Peter G. Peterson Foundation
Our America. Our Future.

2013 Fall Fiscal Agenda

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In recent years, the fiscal policymaking process in the United States has broken down. Rather than passing an actual budget, the government instead lurches from crisis to crisis, with battles over continuing resolutions, debt limits, fiscal cliffs, and sequesters. These partisan fights not only harm the economy and damage the credibility of the U.S., but they also prevent meaningful progress on the critical fiscal challenges that we face.

Unfortunately, the final months of 2013 appear to be more of the same. Members of the House and Senate returned from August break to a full slate of decisions and deadlines. In many cases, there's not much time to act, yet the stakes are high. Whether it's 2014 appropriations, the debt ceiling, dealing with the threat of sequestration, or tackling tax reform, there's no shortage of critical issues that affect our fiscal future.

While these are individual challenges, they are also part of a larger narrative with serious implications for our nation's economy and fiscal health. Rather than governing by crisis — or trying to score political points — Congress and the President should seek a comprehensive bipartisan framework to protect the economic recovery and stabilize our debt for the long term.

In this report, we take a look at key upcoming milestones, examining how each fits into the larger fiscal picture.

THE 2014 APPROPRIATIONS BILL

DEADLINE: September 30, 2013

The most immediate challenge that Congress faces is coming to an agreement to keep the government running. September 30th marks the end of the fiscal year, so Congress only has a few days left to find a compromise on how much agencies can spend in fiscal year 2014.

Unfortunately, they have their work cut out for them. Even putting aside the highly controversial matter of "defunding Obamacare," none of the 12 appropriations bills have been brought to conference or enacted, and the two chambers are approximately $85 billion apart, with the Senate nearly 8% above the House level. One reason the gap is so large is the failure of the House and Senate to reconcile their two budgets by passing a concurrent budget earlier in the year, which would have provided guidance for the appropriations committees.

If Congress cannot close the gap, it risks a government shutdown on October 1. Without funding, all federal personnel except those engaged in protection of life or property will be furloughed, and those "essential" personnel — including soldiers in Afghanistan — will get IOUs instead of paychecks. Additionally, the services provided by many federal agencies will be sharply curtailed. For example, National Parks will be closed, drug approvals will be halted, and passport processing will be stopped. Although Social Security and Medicare benefits will continue, there may not be enough staff to help beneficiaries with administrative matters.

A likely (but far from certain) result is a short-term Continuing Resolution that funds the government for a temporary period, again delaying the difficult decisions until later this fall.

This crisis-driven process about the basic functioning of government raises uncertainty about the future, makes it more difficult for businesses to plan, undermines confidence in government, and reduces the efficiency of government programs. An actual shutdown would have more direct consequences for the economy and the efficiency of government operations.

THE DEBT CEILING

DEADLINE: October 17, 2013 (Treasury estimate)

The Treasury Department actually reached the current statutory limit on the amount of debt it can issue — the "debt ceiling" — on May 19, 2013. Since then, it has been using "extraordinary measures," such as redeeming securities in federal employee retirement and other funds, to allow it to raise enough cash to pay the government's bills.

By October 17th, Treasury estimates that these extraordinary measures will run out and we'll either have to raise the ceiling, or default on some of our obligations. Contrary to some misperceptions, the debt ceiling doesn't directly affect government spending decisions, it only prevents the Treasury from issuing the debt necessary to pay obligations that have already been incurred through existing policy and legislation. Historically, raising the debt ceiling has been relatively easy, but lately it's become a more controversial act.

Failing to reach agreement to raise the debt ceiling would be very dangerous. While the government has shut down previously (most recently in 1995), failing to raise the debt ceiling would be uncharted territory. Given the importance of U.S. Treasuries and the U.S. dollar to world financial markets, the result could set off a catastrophic reaction, damaging markets and the global economy. Unemployment could spike and the economy could tumble into a deep recession. And it's unclear how the government would even function. As opposed to a shutdown, which simply suspends certain non-essential operations of government, a failure to raise the debt ceiling would make the government unable to pay many of its actual obligations.

The Bipartisan Policy Center estimates that if the Treasury exhausts its extraordinary measures on October 17, we would be short about $106 billion over the following 4 weeks and unable to pay about 32 percent of our bills. In that scenario, major unanswered questions include which bills would get paid, which would not, and how that would be determined. And assuming an eventual resolution, it's unknown what the permanent damage would be, such as an ongoing increase in borrowing costs for the federal government and businesses and individuals.

Putting ourselves in a position like this would be an unnecessary, self-inflicted wound to an already fragile economy. Stating the obvious, our nation would be better served if it would utilize an orderly process to make the actual decisions needed to put our fiscal house in order. The nation needs a comprehensive, bipartisan fiscal plan that stabilizes the debt for the long term.

SEQUESTRATION OF DISCRETIONARY PROGRAMS

DEADLINE: Estimated January 2014

The Budget Control Act of 2011 created the Congressional "Super Committee" process, which failed to find the required additional $1.5 trillion in budget savings over 10 years. As a result, the fallback option was triggered, achieving deficit reduction by imposing a sequester of 2013 discretionary spending and lowering caps through 2021 on future discretionary spending.

In 2013, half of the sequestration cuts came from defense. Most of the remaining cuts came from non-defense discretionary spending programs — including scientific and medical research, education, national parks, food inspections, law enforcement, federal employee pay, grants to state and local governments, and the Head Start pre-school program.

Nearly everyone agrees that sequestration has not been a good way of managing the budget. People on both sides of the aisle have identified flaws in the sequester process, including:

- By enacting across-the-board cuts, the federal government did not prioritize important, efficient, and well-run programs, or eliminate wasteful and inefficient programs.
- By focusing the vast majority of cuts on discretionary spending, the sequester did not reform the real drivers of our long-term debt: healthcare and entitlement spending. Furthermore, the discretionary spending subject to sequestration included investments in education, research, and infrastructure, areas which can be helpful to future economic growth.
- The reductions also come at a time when the economic recovery is still fragile. The Congressional Budget Office estimates that the economy will grow more slowly in 2013 — 1.4% instead of 2.0% — due to sequestration.

If policymakers enact a continuing resolution that freezes funding at the post-sequester levels, they would extend all of those sequestration flaws into 2014. If they ignore the limits, or don't raise them, OMB will be required to issue a new sequestration order 15 days after Congress adjourns at the end of this year. Rather than continuing a policy that almost everyone agrees is bad budgeting — and which could harm our economic recovery — Congress should replace this short-sighted and damaging process with a comprehensive plan that addresses the fundamental drivers of long-term debt.

TAX REFORM

DEADLINE: House and Senate Committees to Markup Legislation this Fall

While there is disagreement on specific remedies, there is broad consensus that our current tax code is broken. There will be an effort in the House and Senate to develop legislation to reform the tax code, which is viewed by nearly everyone to be too long, too complicated, riddled with tax preferences, and not supportive of economic growth.

One prominent strategy that has been discussed is the "blank slate" approach. This would eliminate all of the $1.3 trillion in annual tax expenditures, otherwise known as those loopholes, deductions, subsidies, credits and other special interest provisions that make the system highly complex. The resulting revenues could be used to lower tax rates, reduce the deficit, or a combination of both.

While both the President and Congressional leaders from both sides of the aisle have signaled a willingness to tackle tax reform, there is no doubt it would be challenging. Many of these expenditures, like the home mortgage interest deduction and the charitable deduction, are both popular and expensive. Still, tax expenditures are like spending by the federal government through the tax code, and most economists agree that many of them distort economic incentives and subsidize certain sectors of the economy at the expense of others.

Even if Congress does not pass a tax reform bill this year, it will have to decide whether to extend a large number of tax provisions that are scheduled to expire on December 31, 2013. Some of these provisions are broadly used (such as the tax credit for research and experimentation); others benefit more narrow constituencies (the 7-year recovery period for motorsport entertainment facilities, for example). The single most expensive provision set to expire is bonus depreciation, which was enacted as an economic stimulus measure in 2008.

An effective, comprehensive fiscal plan should include meaningful tax reform that results in more simplicity, fairness and economic growth, while raising sufficient revenue to fund our government's obligations.

CONCLUSION

We have been at a crossroads like this before. Unfortunately, in prior showdowns, we haven't fully taken advantage of the opportunity. 2011's debt limit fight led to fiscal reforms in the Budget Control Act, but it failed to address the fundamental drivers of our long-term debt, and therefore did not have a meaningful impact on our long-term fiscal outlook.

CBO recently warned that the national debt is near an all-time high and will grow to unsustainable levels. Under current law, the federal debt is approximately 73% of GDP. CBO projects that debt will climb to 100% of GDP within 25 years, and under less optimistic assumptions, that our debt will reach a staggering 190% of GDP during that same timeframe. Such levels of debt would be dangerous and simply unsustainable.

Rather than continuing to engage in brinksmanship that contributes to greater uncertainty, and results in poor policy, it's time to get our fiscal house in order once and for all. Congress and the President should work immediately to seek a comprehensive bipartisan framework to protect the economic recovery and stabilize our debt for the long term.