averaged about 20 percent of GDP.[18] If those trend lines continue, the federal government's current budget deficit will persist.

The OMB is projecting receipts to fall to 15.7 percent of GDP this year. While receipts are expected to grow close to the average level of 18 percent of GDP in the next five years, both the CBO and the OMB are projecting outlays to continue to exceed receipts. One way to affect this projected-deficit trend and achieve real deficit reduction is to tie federal outlays to a percentage of GDP that does not exceed the projected level of receipts as a percentage of GDP.[19]

Senator Gregg is working on legislation that would limit federal spending to 20 percent of GDP. An enforcement mechanism would be created whereby Congress itself would have two choices: 1) cut the baseline[20] for the upcoming fiscal year by whatever amount federal spending exceeded 20 percent for the most recently completed fiscal year; or 2) the President would be required to cut individual programs based on the size of the program relative to the overall federal budget after October 1, when the upcoming fiscal year becomes the current fiscal year. In addition, a budget point of order would be established in both the House and Senate against considering appropriations or reconciliation bills that fail to make the necessary cuts to bring spending under control. Finally, the mandated Presidential sequester could be waived by an "expedited" joint resolution; but it would take a two-thirds vote in each chamber to proceed to such a resolution once placed on either chamber's legislative calendar.

While the intent of such a proposal is a good one, one issue that may be of concern is that in tying spending to a percentage of GDP, Congress might be compelled to spend more money (in a year in which GDP was high) than it might otherwise have spent. Regardless, this proposal could provide a useful check on annual spending, and could help ensure that spending is in line with overall receipts and productivity.

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[17] Fiscal Year 2005 Budget of the U.S. Government, Historical Tables, Table 1.3, Office of Management and Budget.

[18] Fiscal Year 2005 Budget of the U.S. Government, Historical Tables, Table 1.3, Office of Management and Budget.

[19] Senators Kyl and Shelby have both previously introduced legislation linking spending to a percentage of GDP. In the 106th Congress, Senator Kyl introduced a joint resolution linking spending to 19 percent of GDP. *See* S.J.Res. 4. In both the 105th and 104th Congress, Senator Shelby introduced joint resolutions linking spending to 20 percent of GDP. *See* S.J.Res. 13 (105th), S.J.Res. 11 (104th).

[20] The baseline serves as "a benchmark for measuring the budgetary effects of proposed changes in the federal revenues or spending . . . .The baseline is the projection of current-year levels of new budget authority, outlays, revenues, and the surplus or deficit into the budget year and subsequent years. The Budget and Economic Outlook: Fiscal Years 2005 to 2014, Congressional Budget Office, p.148.

3. Pay-As-You-Go ("PAYGO")

In the past, PAYGO mechanisms required that new mandatory spending or revenues laws must not increase the deficit (or reduce surpluses).[21] PAYGO requirements were implemented through a recorded scorecard that generally worked as follows: OMB and CBO recorded the budgetary effects of mandatory spending and revenue laws over a 10-year period. At the end of each session of Congress, OMB would total the budgetary effects of all of the enacted laws on the scorecard. If the balance caused an increase in the deficit or a decrease in a surplus, then an automatic reduction in mandatory spending equal to the deficit increase or surplus decrease would be ordered through a process known as sequestration.[22] On September 30, 2002, statutory PAYGO expired.

While PAYGO was one means of reducing the deficit in the 1990s, it did not allow for much flexibility with revenue laws. Between 1991 and 1997, most mandatory spending and revenue laws met the budget-neutral requirements of PAYGO.[23] However, when surpluses began to appear in the late 1990s, Congress bypassed PAYGO requirements through legislative directives. These directives permitted PAYGO scorecard effects to be erased. As a result, spending legislation that should have been subject to a sequester was not sequestered. Consequently, PAYGO was more effective in preventing tax cuts than Congressional spending. And, with a number of expiring revenue provisions on the horizon, including the estate tax, the marriage penalty, and the child tax credit, traditional PAYGO could pose a roadblock to making these tax cuts permanent, which consequently could lead to a tax increase for many taxpayers.

4. Modified PAYGO

The President's budget has proposed a modified PAYGO requirement that would only apply to mandatory spending. Thus, revenue legislation would be exempt from this requirement. Under the President's proposal, the five-year budgetary effects of mandatory spending would be placed on a scorecard. Legislation that increases the deficit over a two-year period would trigger a sequestration of mandatory spending programs. Unlike the original PAYGO requirement, the President's proposal would provide a continuing obstacle to increasing the deficit through Congressional spending, while simultaneously providing Congress with the needed flexibility to extend expiring revenue provisions in order to prevent Americans from being saddled with a tax increase.

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[21] P.L. 101-508, Budget Enforcement Act of 1990; P.L. 103-66, the Omnibus Budget Reconciliation Act of 1993; P.L. 105-33, the Balanced Enforcement Act of 1997.
[22] *See Supra* note 13.
[23] The Budget and Economic Outlook: Fiscal Years 2004 to 2013, Congressional Budget Office, Appendix A.

Other Issues Relevant to Budget Process Reform

Beyond the budget process reforms discussed above, Congress should also consider reform in other areas that impact deficit reduction.

1. Long-term Unfunded Obligations

Fiscal conservatives recognize the large and dire problems associated with the long-term impacts of entitlement programs, including Social Security, Medicare, federal civilian and military retirement, veterans' disability compensation, and Supplemental Security Income. Most observers now know that the Social Security Trust Fund is projected to begin running deficits in just 15 years. While long-range projections are always unreliable, it is clear (even before Greenspan's comments before the House Budget Committee on February 25) that Social Security's current spending path cannot be sustained.[24]

This looming shadow is not limited to Social Security; as another impending example, the portion of Medicare's trust fund dedicated to "hospital insurance," (which covers expenses related to hospitalization) is slated to begin running a deficit in 2012 and to be depleted by 2026.

The President's budget would prevent the enactment of legislation that would worsen the long-term unfunded obligation of federal entitlement programs. The President proposes two mechanisms to prevent such legislation: 1) legislative points of order against bills that increase long-term unfunded obligations; and 2) new reporting requirements that highlight such increases.

2. Emergency Spending

A disturbing trend in Congress has emerged in which appropriations designated as "emergency" for budgetary purposes are no longer strictly limited to emergencies. Notably, the Budget Enforcement Act ("BEA"), which was in effect from 1991 to 2002,[25] placed caps on discretionary spending with exemptions designated for "emergencies." Thus, under the BEA, if spending were designated as an "emergency" by both the President and Congress, it would not trigger a sequester because the caps would be adjusted automatically by an amount equal to the emergency spending.

This exemption on emergency spending increased such spending to unprecedented levels: in 1999 and 2000, emergency appropriations totaled $34 billion and $44 billion, respectively, whereas from 1993 through 1998, total emergency appropriations amounted to $36 billion.

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[24] Social Security and Medicare Trustees include 75-year calculations of actuarial imbalance for their respective programs.

[25] The caps expired on September 30, 2002.

In addition to adding to the deficit, current use of emergency appropriations can confuse future budget projections. For instance, the CBO and the OMB took opposing views about whether to include emergency supplemental spending of $87.5 billion for operations in Iraq in future budget baselines. CBO included the funding in its baseline, while OMB did not.[26] OMB argues that it is unrealistic to plan for $87.5 billion in annual spending in Iraq. While this assumption is likely valid, there will be some spending in Iraq in the coming years. Examples such as the Iraq supplemental illustrate that the more spending done through emergency appropriations, the cloudier future budget projections will be. Potential solutions to combat this problem include a strict, statutory definition of "emergency" or a separate, statutory cap on emergency spending.

3. Advance Appropriations

An advance appropriation is an appropriation of new budget authority for a future fiscal year. As with "emergency" appropriations, advance appropriations have been used to circumvent discretionary caps on spending. The President's budget describes the problem: "Too often, advance appropriations have been used to expand spending levels by shifting budget authority from the budget year into the subsequent year and appropriating the [budget authority] freed up under the budget year discretionary cap to other programs."[27]

From 1993 to 1999, the average yearly total for advance appropriations was $2.3 billion in discretionary budget authority.[28] However, in 1999, the advance appropriations total jumped to $8.9 billion, and reached $23.4 billion in 2000.[29]

The President's budget proposes that any advance appropriation in fiscal years 2005 through 2009 that exceeds the level of advance appropriations for 2002 count against that fiscal year's budget authority for purposes of the discretionary caps. The practical effect of this proposal would be to freeze emergency appropriations at the 2002 level. Since advance appropriations are another form of discretionary spending, advance appropriations spending levels should be frozen to prevent overspending in the future.[30]

4. Line-Item Veto

In 1996, Congress enacted a line-item veto law, which became effective on January 1, 1997. However, in *Clinton v. City of New York*, the Supreme Court held the law to be unconstitutional under the Presentment Clause.[31] This year,

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[26] It is necessary to point out that OMB uses two baselines: The statutory baseline does include emergency spending, but the adjusted baseline does not.
[27] *Id*. at p. 216-217.
[28] Fiscal Year 2005 Budget of the U.S. Government, Analytical Perspectives (p. 216), Office of Management and Budget.
[29] Fiscal Year 2005 Budget of the U.S. Government, Analytical Perspectives (p. 216), Office of Management and Budget.
[30] The 2002 level is a good baseline because it precedes U.S. operations in Iraq, thus making it a more realistic number for future spending.
[31] *William J. Clinton v. City of New York*, 524 U.S. 417, 118 S.Ct. 2091 (1998).

however, the President's budget proposes a new line-item veto, which the OMB claims will meet constitutional requirements that the previous law did not.[32]

Beyond the constitutionality of such a proposal, a line-item veto could be an effective mechanism for eliminating provisions in spending and revenue bills that benefit only a select few. Because a line-item veto has the ability to eliminate provisions that are especially troublesome and inconsistent with proper stewardship of public dollars, it remains a budget process reform worth consideration if it can pass constitutional muster.

5. Biennial Budgeting

Biennial budgeting could provide a remedy to a current Congressional budget and appropriations process that rarely meets its statutory deadlines. In fact, only three times[33] in the last 50 years has Congress passed all of the appropriations bills on time.[34] Moreover, proponents of biennial budgeting argue because Congress must produce these bills annually, it cannot provide the proper oversight each program requires. The President's budget argues that "the preoccupation with these annual appropriations bills frequently precludes review and action on the growing portion of the budget that is permanently funded under entitlement law." [35] Illustrating this point, CBO estimates that in recent years, unauthorized appropriations have ranged from $90 billion to $120 billion.[36]

Biennial budgeting, however, may not be without drawbacks. First, given the possibility of a catastrophic terrorist event, Congress must be able to quickly respond. Should such an event occur in a non-budget year, the hands of Congress would be tied to the extent it could not act through the emergency appropriations process. However, a well-defined provision, which provided for spending increases in response to a catastrophe, could solve this problem. Second, were Congress to provide a budget only every other year, it arguably would affect its power in terms of the checks and balances among the three branches of government.[37]

6. Family Budget Protection Act

H.R. 3358, the Family Budget Protection Act, introduced in the House by Representatives Hensarling (R-TX), Ryan (R-WI), Chocola (R-IN), and Cox (R-CA)

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[32] As of press time, OMB had not supplied Congress with the legislative proposal that would back up its constitutional claim.
[33] Fiscal Years: 1997, 1989, and 1995.
[34] Fiscal Year 2005 Budget of the U.S. Government, Analytical Perspectives (p. 218), Office of Management and Budget.
[35] Fiscal Year 2005 Budget of the U.S. Government, Analytical Perspectives (p. 218), Office of Management and Budget.
[36] Fiscal Year 2005 Budget of the U.S. Government, Analytical Perspectives (p. 218), Office of Management and Budget.
[37] The Budget and Economic Outlook: Fiscal Years 2004 to 2013, Appendix A, Congressional Budget Office.

would drastically reform the current budget process: it includes caps on both mandatory and discretionary spending. Specifically, H.R. 3358 replaces the 20 functions that currently make up the budget with four broad spending categories – mandatory spending, non-defense discretionary spending, defense discretionary spending, and a new "rainy day" fund for emergencies. Each spending category would contain a cap. In addition, this bill: 1) converts the concurrent budget resolution into a joint resolution that is signed by the President and has the force of law; 2) provides government shutdown protection by instituting an automatic continuing resolution when appropriations bills are not passed before the next fiscal year begins (October 1); and 3) eliminates baseline budgeting by using real dollars to compare the prior year's actual spending with proposed new spending – thus, eliminating the ability of critics to call scaled-back increases a "cut."[38]

Conclusion

While budget process reform alone will not eliminate the current budget deficit, such tools as described in this paper may help Congress reduce and control it. The climate is ripe for the implementation of budget process reform. After all, it is Congress' constitutional responsibility to deal with spending issues.

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[38] The description of H.R. 3358 is based on the summary provided by Representatives Hensarling, Ryan, and Chocola in their February 10, 2004 summary of the bill.