WebMemo
Published by The Heritage Foundation

No. 2884
April 27, 2010

Guidelines for a Successful Fiscal Commission

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President Obama's Commission on Fiscal Responsibility and Reform (known popularly as the "deficit commission") is set to begin assembling recommendations to reduce the budget deficit to 3 percent of the gross domestic product (GDP) by 2015 and to address long-term deficits. The commission faces an uphill battle, as no bipartisan consensus currently exists on how to close long-term budget deficits. And despite the commission's important duties, it is being run with few resources to assist the commissioners and no funding to get out of Washington and solicit the views of the American people.[1]

The President has not yet built credibility on deficit reduction. Rather than focus on the deficit immediately after taking office, President Obama first deepened the deficit hole with a $787 billion "stimulus" bill, an 8 percent hike in discretionary spending, another unpaid-for Medicare "doc fix," and a trillion-dollar health care expansion. Only after most of the President's expensive spending priorities had already been locked in (and worsened the budget situation) will his deficit commission have had its first meeting. This feeds the perception that President Obama is not serious about spending control but merely seeking a bipartisan rubber stamp for tax increases to pay for his past spending.

The commission can still succeed by focusing on specific reforms to the entitlement programs that are driving long-term deficits upward.

Principles for Reform:

Move Toward Historical Levels of Taxes and Spending. Over the past 40 years Washington has, on average, collected 18.3 percent of GDP, spent 20.7 percent of GDP, and ran a sustainable deficit of 2.4 percent of GDP. Assuming current tax and spending policies continue (including the 2001 and 2003 tax cuts), revenues are soon projected to rebound from their recessionary dip back to the typical 18 percent of GDP. Yet spending is projected to leap to 23.6 percent of GDP by 2015 and 26.4 percent by 2020, on its way past 30 percent of GDP.[2]

Simply put, growing long-term budget deficits are almost exclusively the result of rising spending—not declining revenues. Thus, common sense suggests that most of the reforms should occur on the spending side. Given the magnitude of the long-term spending increase, even splitting the difference between spending cuts and tax increases would leave the highest sustained spending—and tax burden—in American history. Permanently transforming the federal government in this manner would slow economic growth and harm families and businesses.

Bring Long-Term Solvency to Social Security and Medicare and Reform Medicaid. Nearly the entire increase in long-term budget deficits results from rising Social Security, Medicare, and Medicaid costs. It may be possible to squeeze enough savings from other sources to meet the 2015 deficit target, but the surging cost of these three programs would quickly

This paper, in its entirety, can be found at:
http://report.heritage.org/wm2884

Produced by the Thomas A. Roe Institute
for Economic Policy Studies

Published by The Heritage Foundation
214 Massachusetts Avenue, NE
Washington, DC 20002–4999
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devour those savings and continue expanding the budget deficit. Thus, the commission should look beyond just the 2015 target year and seek entitlement reforms that bring long-term solvency to the federal budget.[3]

Reopen the Health Care Law. President Obama has pointed out that health care reform is entitlement reform. Thus, bipartisan health reform should be part of bipartisan budget reform.

The Congressional Budget Office (CBO) estimates that—even in the unlikely event that all scheduled Medicare cuts actually take place and new heath subsidies are not expanded—Obamacare would expand federal spending by $382 billion through 2019 (and substantially more thereafter).[4] As the federal budget sinks under the weight of soaring health care costs, this new health law will pile even more costs on top. This is absolutely unsustainable.

The easiest spending program to cut is one that has not yet been implemented. The commission should reopen Obamacare, reform its unaffordable provisions, and use any savings for deficit reduction rather than new spending.

Offer Specific Spending Reforms, Not Just Numerical Targets. In 1982 and 1990, bipartisan budget deals coupled immediate tax increases with vague promises of distant spending cuts to meet pre-set targets. Predictably, the spending cuts were rarely implemented. Long-term spending targets and caps are an important part of budget reform, yet they are hollow if not accompanied by specific, credible proposals to reform federal spending programs. Rather than punt the tough spending decisions, the commission should specify them.

No New Taxes or Tax Increases. As stated above, the rising long-term budget deficits do not result from declining revenues, which are projected to return soon to the historical average of 18 percent of GDP. Rather, they result from a historic surge in Social Security, Medicare, Medicaid, and net interest spending. Therefore, the vast majority of reforms should aim to reduce those costs.

America cannot tax its way out of this problem. The long-term increase in Social Security, Medicare, and Medicaid costs comes to 10 percent of GDP. In today's economy, a tax increase of 10 percent of GDP would cost $12,000 per household annually. The CBO estimates that, over the long-term, the middle class would be pushed into a 63 percent income tax bracket while the wealthy would move into a 88 percent bracket[5]—and even that assumes health care cost growth slows down. And allowing the 2001 and 2003 tax cuts to expire—including those that currently benefit low-income families—would close just one-tenth of the long-term gap.

Drowning this nation's children in tax hikes is no better than drowning them in debt. Steep tax rate increases—or a new value-added tax—would devastate families, businesses, and the economy. And politicians would likely spend any new tax revenues rather than allocate them to deficit reduction. Rather than simply raise taxes alongside rising spending, the deficit commission should pare back the burgeoning spending programs.

Bring Budget Transparency. Social Security and Medicare face a staggering $46 trillion in unfunded obligations over the next 75 years. Yet those figures appear nowhere in the budget that Congress must

1. Lori Montgomery, "Deficit Commission Has a Name, a Phone Number and a Few Dates," *The Washington Post*, April 23, 2010, at *http://voices.washingtonpost.com/44/2010/04/deficit-commission-has-a-name.html* (April 27, 2010).
2. This "current policy" baseline assumes the 2001/2003 tax cuts are extended, the Alternative Minimum Tax continues to be patched, discretionary spending grows with the economy, war spending winds down, and the Medicare "doc fix" continues. It is based on data in Congressional Budget Office, "The Budget and Economic Outlook: Fiscal Years 2010 to 2020," January 2010, at *http://www.cbo.gov/ftpdocs/108xx/doc10871/BudgetOutlook2010_Jan.cfm* (April 27, 2010).
3. See Brian M. Riedl, "A Guide to Fixing Social Security, Medicare, and Medicaid," Heritage Foundation *Backgrounder* No. 2114, March 11, 2008, at *http://www.heritage.org/Research/Budget/bg2114.cfm.*
4. Congressional Budget Office, "H.R. 4872, Reconciliation Act of 2010 (Final Health Care Legislation)," March 20, 2010, at *http://www.cbo.gov/ftpdocs/113xx/doc11379/Manager'sAmendmenttoReconciliationProposal.pdf* (April 27, 2010).
5. Peter R. Orszag, Director, Congressional Budget Office, letter to Representative Paul Ryan (R–WI), May 19, 2008, at *http://www.cbo.gov/ftpdocs/92xx/doc9216/05-19-LongtermBudget_Letter-to-Ryan.pdf* (April 27, 2010).

approve annually. The commission should require that Congress disclose all unfunded obligations in its annual budget and vote to acknowledge and approve the long-term consequences of their budget decisions. In addition, they should require that new proposals be scored over the long-term (instead of just the next 10 years) and create a long-term budget for entitlement programs.

Standing Up for Future Generations. Unless lawmakers promptly reform Social Security, Medicare, and Medicaid, America faces a future of soaring taxes and government spending that will devastate the economy. Americans will pay onerous taxes, and future generations will have lower living standards than Americans enjoy today. And the longer lawmakers wait to enact the necessary reforms, the more painful those reforms will be.

If the deficit commission calls for finally reforming these entitlement programs, it can promote economic growth while helping to prevent the largest intergenerational transfer of wealth in world history. If the commission instead endorses steep tax increases on future generations combined with spending gimmicks, it will represent another lost opportunity.

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