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THE POLITICS OF CUTTING SPENDING

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Recent exchanges in the press about the House Republicans' "Contract with America" underscore once again why spending is at the heart of the federal deficit problem and why piecemeal spending cut proposals almost invariably fail.

Whenever a lawmaker or candidate proposes to trim the growth of federal spending, or to cut the tax burden on Americans by trimming programs, a familiar political game begins — in which the taxpayer is always the loser. First, the individual advocating spending cuts is challenged to reveal the specific cuts he or she proposes. Then, as soon as a proposed cut is revealed, political opponents appeal to those who would be directly affected by the cut. With most to lose, these program beneficiaries campaign vigorously against the spending reduction. And although the average taxpayer would gain from the cut, the fact that the savings are spread thinly across all taxpayers means the gain to any single household is very small. Consequently, it is difficult for the politicians supporting a cut to mobilize popular support among average taxpayers, while those opposing the cut can count on the well-organized, well-financed, and impassioned backing of the program's beneficiaries.

This lopsided political calculus always gives the advantage to those opposing cuts in spending. It also makes it very risky for lawmakers and candidates to specify how spending should be controlled —doing so can be political suicide because it triggers a special-interest backlash. This calculus has been explained by "public choice" economists as one of the main reasons why it is so difficult to control spending in the U.S. political system.

Understanding the political dynamics of spending cut proposals led Heritage Foundation scholars last year to propose an economic plan based on two political tactics:[1]

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1 Scott A. Hodge, "Putting Families First: A Deficit Reduction and Tax Relief Strategy," Heritage Foundation *Backgrounder* No. 927, February 16, 1993.

1) **A package of spending cuts should in part finance targeted tax reductions.** These tax reforms should not be across-the-board reductions, however, which would have little impact on each household. They should instead be tax cuts that provide large benefits to certain identifiable households, while correcting a genuine problem in the tax code that slows the economy or hurts families. In this way, a strong constituency can be assembled with much to gain from a package of spending cuts. This constituency then becomes a political counterweight to the constituency resisting the budget cuts.

2) **The specific cuts should be assembled by a commission within the framework of a legislated limit on the growth of federal spending.** The spending-cut commission would act much like the military base closing commission, or a team of trade treaty negotiators. It would assemble a package of cuts that balances sensitive competing political concerns, and this package would be presented for an up-or-down vote in Congress without amendment. In this way, the Heritage scholars reason, lawmakers would not be voting on individual cuts, and so would be less vulnerable. Like up-or-down votes on a package of base closings, or a trade treaty, an up-or-down vote on a spending package — especially if linked with targeted tax relief — would help insulate members from attacks by beneficiaries of particular programs.

This strategy led to a tax relief and spending reduction proposal, called Putting Families First, which centers on family tax relief. This plan formed the central features of H.R. 3645, sponsored in the House by Representatives Rod Grams (R-MN) and Tim Hutchinson (R-AR), and S. 1576 sponsored in the Senate by Dan Coats (R-ID). In this proposal:

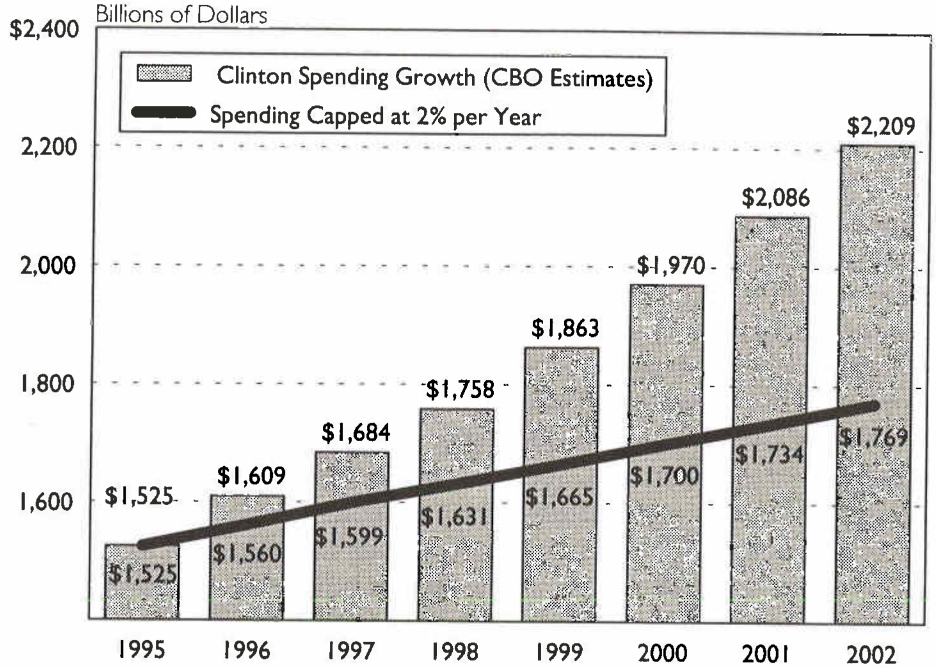
✔ The rate of increase of federal spending would be held at a growth rate of 2 percent per year, or just below the current rate of inflation. This would yield savings of $727 billion over the next five years when compared with the current pattern of federal spending projected by the Congressional Budget Office. The CBO projects total federal spending to grow over 5 percent annually through fiscal 2004. The appendix contains an updated summary of the effect of the spending cap.

✔ The specific cuts needed to meet the required 2 percent limit would be developed by an independent commission, modeled on the base closing commission. The recommendations of the commission would voted on by Congress without amendment.

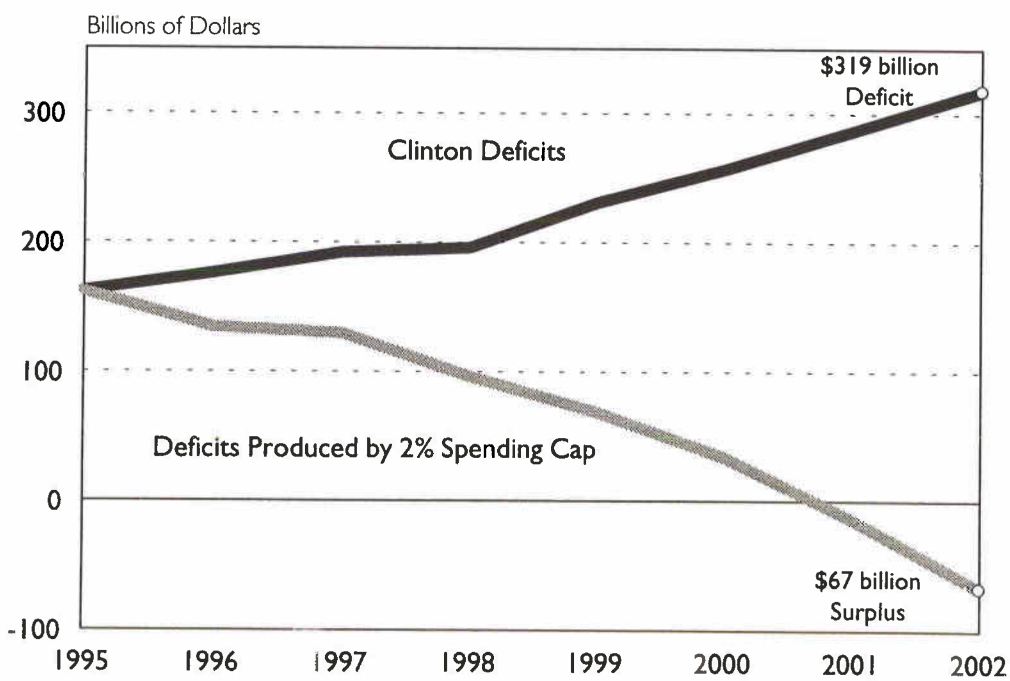
✔ Of the $727 billion in savings from spending cuts, roughly $140 billion would be returned to the economy in tax cuts. Specifically:

- ✂ Some $108 billion would be returned to 35 million families in the form of a new $500 tax credit per child for all working families with children.
- ✂ Another $9 billion would be returned in a package of pro-growth tax reductions, including the indexation of capital gains, expanded individual retirement accounts (IRAs), and a neutral cost recovery plan. It should be noted that the cost of this tax relief assumes a "static" revenue estimate, or that marginal tax rate cuts do not stimulate new revenue — contrary to experience. Thus in reality, the cost of the package would be less than $9 billion.
- ✂ Another $26 billion would be returned to seniors by lifting the tax penalties on seniors who work.
- ✂ The remaining $588 billion would be devoted to deficit reduction, leading to a balanced federal budget in fiscal 2001 (see appendix).

The 2% Spending Cap Saves $727 Billion Over Five Years and $1.5 Trillion by Fiscal 2002



Clinton Deficits vs. Spending Cap Deficits



Note: Deficits produced by 2% spending cap assume static revenue losses from tax cuts.

To be sure, it would be wise to furnish a commission with a menu of possible cuts as the starting point for a package. Ideally this would take the form of cuts likely to have bipartisan support. Perhaps a good starting point would be some 100 cuts already proposed by White House Chief of Staff Leon Panetta when he was chairman of the House Budget Committee, and by Office of Management and Budget Director Alice Rivlin when she was Director of the Congressional Budget Office. Cuts already put forward by two top Clinton Administration officials, and supported by many Republicans, could form the bipartisan foundation of a commission-proposed package. The appendix contains a summary of the Panetta-Rivlin cuts, which total nearly $300 billion in savings.

The public choice dynamics of spending control play into the hands of those who want to block any reductions in the growth of federal spending. Thus, although it may seem reasonable for an opponent to demand which specific cuts a candidate or lawmaker proposes to finance a tax reduction, in reality this merely presents the spending cut and the politician recommending it as open targets for the special interests who gain from the affected program. It is important for politicians who advocate spending control and lower taxes to avoid this trap by arguing for a commission to recommend the package of cuts, and by building constituency support for spending reduction by linking cuts to targeted tax relief. Comprehensive trade treaties could never be enacted by Congress if lawmakers voted on each line of an agreement, and not a single unnecessary military base was closed for ten years until Congress had to vote up-and-down on a commission-recommended list of closings. There will be no real control of federal spending as long as lawmakers and candidates are force to defend specific line-item cuts against the inevitable barrage of special-interest lobbying.

NOTES TO APPENDIX

The attached spending cut recommendations were taken from "Balanced Budget Amendment Options," House Committee on the Budget (Leon Panetta, Chairman), May 26, 1992, and *Reducing the Federal Deficit: Strategies and Options*, Congressional Budget Office (Alice M. Rivlin, Director), February 1982.

The estimated savings resulting from these proposed cuts have been updated, where possible, based upon the estimates contained in CBO's *Reducing the Deficit: Spending and Revenue Options*, February 1994. The estimated savings from the options identified with an asterisk (*) were derived from: "The Balanced Budget Plan," submitted on March 17, 1994, as an alternative 1995 budget by the Balanced Budget Task Force chaired by Congressman Gerald B. Solomon, or CBO's *Reducing the Deficit: Spending and Revenue Options*, February 1993.

SELECTED SPENDING CUTS PROPOSED BY PANETTA AND RIVLIN

Function	DISCRETIONARY SPENDING CUTS	Five-Year Total Savings ($Millions)
150	Consolidate Overseas Broadcasting Programs	$2,150.0
150	Reduce Security Assistance	$1,740.0
150	Phase-out Defense Acquisition Fund*	$200.0
150	Reduce Export-Import Bank Credits	$1,380.0
150	Phase Out Economic Assistance to Israel and Egypt*	$4,510.0
250	Cancel the Advanced Rocket Motor*	$496.0
250	Cancel the Space Station	$10,400.0
270	Eliminate Further Clean Coal Technology	$20.0
270	Change Strategic Petroleum Reserve Funding	$325.0
270	Reduce Rural Electrification Administration Subsidies	$260.0
300	Reduce Below-cost Timber Sales	$235.0
300	Enact Superfund Cost Containment Measures	$2,180.0
300	Hike Weather Service Fees*	$25.0
300	Privatize the NOAA Research Fleet*	$250.0
300	End EPA Sewage Treatment Grants*	$7,115.0
350	Streamline USDA Field Offices	$900.0
350	Reform Foreign Agriculture Service (FAS)	$150.0
350	Reduce ACIF Farm Loans	$430.0
350	Reduce Agriculture Research & Extension Services by 50%	$830.0
370	Eliminate Trade Promotion Activities	$820.0
370	End Small Business Administration Earmarked Grants*	$54.0
370	Eliminate SBA Business Loans	$2,680.0
370	Reduce Export Administration by 25%	$45.0
370	Eliminate FmHA Homeownership Loans	$1,840.0
370	Eliminate FmHA Rental Housing	$1,430.0
400	Cut Highway Demonstration Projects	$2,590.0
400	Cut Airport Improvement Grants	$6,260.0
400	Abolish the Interstate Commerce Commission	$140.0
400	Eliminate Essential Air Service Subsidies	n/a
400	Cut Urban Mass Transit Subsidies	$6,880.0
400	Eliminate Amtrak Subsidies	$1,900.0
450	Eliminate TVA Non-power Programs	$610.0
450	Eliminate the Appalachian Regional Commission	$690.0
450	Eliminate Rural Development Loans and Grants	$1,930.0

SELECTED SPENDING CUTS PROPOSED BY PANETTA AND RIVLIN

Function	DISCRETIONARY SPENDING CUTS	Five-Year Total Savings ($Millions)
500	Eliminate Campus-based Aid	$5,920.0
500	Eliminate State Student Incentive Grants	$350.0
500	Eliminate Impact Aid	$4,120.0
500	Eliminate Consumer Homemaking Grants	$140.0
500	Eliminate Law-related Grants	$25.0
500	Eliminate Community-based Grants	$50.0
500	Eliminate Law School Grants	$60.0
500	Eliminate Library Grants	$70.0
500	Eliminate Follow-Through	$35.0
500	Eliminate the National Endowments for the Arts and Humanities	$5,300.0
500	Consolidate Social Service Programs	$5,590.0
550	Reduce funding for the National Institutes of Health by 10%	$5,110.0
550	Eliminate Most Health Training Subsidies*	$1,427.0
600	Modify Fees for Federal Housing	$1,230.0
600	Reduce HUD Utility Payments*	$145.0
600	End HUD New Construction and Replace with Vouchers	$955.0
600	Reduce Refugee Assistance*	$463.0
700	Cut new VA Construction*	$557.0
700	Improve Management of VA Hospitals*	$3,230.0
700	Close or Convert Outmoded VA Hospitals	$1,170.0
750	Eliminate Justice Assistance	$1,230.0
920	Terminate Most Commissions*	$645.0
920	Cut Civilian Agency Overhead Costs*	$24,489.0
920	Repeal the Davis-Bacon Act	$3,080.0
	Total Discretionary Savings =	**$126,856.0**