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PROPOSAL WOULD REQUIRE CBO TO LOWER THE BASELINE FOR DISCRETIONARY PROGRAMS BY $1 TRILLION OVER THE NEXT TEN YEARS

By Robert Greenstein, Joel Friedman and Magda Cojanu

When the House considers budget-process legislation the week of June 21 or soon thereafter, it is expected to consider a proposal to require that the budget "baseline" for discretionary programs be lowered by more than $1 trillion over the next ten years. This proposal is contained in H.R. 3800, introduced by Rep. Jeb Hensarling and more than 100 co-sponsors, and in H.R. 3925, introduced by Rep. Mark Kirk and about 20 co-sponsors. It is likely to be included in amendments that Reps. Hensarling, Kirk, or others offer on the House floor.

The proposal would have this effect because it would require that the baseline equal the current year's funding levels with *no* adjustment for inflation, repealing a longstanding part of federal budget law and practice. For the past 30 years, CBO and OMB have taken inflation into account in developing their budget baseline estimates. As a result, the baseline for appropriated programs has been set equal to the funding levels for these programs in the current year, adjusted for inflation. CBO and Members of Congress have long recognized that adjusting for inflation is necessary if programs ranging from defense to health research to child care to protecting the borders are to maintain the same level of services from year to year. This is the case because the salaries and health benefits for military and civilian personnel — and the costs of the goods and services purchased through these programs — rise over time with inflation.

This proposal to end inflation adjustments in the baseline, requiring CBO to assume a hard freeze for discretionary programs for ten straight years, is ill-advised. Adjusting a program's funding level to keep pace with inflation does *not* mean the program is expanding, serving more people, or providing richer benefits or services. Compensating for the effects of inflation simply reflects the basic reality that the cost of delivering government-funded services rises with inflation, just as the cost of providing services in the private sector does. Costs for the salaries and benefits of those who deliver these services rise with inflation. So do the costs of materials, supplies, and other goods and services purchased through government programs.

Indeed, some budget experts, such as Urban Institute president and former CBO director Robert Reischauer, have argued that adjusting domestic discretionary programs for both inflation *and population growth* would provide a better estimate than the current inflation-only adjustment of what it costs to provide the same level of services over time. And George W. Bush, as a Presidential candidate, made the same point, arguing that an "honest comparison" of the rate of spending growth in Texas during his tenure as governor must adjust for both inflation and population growth.[1]

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[1] *Dallas Morning News*, October 28, 1999.

Effects of the Proposal

Even with the low average inflation rate of 2.4 percent per year that CBO currently projects, a baseline with no adjustment for inflation would assume deep reductions over time in the levels of services that discretionary programs provide.

- The baseline for discretionary spending would be *$1.1 trillion lower* over the next ten years than current baseline levels, according to CBO. The reduction in the baseline would be $227 billion in 2014 alone. These reductions in the baseline would apply to *all* discretionary programs — defense, homeland security, domestic, and international.

Discretionary Spending in CBO Baselines
(in billions of dollars)

	2014	2005-2014
CBO discretionary baseline:		
--with inflation	1,150	10,364
--without inflation	923	9,246
Difference	**-227**	**-1,118**

Source: CBO March 2004 baseline.

- Discretionary spending would be *19.7 percent lower* after ten years, compared with the current baseline. These lower spending levels would reflect sharp cuts in the services that discretionary programs provide (see box on page 3).

- Expenditures for defense and nondefense discretionary programs now equal 7.8 percent of GDP. Under this proposal, the baseline would show discretionary spending plummeting to 5.1 percent of GDP by 2014. At 5.1 percent of GDP, discretionary programs would be at their lowest level, measured as a share of the economy, since at least 1962 (the first year for which complete data are available) and probably since the Hoover Administration.

  By comparison, this reduction of 2.7 percent of GDP would be greater than the entire increase in Social Security costs measured as a share of GDP that both the Social Security actuaries and CBO project over the next 75 years.

Proposed Change Could Affect Budget Debates and Decisions

If this proposal is adopted and a "freeze baseline" becomes the official benchmark for measuring the impact of policy proposals, efforts simply to keep funding for discretionary programs in line with inflation will be portrayed as increasing costs and enlarging government, despite the fact that doing so would merely maintain services at their current levels. Even proposals to set discretionary funding well *below* the levels needed to keep pace with inflation but modestly above a freeze level — which would require cuts in services over time — will be portrayed as expanding government and increasing spending. Similarly, long-term freezes that entail deep cutbacks in services will be portrayed as *not* being cuts.

A Ten-year Freeze Would Sharply Curtail Services Provided By Discretionary Programs

The Congressional Budget Office estimates that if discretionary funding were frozen at the current level for ten years, discretionary programs would be reduced overall by about one-fifth in 2014, compared to the levels reflected in the current, inflation-adjusted CBO baseline.* At these lower funding levels, services provided by important discretionary programs would have to be cut substantially.

- **Women, Infants and Children (WIC) nutrition program:** The WIC program provides a package of specific nutritious foods, nutrition counseling, and health care referrals to low-income pregnant women and low-income mothers and their young children. The cost of providing these services rises as food prices increase and as the salaries of dieticians and other staff rise with inflation. If funding for the WIC program were frozen for ten years, funding in 2014 would be $867 million below the level in the current CBO baseline. At this lower funding level, the program would serve an estimated *one million fewer women and children* than would be served under current baseline levels.

- **Head Start:** The Head Start program provides early childhood education for preschool children as well as some infants and toddlers. The cost of Head Start rises as inflation raises teachers' wages and salaries, the cost of materials, and the cost of renting or maintaining facilities. If Head Start funding were frozen, funding in 2014 would be $1.3 billion below the current baseline level, and an estimated *134,000 fewer children* would be served by the program at this freeze level than at the inflation-adjusted level.

- **National Institutes of Health:** The cost of conducting research at the National Institutes of Health rises with the wages and salaries of researchers and the cost of medical technology and procedures. If the NIH budget were frozen at the current level, funding in 2014 would be $5.7 billion below the level needed to maintain the inflation-adjusted 2004 level, a 17 percent cut in real funding. At this level, NIH would have to cut back substantially the research that it supports.

- **Education for the Disadvantaged:** Title I of the Elementary and Secondary Education Act provides funding for school districts to improve educational outcomes for low-income and other disadvantaged children. If funding for this program were frozen at current levels, by 2014 funding would fall $2.6 billion, or 17 percent, below the level needed to support the programs and services now being funded through this program.

- **National Resources and Environment:** This is a broad grouping of programs related to environmental protection, national parks, and the management of the nation's land, water, and mineral resources. If funding for these programs were frozen, funding in 2014 would fall $8.7 billion, or 22 percent, below the level needed to continue current programs and services.

*Although the overall reduction is 19.7 percent in 2014, the exact percentage reductions for individual programs would vary somewhat depending on the proportion of spending in each program on federal employee salaries and benefits. This variation would reflect the different inflation-adjustment measures that CBO uses for personnel versus other types of spending.

This portrayal of discretionary spending — which reflects the type of presentation of budget trends that various arch-conservative organizations have long advocated — would acquire an official sanction and, as a result, likely be echoed in the media. Over time, such presentations almost certainly would have an effect on politics and policy, making it more difficult to fund discretionary programs adequately and likely leading to damaging cuts in valuable programs over time.

Change Also Could Facilitate Unaffordable Tax Cuts and Entitlement Expansions

The proposal also has another drawback. A baseline that assumes a discretionary freeze for an entire decade would result in projections of discretionary spending that are unrealistically low, and hence would result in rosy budget forecasts that understate the size of the deficit. Funding for defense, veterans health care, cancer research, homeland security, and various other programs and government functions is not going to be frozen for ten years. (Only once in the last four decades has overall discretionary spending been frozen for as many as *five* years, and that occurred after the collapse of the Soviet Union when defense spending was declining markedly.)

A baseline that assumes that defense and nondefense discretionary programs will be frozen for ten consecutive years consequently will understate the level of discretionary spending in coming years and result in official budget baselines that picture budget deficits as being smaller than they actually will be. Compared with the current baseline, a baseline that assumed a freeze in discretionary spending would show deficits that were $1.3 trillion lower over the next ten years (reflecting both lower estimates of discretionary spending and the lower interest payments on the debt that would result from the lower deficits that would be assumed).

Institutions such as the Concord Coalition, the business-backed Committee for Economic Development, Goldman-Sachs, and the Brookings Institution, among others, have persuasively argued that CBO's *current* ten-year deficit projections are already unrealistically low because the baseline assumes that all of the tax cuts enacted since 2001 will expire and that the Alternative Minimum Tax will be allowed to mushroom. The CBO projections will become even more divorced from reality if CBO is forced to assume that discretionary programs will be frozen at their current levels for ten straight years.

The resulting projections of smaller budget deficits could prove to be dangerous. By making deficits look lower than they are likely to be, these projections could create a false sense of security and help pave the way for new rounds of tax cuts or entitlement expansions, on the grounds that such costs are now affordable. It may be recalled that in 2001, budget forecasts that were too rosy paved the way for fiscal profligacy. There is risk that under this proposal, history could repeat itself.

Conclusion

The proposal has two distinct drawbacks. First, it would skew budget debates by making the adjustments that are needed simply to keep pace with inflation look like enlargements of the federal government. The proposal consequently would be likely to lead to significant cuts in services over time.

Even so — and this is the second drawback — it is inconceivable that the cuts would be so large as to actually freeze overall appropriations for ten straight years or come close to it. As a result, the baseline would present an overly rosy scenario that would understate discretionary spending levels and thereby make projected deficits look artificially low. These seemingly more manageable deficits, in turn, could lull policymakers into taking less seriously the fiscal problems that lie ahead and could foster a continuation of fiscally irresponsible policies.