The Heritage Foundation
LEADERSHIP FOR AMERICA

ISSUE BRIEF

No. 4085 | NOVEMBER 12, 2013

Principles for the Budget Conference

Derrick Morgan, Rea S. Hederman Jr., Nina Owcharenko, and Romina Boccia

For the first time in years, lawmakers have agreed to convene in a budget conference to reconcile differences between their respective budget proposals, as presented by House Budget Committee chair Paul Ryan (R–WI) and Senate Budget Committee chair Patty Murray (D–WA). The two chambers' budgets differ wildly in terms of taxes and the size of government.

A budget conference presents a rare opportunity to address the U.S. government's key fiscal challenges. During this process, it is important to recognize some key principles that are necessary for a good outcome and for a prosperous American future. However, no deal is far preferable to a bad deal.

Leave Tax Reform on Its Own Course. The budget passed by the Senate calls for a trillion dollars of tax increases over the next 10 years. This budget ignores the fact that Washington has already raised taxes by a more than $3 trillion by enacting Obamacare, ending some of the pro-growth Bush tax cuts, and allowing the payroll tax cut to expire.

President Obama's latest budget wants even more taxes, with each dollar in spending reductions paired with $7 in tax increases. President Obama's tax increases have already increased the top tax rate on wages to the highest level in 30 years.[1]

This paper, in its entirety, can be found at **http://report.heritage.org/ib4085**

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

The Heritage Foundation
214 Massachusetts Avenue, NE
Washington, DC 20002
(202) 546-4400 | heritage.org

Furthermore, President Obama's tax increases have damaged an already fragile economy. Academic research has reached a consensus that tax increases are harmful to the economy.[2] This year, taxes went up by approximately $188 billion compared to a reduction in spending authority of $85 billion. Sadly the President and Congress chose twice as many tax increases as spending cuts, doubling down on bad economic policy.

Not only should tax increases be left out of the conference; so should other changes to tax policy. The budget conference needs to spend its limited time working on vital spending reforms. Time spent on taxes would be a distraction from that necessary work.

That includes tax reform. There is no doubt that tax reform is desperately needed to revive the economy, but the budget conference is the wrong place to pursue it. Not only would it distract from spending reform, but the conference would likely do more harm than good if it binds tax-writing committees to a fast-track time line to finish tax reform legislation. By cutting time short, a fast-track procedure would likely bypass the important work done by the Ways and Means and Senate Finance committees that is essential to crafting a workable tax reform package.[3]

Address Future Debt. Entitlement spending is rapidly growing to dangerous levels. Despite more than $48 trillion in unfunded obligations and repeated warnings by the Social Security and Medicare trustees about the problems with these existing entitlements, brand new entitlements in Obamacare are set to take root in 2014. The first order of business for budget conferees should be to stop the unaffordable subsidies and Medicaid expansion of Obamacare.

The major entitlements—Medicare, Social Security, and Medicaid, and Obamacare health exchange subsidies—are the key drivers of spending and debt. Social Security and Medicare are the two largest government programs, and their growth rate is exploding in large part because the nation is confronted with the retirement of the baby-boom generation. But Medicaid is also expanding quickly and is further fueled by the Obamacare Medicaid expansion. In only 10 years, Social Security, Medicare, and Medicaid will devour almost half of the federal budget.

The conferees' focus should be on making a sizable down payment toward the nation's fundamental fiscal challenges through basic entitlement reforms.

Stick to the Budget Control Act. Sequestration was included in the Budget Control Act (BCA) to force lawmakers to agree to additional deficit-reduction measures, including in entitlement spending. Nevertheless, the super committee squandered the opportunity to address the key drivers of spending and debt before sequestration kicked in.

Sequestration targeted the defense discretionary budget for half the cuts and domestic discretionary and mandatory spending for the other half. Proportionally, defense took a bigger hit. And, save for a small reduction in Medicare, the entitlements went basically untouched.

Since then, lawmakers have raised taxes by more than $3 trillion, while entitlement spending continues growing out of control.

To honor the original intent of sequestration, conferees should recommend programmatic or structural reforms to control the growth in entitlement spending. To be considered in any deal, these reforms should lock in immediately to reduce spending significantly within the 10-year budget window and beyond.

Enforce Lower Levels of Spending. Lawmakers are already wrangling over how to undo the BCA's modest spending cuts. While Congress should restore needed defense capabilities and resources, it should not enact spending that exceeds the BCA's reasonable spending limits overall in the process.

Except for substantive structural reforms to curb the growth in spending from Social Security, Medicare, or Medicaid, conferees should stay away from trading the sure savings in the BCA in exchange for uncertain savings in the future. Since no Congress can bind the actions of a future Congress, future spending reductions can be erased and are therefore less valuable than savings already in law and taking effect.

There is also a time value to money. Just as no lender would give out a dollar today in exchange for just one dollar in 10 years, budget savings today are much more valuable than potential savings in later years. An example of an unacceptable trade would be one that counts savings over 10 years from a bill such as the farm bill, which is reviewed periodically already, in exchange for higher spending in 2014.

Do Not Play Inside-the-Beltway Games. In the back rooms of budget conferences, lawmakers often fall prey to using budget gimmicks. Lawmakers already set a bad precedent in December 2012 when they delayed the impact of sequestration through a timing shift, pulling revenues from outside the 10-year budget window to count as savings.

Other common gimmicks, extensively used in the President's budget, leverage the baseline to count war savings that were never intended to be spent or cancel estimated disaster and emergency-related spending. The Medicare sustainable growth rate, which ends up canceled through a "doc fix" every year or so, is another example of falling for a spending cut that is unlikely to materialize. Congress should not allow these types of tricks to emerge from the budget conference.

No Deal Better Than a Bad Deal. The budget conference offers a chance for real fiscal reform. Lawmakers can address the rapid growth in the entitlements that will threaten economic performance and eliminate wasteful and ineffective programs.

However, zeal for a deal should not result in a budget agreement that is worse for taxpayers and the economy. No budget agreement at all would be

1. Curtis S. Dubay, "Fiscal Cliff Deal: Tax Increase Spoils Permanent Victory for Most Taxpayers," Heritage Foundation *Issue Brief* No. 3821, January 9, 2013, http://www.heritage.org/research/reports/2013/01/fiscal-cliff-deal-how-it-will-affect-taxpayers-and-the-economy.
2. Salim Furth, ed. "Europe's Fiscal Crisis Revealed: In-Depth Analysis of Spending, Austerity, and Growth," Heritage Foundation *Working Paper* No. 10-13, October 24, 2013, http://www.heritage.org/research/reports/2013/10/europes-fiscal-crisis-revealed-indepth-analysis-of-spending-austerity-and-growth.
3. Curtis S. Dubay, "Leave Tax Reform and Tax Increases Out of Budget Conference," Heritage Foundation *Issue Brief* No. 4074, October 29, 2013, http://www.heritage.org/research/reports/2013/10/leave-tax-reform-and-tax-increases-out-of-budget-conference.

better than one that would result in more immediate spending in return for promises of long-term reforms that would never materialize.

*—**Derrick Morgan** is Vice President for Domestic and Economic Policy, **Rea S. Hederman Jr.** is Director of the Center for Data Analysis and Lazof Family Fellow, **Nina Owcharenko** is Director of the Center for Health Policy Studies and Preston A. Wells Jr. Fellow, and **Romina Boccia** is Grover M. Hermann Fellow in Federal Budgetary Affairs at The Heritage Foundation.*