THE BUDGET PROCESS

Statement of

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It is tempting to believe that if only we could come up with some clever budget rules, fiscal prudence would follow. Unfortunately, it does not work that way. The desire for fiscal responsibility must come first. Then rules can be important in strengthening the efforts of those supporting fiscally responsible policies. They also can protect those who are fiscally responsible from the special interests that will inevitably oppose them.

The problem in recent years has not been a lack of rules. It has instead been the failure of the Congress to follow rules that are already on the books. The Senate has not passed a normal budget in 2 years (The caps imposed by the Budget Control Act of 2011 have recently been deemed to constitute a budget.) and last year the House failed to pass a budget for the first time in the history of the modern budget process. It is hard to think up useful rules governing the development of a budget resolution when no budget resolution passes the entire Congress.

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[1] The views expressed are those of the author and should not be attributed to the Urban Institute, its trustees, or its funders.

The Congress almost never passes appropriations on time. That makes it very difficult for the bureaucracy to make rational plans.

Rules versus Changes in the Structure of Programs

The difficulty in following rules and schedules may imply that it is more promising to think about changes in the structure of spending programs or in the tax structure that would make deficits easier to control. It is Social Security and health spending that now create our biggest budget challenges. The two areas constitute almost half of noninterest spending. Both areas are growing faster than tax revenues.

Part of the problem is that Social Security, Medicare and Medicaid, along with some less important health programs, are open-ended. That is to say, they are not subjected to a budget. The law defines an eligible population and the benefits to which they are entitled and then we pay for everyone who shows up. A lot more people are showing up these days as baby boomers retire in larger and larger numbers.

My colleague Eugene Steuerle and I have written about automatic triggers that might be used to make Social Security more secure financially.[2] Upon a finding by the actuary that the program is in trouble, the spending and/or tax structure could be altered automatically to put the program on a more sustainable course. For example, the full retirement age could be increased automatically, indexing could be changed to reduce benefit growth, or the tax base could be raised. Sweden has designed a system in which the generosity of the index applied to new and future retirees is automatically made less generous whenever the present value of future revenues falls short of the present value of future expenditures.

Steuerle and I also wrote favorably regarding the automatic Medicare trigger that was embedded in the Prescription Drug Act. Upon a finding that indicated that the system was in financial trouble, the president was to issue recommendations that would improve the program's financial outlook, and the Congress was supposed to consider the recommendations in an expedited manner. The actuary found that the system was in trouble; President Bush made some money saving recommendations; and then nothing happened. The Congress passed a new rule that relieved them of the burden of considering the

[2] Rudolph G. Penner and C. Eugene Steuerle, "*Stabilizing Future Fiscal Policy: It's Time to Pull the Trigger*," an Urban Institute Research Report, August 2007.

recommendations. The experience shows that nothing is foolproof. The Congress can create laws and change laws at any time.

Medicare can be put on a budget through a premium support approach and Medicaid can be controlled through a block grant, as suggested in the budget you put forward Mr. Chairman and in the Domenici-Rivlin report.[3] The amount of money that should be put behind these ideas can be debated, but once the debate is resolved Congress has a more direct way of controlling total expenditures.

On the revenue side, a revenue neutral tax reform that broadens the tax base and lowers marginal rates can be designed to provide a revenue stream that grows faster than GDP in the long run. Such a system was designed by a committee that I co-chaired for the National Academies of Science and Public Administration.[4] Admittedly, the revenue growth was largely fueled by the elimination of the exclusion from taxable income of the cost of employer provided health insurance. The exclusion is currently a major drag on revenue growth because of rapidly growing health costs. However, we designed our system before health reform passed. Now one has to worry that the removal of the exclusion would drive many more people into subsidized exchanges.

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[3] Debt Reduction Task Force 2010, "*Restoring America's Future: Reviving the Economy, Cutting Spending and Debt, and Creating a Simple Pro-Growth Tax System",* Washington, DC, Bipartisan Policy Center.
[4] Committee on the Fiscal Future of the United States (National Academy of Public Administration and National Research Council of the National Academy of Sciences, 2010, "*Choosing the Nation's Fiscal Future",* Washington, DC, National Academies Press.

Proposals for Changing the Budget Process

There are some proposals for changing the budget process that I oppose, some that should be adopted, and others that deserve more study.

A Joint Resolution -- It has often been suggested that the Congress pass a Joint Budget Resolution that would replace the Concurrent Budget Resolution called for in present law. A Joint Resolution is a law that would be signed or vetoed by the president. A Concurrent Resolution is not a law and is not signed by the president. Proponents of this change argue that it would be useful for the president and the Congress to agree to a budget early thus avoiding time consuming debates later in the year. Because it would have the force of law, the budget resolution should be easier to enforce.

I must confess that I was for a Joint Resolution before I was against it. I now believe that it would be impractical to reach an agreement between the president and the two houses of Congress early in the year. As noted earlier the Congress has had problems reaching an agreement itself. Finding an agreement with the president would probably involve a protracted bargaining session that would take far too much time.

A few years ago, then Chairman Nussle and Representative Cardin put forward a proposal for a Joint Resolution that had a fallback provision. If the president and the Congress did not reach agreement within a specified time period, the Congress would then revert to a Concurrent Resolution. This would be a better approach than not having a fallback, but I suspect it would be necessary to revert to a Concurrent Resolution almost every year.

Biennial Budgeting – Many have suggested that the Congress prepare a budget only every two years, thus leaving more time for oversight of programs. I have never liked this idea. I see budgeting as an iterative process in which we are constantly groping for a better allocation of resources. It is an extremely complicated process that we never get quite right and it useful to return to the problem at least once a year. I would say that even if conditions remained constant, but they don't. There tend to be significant unpredicted changes in the economy each year and budget projections can vary dramatically. One might diminish the problem by relying more on supplementals, but supplementals tend to be hard to discipline. Besides, what if political conditions suddenly favored some budget consolidation, but it happened in an off year. One might miss an important opportunity.

A Balanced Budget Amendment – Forty nine states have laws or constitutional provisions that favor a balanced budget. They vary greatly from state to state. Some only require that balanced budgets be proposed and some only require that budget for current operations be balanced and allow borrowing for capital projects.

Such laws have greatly distorted state budgets. First, they have driven many state activities off budget. There are more than 30,000 independent agencies and off-budget accounts at the state and local level that are not subjected to a balanced budget requirement. Second, they promote the use of accounting gimmicks as a first response when states get into trouble. For both reasons state budget become very hard to understand.

It is true that governments eventually run out of gimmicks in a severe recession and balanced budget rules start to have a real restraining effect, but it is not a good time for restraint. Over the longer run the main restraint on states comes from the rating agencies whose rulings can have a significant impact on the interest rates on state debt. In my view, balanced budget rules only have a sporadic restraining effect that generally comes at just the wrong time.

A balanced budget amendment would reduce the ability of the Federal government to respond to recessions and other emergencies. If exceptions are put in the amendment, they will almost certainly be abused. It was not so long ago that the Congress declared the 2000 census to be an emergency, even though we knew that we had to have one since 1789.

Lengthening the Budget Time Horizon – The Committee for a Responsible Federal Budget has proposed a series of process changes that would take a longer term view of the budget.[5] Most important the Congress would set a target at which it would stabilize the debt-GDP ratio and announce the year in which the target would be achieved. It sets out a number of enforcement mechanisms with an automatic sequester as a last resort.

Choosing a New Baseline – The current law baseline now used by the Congress in budget deliberations has become almost totally useless. The problem arises because of Congress' propensity to pass deficit increasing measures for short time periods. Consequently, all the Bush tax cuts are now scheduled to expire at the end of 2012, including those for the middle class; it is assumed the alternative minimum tax will soon afflict millions more taxpayers; numerous other tax provisions that are routinely renewed every year are assumed to expire; and Medicare reimbursements will be cut to the bone. These unrealistic assumptions lead to unrealistically rosy deficit projections.

[5] Committee for a Responsible Federal Budget, *Getting Back in the Black, November 2010.*

This is not an easy problem to fix, because there is no such thing as a perfect baseline. However, I believe that it would be more sensible to have a new baseline that assumed that all temporary tax measures are renewed. On the spending side of the baseline, it is now assumed that authorizations for programs, such as TANF, highways, etc., are automatically renewed when necessary. The most important problem with my approach is that it does not take account of instances where the Congress truly wants a tax or spending measure to be temporary, but this is rare. My proposed baseline has the major advantage that it is much better predictor of where policy and deficits are going than the current law baseline.

A Joint Budget Committee – It has often been suggested that the House and Senate combine to form a Joint Budget Committee. The same resolution would be put before each house of the Congress and even if the resolution was successfully amended, the end results should be easier to reconcile than if you start with two different resolutions from two separate committees.

I am not absolutely convinced that this proposal is a good idea. I would defer to those with actual legislative experience who are in a better position to judge, but I do think it worthy of consideration.