Fixing the Budget Process

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Once we have a plan in place that reduces spending and increases revenues, a strong annual budget process for the government would help us stay on track. During the 1990s, tough budget controls combined with a growing economy to help improve the budget's bottom line. In 1990, when the first controls went in place, the federal deficit was $269 billion, or almost 4 percent of the economy. By 2000, our country was experiencing a surplus of $236 billion, or more than 2 percent of the economy. These controls expired, however, in 2002 while the economy was recovering from a recession and the country was engaged in a new fight against terrorism, all of which made many lawmakers reluctant to re-impose the budget controls. The budget situation in Washington has been out of balance ever since.

The current budget process is an annual process—and the attention of policy makers is focused on the next year even though many of their decisions will affect budgets for years to come. As a result, lawmakers are not required to consider the impact of their current budget decisions on future generations.

Although budget process changes cannot, by themselves, solve our long-term fiscal challenges, a better process could encourage policy makers to adopt a longer perspective and "lock-in" whatever multi-year savings decisions they make. Lawmakers would always be able to vote to change the budget process and relax any discipline it imposes, but a stronger process would create a high enough hurdle to make budget enforcement measures worthwhile.

There are various policy tools that would help reinforce fiscal discipline and maintain budget balance. These so called "budget controls" have been effective in the past. For example, adopting "pay-as-you-go" rules would require that any entitlement spending increases or tax cuts must be "paid for" before they are adopted. In addition, setting "caps" would limit annually appropriated spending, and adopting long-term budget goals would limit future deficit or debt levels.

Budget process reforms would be one part of what would be a multi-pronged plan to reduce the budget's long-term, structural imbalances. Policymakers could reinstate the budget controls that were effective in the past, set and adhere to longer-term budget goals, and establish a ceiling for the total amount of the national debt. These types of budget controls, when used in concert with other broad packages of fiscal restraint, could effectively help elected officials stay on the path toward fiscal health.

Policy options:

Re-impose statutory caps on discretionary spending

Spending caps would put a limit on spending, and are most often associated with discretionary (as opposed to mandatory) spending. Policy makers set discretionary spending levels each year during the appropriations process to fund many of the most visible activities and programs of the federal government, including national parks, transportation programs, the Congress and the White House. Discretionary spending caps were effectively used in the 1990s under both Presidents George H.W. Bush and Bill Clinton.

Many budget experts argue in favor of new statutory caps on discretionary spending to help to ensure that spending levels are limited. . If discretionary spending were to exceed the cap, then an across-the-board cut (or sequestration) would be made in that spending category. Discretionary spending takes up about one-third of the federal budget, so an enforceable cap would be an effective tool in stemming growth in spending. Lawmakers could vote to change the caps should new priorities emerge, emergencies arise, or national conditions change.

Tougher pay-as-you-go budget rules

A pay-as-you-go (often referred to as PAYGO) rule would apply to entitlements and other mandatory programs. PAYGO would require that the spending resulting from new or expanded mandatory spending be paid for either with new revenue increases or new mandatory spending cuts. Similarly, changes to existing laws to cut taxes would need to be offset with revenue increases or mandatory spending cuts. PAYGO rules generally apply for as many years as the new spending increase or revenue reduction would last—up to the full 10-year period used by Congress for projections. A temporary, or one-year tax cut, for example, would have to be offset for that one year only, while a permanent expansion of eligibility for an entitlement program or tax cut would have to be offset over the next 10 years. If all of the changes enacted during the year to mandatory spending or revenues were not sufficiently offset, an across-the board reduction would be applied to mandatory spending programs to correct the shortfall. PAYGO would not apply to changes in spending or revenues that result from unanticipated economic or other factors. For example, PAYGO would not apply if rising unemployment led to more benefit claims, but it would apply if the Congress and President enacted a law to raise the benefit levels or make them available for a longer period of time.

The Congress and the President recently enacted a form of PAYGO. This new law, however, exempted many costly policy changes, including extension of the 2001 and 2003 tax cuts for all but higher-income taxpayers and upward adjustments to Medicare payments to physicians.

Many budget experts propose a strict PAYGO rule that would apply to all changes to current law affecting entitlement and mandatory programs and revenues. Others argue in favor of PAYGO that would apply only to proposed spending changes. However, exempting tax changes from PAGYO might encourage lawmakers to rely more on tax expenditures to extend benefits, and a broader PAYGO would be more likely to promote fiscal restraint than one that exempts only certain types of changes, either to revenue or spending laws.

Design and apply budget “triggers” as a method of enforcement

Budget “triggers” are another option that has been proposed by some budget experts to constrain the growth of mandatory spending, which currently makes up nearly two-thirds of our budget. The vast majority of mandatory spending goes to three of the government’s largest programs: Social Security, Medicare, and Medicaid. These programs are particularly vulnerable to growth as a result of increased longevity, population shifts, and the rapid rise in health care costs. Since mandatory spending, unlike discretionary spending, does not require annual review or depend on new funding each year, a trigger would encourage lawmakers to take notice when mandatory programs are projected to cost more than anticipated by Congress and the President in their most recent budget decisions.

Whether the trigger prompted a “hard” action (legislation that would reduce spending automatically unless Congress and the President step in to stop it), or a “soft” action (the publication of a report warning that the budget limit is expected to be breached), it would require lawmakers to review and reconsider the status of mandatory spending programs.

A few experts argue that revenue triggers would also be possible. Revenue triggers would be designed to encourage reconsideration of tax changes, but because it is more difficult to gather information about how much revenue was lost as a result of a tax cut, they would be much harder to design.

Set sustainable debt targets

As its name suggests, a debt target would be an explicit ceiling of the nation's publicly held debt. Debt targets are generally expressed as a percent of the country's gross domestic product, or GDP. Currently, Congress and the President have some control over the national debt: they must pass legislation periodically to increase the nation's debt ceiling. While it does demand regular attention to our debt levels, this method restricts that consideration to very short-term demands.

Many fiscal experts have proposed debt targets. Whatever the debt limit, the aim is to choose a target that can accommodate a sustainable fiscal plan. The European Monetary Union has set the goal of 60 percent of GDP as part of the admission requirements for its member countries. That level reflected a view that the 60 percent ceiling would be feasible to achieve and that carrying debts above that level would increases risk to a country's economy. However, by itself, a debt limit would be ineffective. It would depend on a comprehensive and detailed fiscal plan in order to be effective.

Learn More:
PGPF BUDGET PROCESS PRIMER

Taking Back Our Fiscal Future (by members of a Fiscal Seminar sponsored by the Brookings Institution and the Heritage Foundation: April 2008)
Mandatory Spending: Using Budget Triggers to Constrain Growth (The Government Accountability Office, January 2006)
Red Ink Rising (The Peterson-Pew Commission on Budget Reform: December 2009)
A Path to Balance: A Strategy for Realigning the Federal Budget (The Center for American Progress: December 2009)
Fiscal Rules—Anchoring Expectations for Sustainable Public Finances (The International Monetary Fund: December 2009)
The Right Target: Stabilize the Federal Debt (The Center for Budget and Policy Priorities: January 2010)
Choosing the Nation's Fiscal Future (The National Academy of Public Administration and the National Research Council of the National Academy of Sciences: January 2010)
