Backgrounder

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Restrain Runaway Spending with a Federal Taxpayers' Bill of Rights

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Federal spending has leaped 25 percent since 2001, exceeding $20,000 per household (See Chart 1). Frustrated taxpayers are seeking ways to protect their family budgets from the federal budget. These taxpayers should look to Colorado.

In 1992, Colorado citizens revolted against their free-spending lawmakers by petitioning for a referendum to limit the growth of state government to the inflation rate plus the population growth rate. Voters quickly approved the Taxpayers' Bill of Rights (TABOR), ushering in a new era of fiscal responsibility and economic growth. Over the next decade, spending was reined in, taxes plummeted, and the Colorado economy became the envy of the nation.

Just as Congress followed the states' lead on welfare reform in the 1990s, it should follow the states' lead on spending limits. A federal Taxpayers' Bill of Rights would succeed where other budget reforms have failed. It would protect taxpayers' paychecks by forcing lawmakers to live under constraints—just like families, businesses, and state and local governments do. This paper explains how such a policy could work.

Talking Points

- Runaway federal spending is the predictable result of an outdated budget process that lacks any enforceable spending limits, and therefore requires no priority setting, no trade offs, and no difficult decisions.
- A federal Taxpayers' Bill of Rights (TABOR) would limit annual spending increases to the inflation rate plus the population growth rate and reserve any budget surpluses for tax relief and debt reduction.
- Colorado enacted the nation's first TABOR law in 1992. Since then, the state's taxes have plummeted while its economic, job, and income growth rates have all nearly doubled.
- A federal Taxpayers' Bill of Rights would save taxpayers $4 trillion over the next decade.

This paper, in its entirety, can be found at:
www.heritage.org/research/budget/bg1793.cfm

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The Failure of Other Options

During the past decade, reforming the budget process has been an exercise in futility. Lawmakers who focus obsessively on a single $100,000 pork project pay scant attention to the overall budgetary framework used to allocate $2.3 trillion in federal

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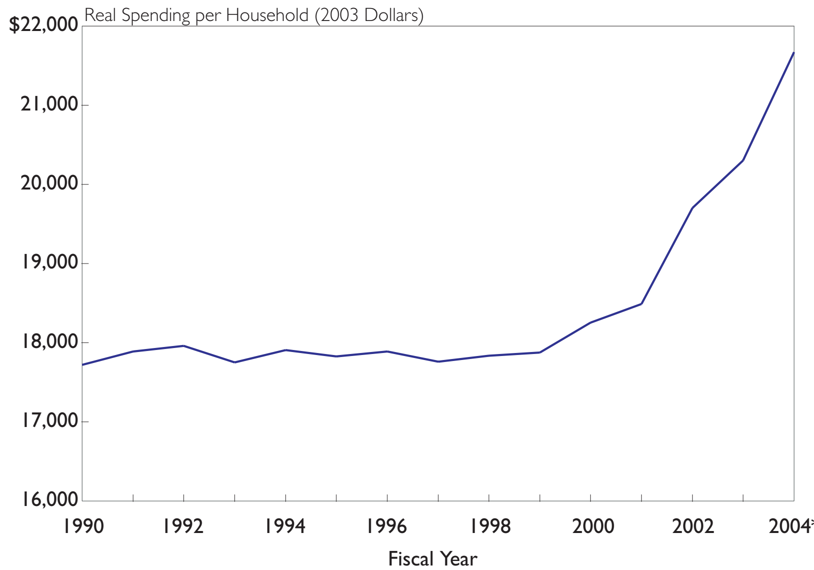
spending. When budget process reform is finally debated, lawmakers focus more on protecting their committees' turfs than on fixing the budget problems. The rare (and overly arcane) reforms that are enacted are first watered down to irrelevance and then riddled with loopholes. All four reforms of the budget process that have been tried in the past decade have failed.

Chart 1 B 1793

Washington Now Spends More Than $20,000 per Household



Source: Heritage Foundation calculations based on data from the U.S. Census Bureau and the Office of Management and Budget.

Pay-As-You-Go (PAYGO) Rules and Discretionary Spending Caps. PAYGO rules, in place from 1990 through 2002, mandated that any new law cutting taxes or expanding entitlements be balanced by equal tax increases or entitlement cuts. It was an abysmal failure: Mandatory spending actually grew faster *after* PAYGO was enacted. It failed because it limited only the creation of new entitlements, while allowing current programs—such as Social Security Medicare, Medicaid, and farm subsidies—to expand rapidly. Additionally, PAYGO placed barriers on tax relief, and Congress easily dismissed PAYGO rules when they became inconvenient.

Discretionary spending caps, written every three to five years, were more successful. Yet, even caps were too easily disregarded by lawmakers, who could exempt any program simply by labeling it an "emergency." In the House of Representatives, caps could be waived with a simple majority vote. Recently, Members of the House strongly rejected a measure that would have restored discretionary spending caps—effectively refusing to accept any statutory limit on their ability to spend tax dollars.

The Family Budget Protection Act. Proposed by several conservatives and moderates in the House, the Family Budget Protection Act (FBPA) contained over one dozen important procedural reforms.[1] These included converting the concurrent budget resolution into a joint budget resolution (which would have the force of law), entitlement caps, point-of-order reform, enhanced rescission, and rules making it easier to save money in appropriations bills. Instead of a bias toward bigger government and higher taxes, the budget process would finally protect taxpayers. Regrettably, these reforms were overwhelmingly defeated in the House.

The FBPA was rejected, in part, because it was too arcane to be understood outside the Beltway. Lawmakers are typically interested in protecting their committees' turf and retaining their ability to distribute government benefits. Only a popular outcry from the voters back home will persuade most lawmakers to overcome their own bias and vote for fiscal responsibility. Because the FBPA was too complex to be understood by most

1. H.R. 3800. For a summary of the bill, see Brian M. Riedl, "Better Budget Reform: A Guide to the Family Budget Protection Act," Heritage Foundation *Backgrounder* No. 1758, May 17, 2004, at *www.heritage.org/Research/Budget/BG1758.cfm*.

voters, there was no popular push for it, and lawmakers were free to reject it without serious political consequences.

Balanced Budget Amendment. Unlike the FBPA, the balanced budget amendment is widely understood by the American people (which is why it receives broader support from lawmakers, despite being a more radical reform). The movement for a balanced budget amendment has stalled as well, not only because the budget reached surplus between 1998 and 2001, but also because constitutional amendments are extremely difficult to enact.

Additionally, a balanced budget amendment focuses on the wrong issue. The budget deficit is merely a symptom; runaway spending is the disease. The United States could balance the budget tomorrow by raising taxes to levels that would devastate families, businesses, and the economy. Instead of seeing deficit reduction as end in itself, lawmakers should focus on the runaway spending that creates the deficits and high taxes in the first place.

Trust Lawmakers to Cut Spending. Lawmakers continue to work within a budget framework designed 30 years ago to maximize federal spending. Many Members of Congress claim that they can cut spending on their own and do not need any budget process reforms or spending limits to enforce what they plan to do anyway. This viewpoint represents the triumph of hope over experience. These lawmakers are absolutely correct that people, not process, are ultimately to blame for runaway spending. However, persistent runaway spending provides ample evidence that lawmakers are unable to control spending on their own without outside constraints.

According to public choice theory, lawmakers have incentives to continually expand government. This is exactly what is happening. The current federal budget process requires no priority setting, no trade offs, and no difficult decisions. Families operate under external budget constraints, as does virtually every state government. It is naïve and ahistorical to believe that Members of Congress will resist the budget process pro-spending bias and reduce spending on their own.

Five Lessons

Five lessons can be drawn from these failures:

1. Members of Congress will not make difficult spending trade-offs unless required by law.
2. Although a constitutional amendment would be the most enforceable means of reform, it is too difficult to enact.
3. A successful proposal for reforming the budget process must be understood and strongly supported by voters in order to overcome the turf-protection and pro-spending bias in Congress.
4. Spending constraints should put all spending on the table—mandatory and discretionary, current and proposed. All programs should have to compete with each other for the limited federal funds.
5. Members of Congress will exploit every possible weakness in spending constraints.

The Promise of a Taxpayers' Bill of Rights

A Taxpayers' Bill of Rights presents a simple, yet effective way to curb runaway spending. TABOR would limit the growth of federal spending to the inflation rate plus population growth. Rather than growing 6.4 percent annually (the average during the past five years), federal spending would typically increase by approximately 3.3 percent annually. Although this slower growth rate may not seem like a significant change, it would save taxpayers more than $4 trillion over the next 10 years (See Chart 2).

Limiting annual federal spending growth to approximately 3.3 percent is not too much to ask of Congress, especially considering that the federal budget has expanded by 30 percent in the past five years and contains hundreds of billions of dollars worth of wasteful and obsolete programs. The current $2.3 trillion federal budget would still be large enough to fund all current programs, and these programs could continue growing at the inflation rate plus the population growth rate. Programs that expand at faster rates would need to be offset by reductions in the growth rates of other programs.

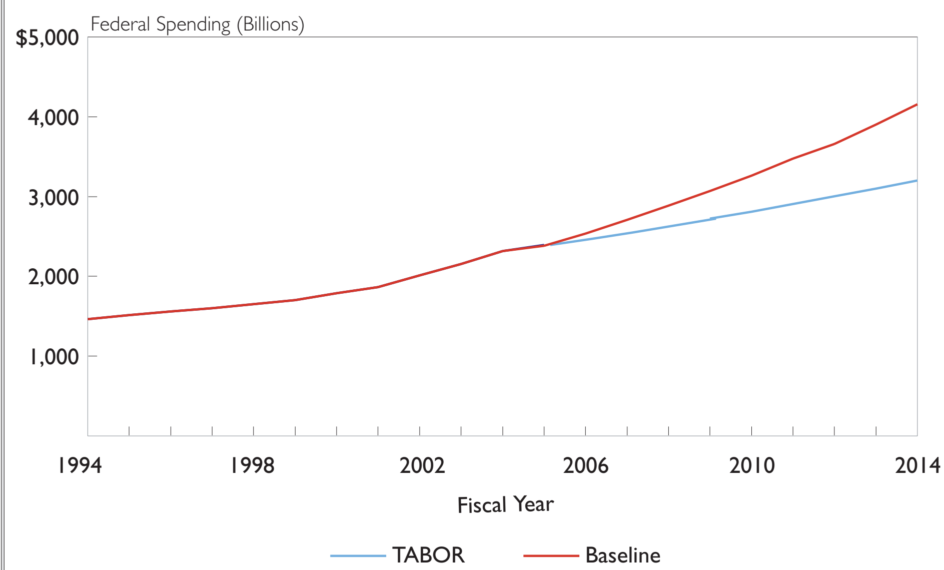
Six Principles of a Federal TABOR

A federal Taxpayers' Bill of Rights should follow six basic principles:

Principle 1: A TABOR Should Restrict Spending Growth, Not Revenues. High tax rates devastate economies. Yet a law simply requiring low tax revenues without any spending controls is not sustainable because unrestrained spending would likely create unallowably large budget deficits until taxes would need to be raised. The simple truth is that federal spending determines the required level of taxes. Therefore, a law limiting federal spending is the most effective way to guarantee long-term tax relief.

Chart 2 B 1793

A Taxpayer Bill of Rights Would Save $4 Trillion over the Next Decade



Source: Heritage Foundation estimates based in part on data from the Congressional Budget Office.

Furthermore, lawmakers cannot exercise much control over tax revenues. Economic trends create short-run revenue fluctuations that make it nearly impossible to target a specified revenue level. A TABOR would be more effective by focusing on spending, which lawmakers can directly control.

TABOR spending restrictions can easily avoid two predictable problems: First, in order to prevent forecasting games, the TABOR inflation and population growth allowances should be a rolling average of the previous three years' rates. Second, TABOR should apply to outlays (actual expenditures) rather than budget authority (the credit limit Congress provides to an agency to spend down). Over the past few years, Congress has manipulated budget authority amounts to the point that they have become meaningless. Outlays are what matter because they are actual expenditures of taxpayer money.

Principle 2: TABOR Spending Limits Should Be Enforced by a Two-thirds Supermajority and by Sequestration. TABOR spending limits would be enforced during the budget resolution vote, as well as the vote on any discretionary appropriations bill or entitlement reform that would put total spending above the TABOR cap. (A projection of total mandatory outlays would need to be combined with the discretionary spending bills to arrive at the spending total.) Legislation violating TABOR would require a two-thirds supermajority.[2]

The two-thirds supermajority requirement recognizes that there will be rare emergencies (e.g., war) when Congress may need to spend more than

2. Colorado requires a voter referendum to exceed the spending limits, which is more effective but less feasible at a federal level.

Colorado's Successful Taxpayers' Bill of Rights

Following the lead of innovative states such as Wisconsin, Congress reformed federal welfare programs in the 1990s, resulting in the most successful federal social policy of the past 60 years. This decade, Colorado's TABOR offers a proven model for Washington to use to restrain spending.

In 1992, Colorado taxpayers, frustrated with ever-rising taxes and wasteful state spending, petitioned for a referendum to amend the Colorado constitution to limit the growth of government to inflation plus population growth. The Taxpayers' Bill of Rights passed with 54 percent of the vote. Some of its results are shown in Table 1.

Other facts about TABOR include:

- Between 1989 and 2000, Colorado's state and local tax burden ranking dropped from 28th to 43rd.
- If spending and revenues had continued growing at their pre-TABOR rate, the average Colorado household would have paid $3,729 more in taxes in 2002.
- In the five years before TABOR, the Colorado economy grew at the national average. Following TABOR's implementation, it surged to 6.1 percent average annual growth, dwarfing the national average of 3.6 percent.
- Colorado's 1993–2001 per capita economic growth rate ranked fifth in the U.S.
- A majority of Colorado's elected officials say that TABOR has made them less likely to support or propose a tax increase.
- After 10 years of TABOR—and despite a national recession and well-financed campaign to repeal the amendment—Colorado residents continue to support the amendment by an overwhelming 3:1 margin.

Other states are following Colorado's lead. TABOR movements are gaining momentum in New Hampshire, Wisconsin, and Minnesota.

Table 1 B 1793

Colorado: Before and After TABOR

	1983–1992 (Pre-TABOR)	1993–2002 (Post-TABOR)
Average annual per-capita govt. spending increase	7.2%	3.1%
Average annual per-capita govt. revenue increase	8.5%	2.9%
Total automatic tax refunds	$0	$3.25 billion
Total job growth	18.1%	34.6%
Total nominal per-capita personal income growth	$7,810	$14,437

SOURCES: Fred Holden, "A Decade of TABOR," Independence Institute *Issue Paper* No. 8-2003, June 2003, pp. 6-7, at *i2i.org/articles/tabor2003.pdf* (August 17, 2004); Bell Policy Center, "Ten Years of TABOR," March 2003, pp. 8-10, at *www.thebell.org/Revised.pdf* (August 17, 2004). See also Ciruli Associates, "All Three Statewide November Ballot Issues Faced Uphill Battle," November 5, 2003, at *www.ciruli.com/polls/nov03polls.htm* (August 17, 2004). Economic growth statistics were calculated by the Heritage Foundation using data from the Bureau of Economic Analysis in the U.S. Department of Commerce.

TABOR allows. Setting the bar at two-thirds is low enough to clear during a national emergency or war, but high enough to prevent abuse. This policy would require Rules Committee reforms (or at least cooperation from the Rules Committee) to prevent the altering of this two-thirds requirement during key votes.[3]

If Congress exceeds TABOR spending without getting the two-thirds vote necessary to enact the spending override (for example, entitlement programs that spend more than projected), Congress could come back and cut spending elsewhere to remain in line with TABOR's limits. Otherwise, the Office of Management and Budget would seques-

Applying TABOR to the Federal Government

Although a federal TABOR should be based on Colorado's law, applying this successful state policy to the federal government would require a few modifications:

- Colorado's TABOR is a constitutional amendment, which would be too difficult to pass at the federal level.
- Overriding Colorado's TABOR spending limits requires a voter referendum, which is not realistic at the federal level. This leaves a legislative supermajority as the best federal option.
- Colorado's TABOR restricts tax revenue growth, which has caused some problems due to economic fluctuations and the "ratchet effect" of recessions, which permanently lower the revenue base. Beyond the obvious economic effects, this would also be politically problematic and could undermine support for a federal TABOR.
- Colorado's TABOR mandates that all budget surpluses be used for tax cuts, yet, Colorado does not carry a debt burden anywhere near the federal government's burden.

ter funds using preset sequestration formulas, which were used under discretionary spending caps and PAYGO.[4]

Principle 3: Congress Should Be Required to Budget for Emergencies. No spending restraint is legislatively foolproof, so there must remain a political stigma attached to bypassing the spending limits. However, if two-thirds of Congress had to override TABOR every time there was a small emergency somewhere in America, these overrides would become routine and less controversial. Requiring Congress to reserve room in the budget for the predictable emergencies would keep all but the most catastrophic emergencies from requiring TABOR overrides.

Principle 4: States Should Be Protected from New Unfunded Mandates. In a budget-cutting environment, lawmakers may be tempted to find savings by passing new unfunded mandates onto states. This is counter to TABOR's goal of reducing the cost of government. If Congress passes a new unfunded mandate, the TABOR cap should be reduced by the amount of federal money saved, as determined by the Congressional Budget Office.

Principle 5: Budget Surpluses Should Be Split Between Tax Rebates and Debt Reduction. The 1998–2001 budget surpluses induced a massive spending spree because these surpluses were portrayed as "free money" sitting in a pile waiting to be used. If TABOR successfully restrains spending and creates budget surpluses, lawmakers will surely be tempted to override TABOR and spend more on popular programs.

What if budget surpluses were automatically split between tax rebates and debt relief? Instead of spending "free money," lawmakers would be cutting the tax rebates to taxpayers as well as raiding a debt relief fund designed to reduce the debt burden passed onto future generations.[5]

Principle 6: TABOR Should Be a Statute, Not a Constitutional Amendment. While Colorado's TABOR is an amendment (and therefore well enforced), attempting to amend the U.S. Constitution would probably be a futile quest, which leaves reform by statute as the best option.

3. Of course, a congressional majority could circumvent TABOR by simply writing a new law altering TABOR and adjusting the cap. (This was done with discretionary caps and PAYGO.) In the absence of a constitutional amendment, such chicanery cannot be completely prevented. One of the most feasible ways to prevent such games is through political pressure to respect TABOR caps and restrict overrule votes to catastrophic emergencies.
4. Given that PAYGO exempted the vast majority of mandatory spending from sequestration, Congress should revisit sequestration formulas in order to guarantee sufficient room for these required spending cuts,

What About Medicare and Social Security?

The most predictable objection to a Taxpayers' Bill of Rights is that the exploding costs of Medicare and Social Security will make restraining federal spending nearly impossible. These programs are projected to grow 6 percent annually, which would seem to bar lawmakers from capping total federal spending at an annual growth rate of about 3.3 percent.

However, this is exactly why the nation needs a TABOR law. If Social Security and Medicare are allowed to grow at the current rate, they will bankrupt the federal budget. Within a few decades, taxes will have to increase by the current equivalent of $10,000 *per household* just to pay for Social Security and Medicare—unless these programs are reformed.

Furthermore, excluding Social Security and Medicare from TABOR would deny the fundamental reality that budgets are about setting priorities and making trade-offs. These programs do not exist in a vacuum and cannot be considered separately from the rest of the federal budget. If lawmakers choose to let these programs grow at their projected rates, they will be forced to either eliminate every other federal program or raise taxes to economically devastating levels. Exempting these programs from TABOR will not avoid this mathematical reality. It will merely delay the painful but inevitable trade-offs.

This does not mean that lawmakers would immediately have to reform Social Security and Medicare before the nation has developed a consensus on these issues. These programs are currently growing approximately $20 billion per year faster than they would if they grew at a 3.3 percent rate that would be consistent with a typical TABOR allowance. Over the next few years, Congress could easily offset the $20 billion increases by eliminating the hundreds of billions of dollars of wasteful and obsolete spending in the federal budget.[6] Those offsets would buy Congress at least five years to reform Social Security and Medicare before their costs begin to overwhelm TABOR spending levels.

Conclusion

The current federal spending spree is unsustainable; yet, Congress has rejected recent attempts to bring sanity to the budget process and encourage fiscal responsibility. A federal Taxpayers' Bill of Rights provides a simple, effective, proven model for spending reform. A TABOR would force lawmakers to live under spending restraints in the same manner that families, businesses, and state and local governments do. It would force lawmakers to set priorities, make trade-offs, and reduce wasteful spending. Colorado has proved that TABOR can restrain spending, reduce taxes, and facilitate economic growth. More than ever, a Taxpayers' Bill of Rights is needed to protect the family budget from the federal budget.

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5. Lawmakers would not have to wait until the end of the year to cut taxes. They could reduce taxes any time in order to prevent a budget surplus from occurring in the first place.
6. For example, the federal government cannot account for $24.5 billion spent in 2003. This and other examples of government waste are detailed in Brian M. Riedl, "How to Get Federal Spending Under Control," Heritage Foundation *Backgrounder* No. 1733, March 10, 2004, at *www.heritage.org/Research/Budget/bg1733.cfm*.