Center for American Progress
Budgeting for Growth and Prosperity
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Introduction

The purpose of the Center for American Progress plan for long-term deficit reduction is to build a strong American economy that provides the best opportunities for success of any country in the world and secures the position of the United States as the leading nation of the 21st century. It will not be possible to achieve these goals without addressing the dual challenges of rising red ink and a weakening middle class. That's why our plan's primary objective is to set the budget on a path toward full balance while growing and strengthening the middle class.

Why the focus on the middle class? First, growing and strengthening the middle class, creating the greatest good for the greatest number, is obviously a goal that has value unto itself. But it is also a key to economic growth and, hence, also a critical element for getting our national fiscal house in order. Without strong growth, balancing the budget is much harder. And without a strong middle class, our economy will not grow as it should.

The middle class is, in fact, the heartbeat of the American economy. Middle-class Americans are the indispensable workforce and the all-important consumer. It is from the middle class that the great American entrepreneurs and inventors have arisen. The education and skills of the middle class are responsible for the rise in productivity that underpins our prosperity. And a stable and large middle class keeps the United States largely free from internal political turmoil while at the same time demanding vital investments in education, roads, and other economically important infrastructure. The American ascent to becoming the richest nation on the planet is fundamentally a middle-class achievement. And the future of the American economy, and our ability to pay off our national debts, is just as linked to a strong middle class now as it has been in the past.

And the federal government has a key role to play in helping grow and strengthen the middle class. That role includes making critical investments in the areas such as education, infrastructure, and scientific research—areas that provide the foundation for a middle-class lifestyle and economic mobility. It includes ensuring the basic protections of civil society are maintained, as well as maintaining an effective and fair safety net. And it also includes guaranteeing every American a dignified retirement.

While there is tension between addressing our twin challenges of balancing the budget and revitalizing the middle class, our plan shows how the arithmetic can work.

Priorities for the next president and Congress

The president and Congress will be immediately faced with a myriad of important fiscal choices after the election and into 2013. With the so-called "fiscal cliff" looming, there is enormous pressure to avoid the economic consequences of dramatic fiscal contraction while simultaneously putting in place a plan to achieve significant deficit reduction over the next decade. Threading this needle will be challenging but it is by no means impossible. A comprehensive long-term budget deal that addresses these immediate challenges as well as the long-term needs of the country would be ideal. But at a minimum, in order to be successful, the president and Congress should enact the three policy changes detailed below.

Tax reform that generates adequate revenues and improves the progressivity of the entire tax system

The primary cause of our fiscal shortfall over the medium term is a lack of tax revenue. The primary obstacle to a large-scale budget deal over the last two years has been the refusal of conservatives in Congress to agree to any new revenue at all. The first priority must be to overcome that obstacle. If it isn't overcome, the country can forget about serious progress in addressing fiscal problems.

There are many forms that a successful tax reform can take. Our plan identifies one of them. But any reform must have two characteristics. First and foremost, it must generate adequate revenues—equal at the very least to those proposed by the chairmen of the bipartisan Bowles-Simpson commission. That plan was the product of a bipartisan negotiation, and it skewed somewhat toward spending cuts. Its recommended levels of revenue should be a minimum. Second, reform must improve progressivity, asking those with the most to pay more. Households at the top of the income ladder have seen their federal taxes drop dramatically over the past 15 years. Before we ask the middle class or the poor to pay more, we should reverse that trend.

Removing the sequester

If allowed to take effect, the automatic spending cuts known as the sequester, triggered by the failure of the "super committee" process last fall, would have a large and deleterious impact on the economy and on the federal government's ability to carry out its most basic functions. They should not be allowed to go forward. Ideally, Congress would replace them with better targeted and less economically harmful deficit reduction. To this end, accomplishing revenue raising tax reform would help. New revenue could be used to replace the "savings" from the sequester.

Implementing new job creation measures

The unemployment rate has fallen substantially over the past year, but it still remains near 8 percent. There is no realistic path to deficit reduction with joblessness at that level. More can and should be done to jumpstart job creation and help heal the labor market. We have proposed several measures, including directing more resources toward road construction and maintenance, helping local schools rehire teachers who have been laid off, and enhancing programs that retrofit buildings to become more energy efficient. These are just a few approaches that Congress could take.

Spending

The federal government makes investments that are important to our economy, provides services to the public, and carries out a variety of activities necessary to a well-functioning society. Our spending plan is designed to do those things well, do them efficiently, and do them at the appropriate level of public expenditure so that budget deficits are reduced to manageable levels in the medium term and eliminated entirely in the long term.

The CAP budget plan is roughly divided into two time periods: the next decade and the decades that follow. Our proposals for the next decade show a path that would bring budget deficits down to responsible levels in a manner consistent with today's political realities. We do not believe that these changes are sufficient to balance the budget, to invest appropriately in the middle class, or to address many other national challenges. Meeting those challenges will require a bolder strategy. For the purposes of this plan, we show that bolder strategy beginning in 2023. In fact, the country would be far better off if we adopted all of the policy changes recommended in our budget plan as soon as possible.

When considering changes in federal spending, it is critical to first understand that spending in one particular area—discretionary spending—has already been cut dramatically. Since January 2010 projections for federal discretionary spending over the next decade have been reduced by about $1.7 trillion, and that does not include the sequester. As a result, by 2017 federal nondefense discretionary spending will reach its lowest level, as a share of GDP, since at least 1962. Clearly, any additional cuts to federal spending must come from other areas.

To that end, our plan includes hundreds of billions of dollars in additional savings over the next 10 years from federal mandatory health care programs. In the long run, rising costs and an aging population make health care a major driver of our deficits. Many recent proposals to control federal health care costs, however, merely shift costs onto families and individuals without addressing the underlying problems. The savings in our plan would instead encourage health care providers to be more efficient and innovative, while also making targeted improvements to Medicare and Medicaid. Many of these savings enhance those already found in the Affordable Care Act, passed in 2010. The result will be lower federal spending on health care without sacrificing quality or access.

Our plan also finds savings in a variety of other "mandatory" spending programs in departments ranging from the Department of Agriculture to the Department of Transportation. The 10-year savings from these "other mandatory" programs total approximately $160 billion.

All together, including the discretionary cuts already enacted, the CAP plan would cut federal noninterest spending by more than $2.2 trillion over the next 10 years.

The spending cuts discussed above, along with the tax reforms described below, will put the federal budget on far more stable footing by the end of the decade. Those changes will not be enough, however, to sufficiently address three other important challenges: investing in the middle class and economic growth, combating poverty, and fully balancing the budget. Therefore, our plan also includes significant reforms to address those challenges. We recognize that the political will to carry out these reforms may not exist right now, and in deference to that recognition, our plan assumes that these types of reforms will begin in 2023. But that does not make these changes any less pressing right now.

Starting in 2023 the CAP plan makes significant new investments in scientific research, all levels of education, clean energy technologies, and transportation and infrastructure—areas where nations around the world are making substantial commitments. Our plan makes major investments in strengthening the American middle class. All of these investments are necessary if the United States wants to avoid being surpassed as the country with the greatest opportunities, the best jobs, and the most powerful economy. They are essential if we want our nation to continue to be where the great ideas and the most innovation comes from, and to remain a nation where entrepreneurs thrive and build successful businesses both large and small.

Investments such as these are the foundation of a strong 21st century economy. The country that leads in basic scientific research obviously has a huge advantage in innovation and technology. The country that can rely on domestically produced renewable energy isn't exposed to the risks associated with relying on imports, keeps funds at home that would otherwise go abroad, and gets a leg up on what will be one of the most important industries of this century. And the country that invests in its middle class produces educated, productive, and creative workers; a strong domestic market; a motivated workforce; and a population from which the greatest innovators and entrepreneurs emerge.

The CAP plan also makes a significant new investment in patching the holes in the social safety net. We propose increasing participation in the Supplemental Nutrition Assistance Program to 85 percent of eligible people, increasing the Supplemental Security Income benefit, increasing housing assistance by 20 percent, and boosting funding for children's programs.

Finally, we believe that the default position of the federal budget should be full balance, with the red ink reserved for recessions and emergencies. Along with our proposals to sufficiently invest in the middle class and combat poverty, our plan also makes long-run changes that will result in a balanced budget by 2031. This includes a broad reform to Social Security—the details of which can be found in a previously released report entitled "Building It Up, Not Tearing It Down."

It also includes a health care failsafe mechanism. We believe that the savings and reforms we've proposed, along with aggressive implementation of those in the Affordable Care Act, will result in dramatically lower health expenditures, both for the federal government and overall. But predicting the exact effect of the myriad test programs and reforms in the new health law is fraught with uncertainty. We therefore also include a failsafe mechanism that would ensure significant savings.

Our failsafe would be triggered if, starting in 2023, total economy-wide health care expenditures grow at a rate faster than the economy. Should that happen, we would empower the Independent Payment Advisory Board to extend successful reforms in Medicare and other public programs to insurance plans offered in the health care exchanges and then potentially to all health care plans, such that the target is met. This will ensure that costs are constrained across the health care sector, preventing cost-shifting and maintaining access for all.

Revenue

The number one priority of the next president and Congress is to pass a revenue and progressivity enhancing tax reform. Our tax reform plan makes the individual income tax simpler and fairer. Many loopholes, deductions, and exemptions are eliminated, but the ones middle-class families most rely on are replaced by better-targeted credits.

In addition, there will be a large flat "standard credit" that taxpayers can choose instead of the itemized credits. This standard credit works similarly to the current standard deduction. For most Americans, choosing the alternative credit instead of the itemized credits will both lower their overall tax bill and make filing simple and easy.

Our plan restores the top income tax rate to what it was under President Bill Clinton, which is still lower than it was during most of the postwar period. The plan also restores the top capital gains tax rate to the level signed into law by President Ronald Reagan.

Finally, the various reforms we've proposed will obviate the need for the alternative minimum tax and various high-income phase outs.

In addition this income tax reform, our plan includes a number of other tax changes, including:

- Restoring the estate tax to earlier levels, but indexed for inflation
- Adopting the corporate revenue proposals in President Obama's 2013 budget
- Eliminating some industry-specific tax expenditures that are effectively government spending administered through the tax system, including those for the oil industry
- Increasing some excise taxes

All together, our tax reforms would raise revenue to slightly above those proposed in the Bowles-Simpson plan.

As with the spending side of the equation, there are several additional tax measures that should be taken to ensure that the federal government can adequately address significant challenges such as investing in the middle class, combating climate change, and fully balancing the federal budget. These additional changes include:

- **Reducing greenhouse gas emissions and reliance on foreign oil by pricing carbon pollution and levying an oil-import fee.** Our plan addresses the risks and economic damage from our heavy reliance on foreign oil and the dangers of climate change by establishing a carbon tax and introducing an oil-import fee of $5 per barrel.

- **Financial transactions tax.** Starting in 2023 our plan imposes a modest fee on financial transactions, including trading in stocks, bonds, and derivatives. The tax is applied at a very low rate—less than two-tenths of a percent on stock trades. We believe the purpose of Wall Street is to raise capital for the productive sectors of the economy and that excessive financial speculation is counterproductive toward this purpose and harmful to stable growth in general. A financial transactions tax discourages unnecessary rapid turnaround speculation and improves incentives for long-term investment while raising revenue.

- **Social Security reform.** As mentioned above, a comprehensive reform to Social Security will be part of any plan that achieves full budgetary balance. CAP's reform proposal includes changes to both the spending and the revenue components of the program. On the revenue side, the most notable change is that our plan would remove the cap on the employer side of the payroll tax.

Conclusion

The Center for American Progress plan will move the federal budget onto far more sustainable ground. Most importantly, it will do so without unfairly burdening the middle class and the poor. It will do so by making our tax code fairer and simpler; by rooting out inefficiencies in our federal health care programs, asking health care providers to innovate and improve; and by doing away with spending that is outdated, wasteful, or simply unnecessary. By 2023, instead of debt soaring past 90 percent of GDP on its way to 100, debt will be under 65 percent of GDP and falling.

Furthermore, our plan shows how we can achieve a fully balanced budget by 2031, while simultaneously making adequate investments in the middle class, and moving affirmatively towards a 21st century economy. And our plan would allow the country to more effectively meet great national and global challenges like poverty and climate change.

We can balance the budget while investing in growth, fighting poverty, and addressing climate change. And we can start down that path immediately.

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Percent of GDP	2022	2037
Revenues	20.8	23.1
Spending	22.4	22.5
Deficit (-)	-1.6	0.6
Debt held by the public	66.0	40.4