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Automatic Reconciliation an Undesirable Part of Enzi-Whitehouse Budget Process Bill

Could Drive Harmful Budget Cuts, Unsound Economic Policy

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The Senate Budget Committee is scheduled to consider legislation this week from Chairman Mike Enzi and Committee member Sheldon Whitehouse that would alter the congressional budget process in highly problematic ways. Although the bill includes positive elements (see the box on page 2), it also includes a significant land mine — a requirement that Congress craft and consider deficit-reduction legislation under highly expedited "reconciliation" procedures if the Congressional Budget Office (CBO) finds that the debt projection for the final year that the congressional budget resolution covers (e.g., the tenth year of the ten-year budget resolution that Congress adopted the previous year) is higher than that reflected in the budget resolution. That finding is very likely, history shows, and it could drive deep cuts in mandatory programs such as Medicare, Medicaid, health insurance subsidies, SNAP, and Supplemental Security Income (SSI) — and at a time when the economy is weak, thus making the economy still weaker.

Enzi-Whitehouse (S. 2765) would shift the congressional budget resolution from an annual document to one that covers two years. Under the bill, Congress would approve a budget resolution in the first year of a two-year session. Then, on February 15 of the second year, CBO would calculate whether the debt ratio — the debt held by the public as a share of the economy (gross domestic product, or GDP) — for the final year of the budget resolution would exceed the debt ratio projected for that year in the budget resolution that Congress adopted a year earlier. Such a CBO calculation would trigger a new, *automatic* deficit-reduction process. That new, automatic process would be even more expedited than the current reconciliation process on which it's modeled, though it also differs from that process in crucial ways and has major flaws.

Tying reconciliation to debt estimates that can vary widely from year to year is ill-advised fiscal policy for several reasons. It likely would drive the public debate toward hitting an ever-moving debt-ratio figure and away from using the budget to address key national issues. Most worrisome, the new, automatic deficit-reduction process would likely increase the chances that policymakers would make budget cuts (thus, imposing austerity) at times when the economy is weak or in recession, which would further weaken the economy. In addition, the new process would confer sweeping new powers on the Senate Budget Committee while weakening the Senate as a whole — and its authorizing committees in particular — in developing important fiscal policies.[1]

Enzi-Whitehouse also would retain the existing reconciliation process, prompting the question of why a second one is needed.

Enzi-Whitehouse Also Has Positive Elements

Some elements of Enzi-Whitehouse could prove helpful, most notably a provision that could reduce dangerous brinksmanship around raising the statutory debt limit. The bill provides that, if Congress agrees to a budget resolution, legislation raising the debt limit to the level in that resolution would be deemed to have passed Congress and go directly to the President, avoiding separate House and Senate votes solely on the debt limit. Known as the "Gephardt procedure" (after the former Democratic Majority Leader who spearheaded a similar rule in the House), this provision would substantially reduce the risk of a harmful federal default and of artificial crises in which a minority can threaten to force a default to obtain concessions on other issues. An even better approach would be to repeal the debt limit (see https://www.cbpp.org/blog/the-debt-ceiling-scrap-it-or-adopt-the-danes-great-approach) or, as a fallback, to suspend the debt limit for the duration of the time that an approved budget resolution is in effect.

The bill also would move budget resolutions to a biennial schedule, which could be a more realistic approach to designing budget plans, while retaining the role of annual appropriations bills to fund the government on an annual basis.

Reconciliation Should Not Be Tied to Uncertain Budget Projections

The process that would trigger a new, automatic reconciliation process could force budget cuts that are disconnected from a solid policy rationale. The projected final-year debt ratio might exceed the level projected in the budget resolution:

- Because, even though the debt ratio is falling, it's not falling as fast as the budget resolution assumed; or
- Because Congress rejected a deficit-reduction plan of spending cuts and/or tax increases the previous year or the President vetoed it; or
- Because the Federal Reserve set interest rates somewhat higher than the budget resolution had assumed, increasing interest costs and thereby leading to higher deficits and debt; or
- Because of purely technical reasons related to underlying demographic and other assumptions about current-law spending and revenue levels, unrelated to any changes in policies that affect projected deficits. Stated another way, even if Congress made every change in spending and tax policy assumed in its budget resolution, CBO might still subsequently project a final-year debt-ratio level higher than the level that the budget resolution projected for that year.[2]

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[1] Although the bill proposes changes to the entire congressional budget process, it addresses only Senate procedures. The Senate sponsors of this legislation presumably expect that the House would add parallel House procedures if it were to consider the bill.

[2] Also see the Appendix.

What programs are at risk? Congress can use reconciliation to change revenue and mandatory programs, except Social Security. The largest mandatory programs, more or less in order, are Medicare, Medicaid and the Children's Health Insurance Program (CHIP), refundable tax credits (Earned Income Tax Credit, the Child Tax Credit, and the Affordable Care Act's premium tax credits), civil service retirement, veterans' compensation and pensions, SNAP, military retirement, SSI, family support and foster care, farm supports and crop insurance, and child nutrition.

(Note: Policymakers cannot change Social Security in a reconciliation bill. The level of debt held by the public, however, is driven by the entire budget, including Social Security, even though Social Security is designated by law an "off-budget federal agency." Therefore, debt ratio projections also will vary from earlier expectations if Social Security cost or revenue projections change. As a result, under auto-reconciliation, *other* mandatory programs may have to be cut to make up for, say, a decrease in projected Social Security revenues.)

Of major concern, the media and the public may interpret a CBO finding that the projected debt ratio for the final year will be exceeded as an official, non-partisan determination that Congress didn't meet its budget commitments, and that policymakers now should reduce the deficit by the excess amount that CBO calculates. The bill gives the Senate Budget Committee authority to set a different amount of deficit reduction (smaller or larger) than CBO projects. But the media and public will logically presume that the CBO estimate would be the most appropriate amount. Furthermore, they will presume that policymakers need to reduce the deficit even if current economic circumstances suggest the opposite, as discussed below.

Effect of the Automatic Process if Applied to Past Budgets

Were this process in place for the last four budget resolutions that Congress adopted, for fiscal years 2010, 2016, 2017, and 2018,[3] *the last three* would have generated a CBO calculation projecting a tenth-year debt ratio above those in the budget resolutions, thereby *triggering the auto-reconciliation process in each case.*[4]

Under Enzi-Whitehouse, CBO is also required to estimate the size of the policy savings — mandatory program cuts or revenue increases — needed over the multi-year period of a budget resolution to hit its final-year debt ratios.[5] Those CBO reports would have shown the following amounts of budget cuts for a ten-year auto-reconciliation bill: $3.0 trillion for the 2018 budget resolution; $1.0 trillion for the 2017 budget resolution; and $5.5 trillion for the 2016 budget resolution.

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[3] Both the 2017 and the 2018 budget resolutions were created and agreed to in calendar year 2017. One might say that Congress agreed to two budget resolutions for fiscal year 2018. The first created a reconciliation process intended to repeal the Affordable Care Act, though that failed. The second created a reconciliation process to enact the 2017 tax cuts. As a result, with respect to each of those two budget resolutions, the CBO debt-ratio calculation would (under Enzi-Whitehouse) have occurred in February 2018 and used the same CBO baseline.

[4] The 2010 resolution, in contrast, would have generated a CBO calculation projecting a lower fifth-year debt ratio than in that five-year budget resolution, and so would not have triggered the auto-reconciliation process.

[5] Existing law does not require the assumed level of GDP to be shown in budget resolutions, and it has not been. Our calculations are made under the understanding that the budget resolution in question had relied on the GDP levels projected by CBO in applicable baselines.

The 2018 budget resolution is particularly instructive. It paved the way for the 2017 tax cut legislation, which increased the deficit by an estimated $1.9 trillion over ten years.[6] Under Enzi-Whitehouse, CBO would have estimated two months after policymakers enacted the tax cuts that the debt ratio in the resolution was being exceeded, and that $3.0 trillion of deficit reduction would be required to meet that ratio.[7] That would have triggered the automatic process to reduce the deficit. In designing a deficit-reduction package, the Republican majority surely would have protected the new tax cuts, instead designing a package solely of cuts to mandatory programs — an approach that would have exacerbated the inequities in the new tax law, which provided the overwhelming share of its tax cuts to the nation's wealthiest households and most profitable corporations.[8]

Moreover, even though CBO's projections are highly credible, they are — like all budget projections — subject to substantial variation that, under Enzi-Whitehouse, could trigger the automatic deficit-reduction process. CBO recently assessed its past projections of deficits and debt,[9] measuring the accuracy of each of its five-year debt projections since 1984, excluding the effects of legislation. While that's not the same calculation that Enzi-Whitehouse would require, it highlights the impact of shifting economic and technical estimating assumptions. Although CBO found little or no bias in its projections, some projections were far too high and some were far too low. *Its fifth-year debt projections missed the mark by an average of 7.1 percent of GDP*. Five years from now, that would equal $1.8 trillion. And ten-year projections would have been off by substantially larger amounts. Nevertheless, CBO found that, since 1984, its multi-year economic forecasts have been as good as the forecasts of the Office of Management and Budget or the Blue Chip consensus, showing that *all* such forecasts are inherently uncertain.

Automatic Austerity Is Unsound Economic Policy

Most worrisome, the final-year debt ratio in a budget resolution might be exceeded mainly, if not exclusively, because the expected pace of future economic growth slowed in the year after Congress adopted the budget resolution. *Periods of slower economic growth are exactly the wrong time to enact new budget cuts because they would make a weak economy still weaker and make recessions that are underway deeper*.

Potentially, the Senate Budget Committee could address this challenge in three ways, but none seems realistic:

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6 "2017 Tax Law Is Fundamentally Flawed," Center on Budget and Policy Priorities, updated, October 31, 2018, https://www.cbpp.org/research/federal-tax/2017-tax-law-is-fundamentally-flawed.

7 The figure of $3.0 trillion over ten years occurs because the tax cut was supposed to cost $1.5 trillion over ten years, not $1.9 trillion, and the budget resolution assumed deep specified and unspecified cuts to mandatory programs that were not enacted (nor did the budget resolution use the standard reconciliation process to attempt to enact them).

8 The 2017 budget resolution is also instructive because that resolution was publicly referred to as a "shell," so its dollar figures incorporated no assumed changes in policy, merely reflecting levels virtually identical to those in CBO's baseline. (It was designed purely as a vehicle to allow Congress to use the reconciliation process — and thereby avoid the Senate filibuster — to try to repeal the Affordable Care Act.) Yet even with no assumed deficit reduction, CBO's 2018 calculation would have shown that the debt ratio would have exceeded the 10th-year level in the budget resolution for economic and technical reasons, triggering a reconciliation process to achieve $1.0 trillion in deficit reduction.

9 Congressional Budget Office, An Evaluation of CBO's Past Deficit and Debt Projections, https://www.cbo.gov/publication/55234, September 11, 2019.

- First, the Committee could set the final-year debt ratio in the budget resolution much higher than anticipated given its policy, economic, and technical assumptions,[10] thereby reducing the risk that CBO will calculate in the following year that the debt ratio would be breached. But setting higher levels of debt in the budget resolution seems quite unlikely; indeed, the far likelier scenario, given the history of recent budget resolutions, is that Congress will be *overly optimistic* in its "out-year" projections in order to make the debt problem seem less serious than it is — thereby increasing the chances that a large, economically ill-advised deficit-reduction package would be triggered as the economy is slowing.
- Second, if the final-year debt ratio is on track to be breached, the Committee could ignore the CBO estimate of the amount of deficit reduction needed to hit the assumed debt-ratio level and instead set a very low auto-reconciliation deficit-reduction target, such as $1. But deficit "hawks" would almost certainly deride such an approach as irresponsible gimmickry, even when it would be the most prudent economic policy. The public debate would likely fixate on reports about gimmickry, when instead it should focus on whether (or how much) economic stimulus (tax cuts and/or spending increases) policymakers should enact to strengthen a weakening economy, or at least the degree to which austerity would harm a weakening economy.
- If the committee does decide to require deficit reduction in the full amount that CBO estimates at a time when the economy is weak, it might include year-by-year deficit reduction targets rather than just a single total over the entire multi-year period. And if so, it should call for all the deficit reduction to occur at the tail end of the period, when the economy might have fully recovered.

As a result, this aspect of Enzi-Whitehouse represents unsound economic policy. Indeed, policymakers ought to amend the budget process to *increase* Congress' tools to make appropriate fiscal policy when the economy weakens, rather than establishing automatic processes that can push Congress to make ill-advised policy — and Congress to have to circumvent those processes to make sound fiscal policy when the economy falters.

New Process Concentrates Power and Is Less Transparent

This new automatic deficit-reduction process would also give the Senate Budget Committee sweeping new powers.[11] When triggered, this auto-reconciliation process would let the committee *unilaterally decide how much deficit reduction to mandate and which Senate committees would be required to cut programs* (or, in the case of the Finance Committee, raise revenues). Further, if any Senate committee fell short of its target, the Budget Committee would have the authority to increase that committee's cuts or draft new ones to meet the target, and those proposals would be included in the auto-reconciliation bill that goes to the full Senate.

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[10] There is no requirement under existing budget law or in the Enzi-Whitehouse proposal that the level of debt in a budget resolution be consistent with the level of deficits in the resolution.

[11] The Enzi-Whitehouse bill would make the chair and ranking member of the Senate Appropriations Committee and the Senate Finance Committee *ex officio*, non-voting members of the Budget Committee.

The auto-reconciliation process would continue to a final vote on the reconciliation bill, giving the Senate as a whole no chance to first vote on whether it wanted to proceed; no chance to amend the size of the auto-reconciliation package; and no chance to amend the distribution of cuts among the other Senate committees. And when the auto-reconciliation bill reached the floor, reducing the budget cuts would violate the new rules.

Thus, every aspect of the process — from the size of the cuts to their allocation by committee to the drafting of the cuts themselves — would be driven by Senate Budget Committee decisions rather than by the whole Senate. In contrast, under current reconciliation procedures, reconciliation directives are included in the budget resolution that Congress must debate and approve before lawmakers take further action.

Further, with such unprecedented authority for the Senate Budget Committee under the new reconciliation process, transparency around budget decision-making will likely shrink. That's because the public will receive less information due to the media's more limited coverage of committee action than of Senate floor deliberations. Thus, the public, which already struggles to understand the congressional budget process, will likely receive less information about how Congress is making key budget decisions.

Conclusion

The question of what's sound budget policy should not be driven by a presumption that austerity is always the right answer, nor by a mechanical calculation that could trigger austerity at the wrong time in an economic cycle. Finally, budget policymaking should be transparent and inclusive and should not be driven by uncertain projections of a moving target that may not indicate whether Congress is actually adhering to the budget policies it has set for itself.

Appendix

In this analysis we discuss reasons why CBO might subsequently project that the debt ratio for the final year covered by a budget resolution that Congress approved the previous year might be higher than the resolution had assumed, triggering the automatic reconciliation process. There is an additional reason: in measuring the debt ratio, the Enzi-Whitehouse proposal relies on the federal government's standard measure of its debt, which doesn't fully account for the government's financial position and could actually trigger the automatic reconciliation process even when *no* deterioration in the government's position has occurred, and in some cases, even if deficits now are expected to be lower than the budget resolution assumed.

Here's why:

The proposed automatic reconciliation process focuses on the estimates of "debt held by the public" — the debt from government borrowing in the credit markets — that are shown in the final year of a budget resolution (e.g., the tenth year of a ten-year resolution). Debt rises whenever the federal government runs a deficit, so a budget resolution with a decade of deficits will increase the debt by the sum of those ten deficits. But the federal government also has financial assets, such as cash, gold, and direct loan assets, that somewhat offset the debt.

Suppose, for example, that the Treasury Department borrows more money solely to build up its cash reserves that have fallen dangerously low, threatening its ability to pay federal bills on time. In that case:

- the federal government's financial position would be unchanged; the debt would be higher, but the increase in debt would be offset dollar for dollar by an increase in cash; and
- the additional borrowing would *not* show up on the federal books either as an increase in spending or an increase in deficits.

So sometimes an increase in debt doesn't reflect any deterioration in the government's financial position. That is, the growth of debt over some period of time is often *not* simply the sum of deficits over that period. Debt can grow significantly more or less than the sum of deficits. In 2015, in fact, the deficit was $442 billion but the debt rose by only $337 billion. In 2016, by contrast, the deficit was $585 billion but the debt rose by $1.1 trillion.

As CBO has written, "Other factors — collectively labeled 'other means of financing' and not directly included in the budget totals — also affect the government's debt. Those factors include the cash flows associated with federal credit programs, such as student loans, as well as changes in the government's cash balances."

Now, let's look more closely at student loans, which highlight the potentially large policy implications of the automatic reconciliation process. Over the ten years from 2008 through 2017, federal deficits totaled $8.4 trillion. Over the same period, however, debt held by the public grew by $9.6 trillion. The overwhelming reason for the $1.2 trillion difference was the government's 2010 conversion of the federal student loan program from loan guarantees to direct loans. Under the loan guarantee program, the financing took place *off* the government's books, with banks lending money to students, the students paying back the banks over time, and the government responsible for defaults. Under the direct loan program, the financing takes place *on* the government's books: the Treasury borrows from the credit markets and lends the money to students. The government's costs over time are *essentially the same either way,* arising from defaults — *but with direct loans, the government's books show higher debt because the government borrowed from the credit markets to finance direct loans, and the books also show corresponding larger financial assets*, which are the value of those direct loans to the government.

The Enzi-Whitehouse automatic reconciliation trigger accounts for only half of such transactions (the government's additional borrowing), while missing the other half (the government's acquisition of direct loan assets, when students repay the government). Such accounting would have missed more than $1 trillion in student loan assets that the government acquired.[12] Indeed, when CBO estimated the budgetary effects of the 2010 conversion from guaranteed to direct loans, it concluded that the legislation would *reduce spending and deficits in every year even though it would increase debt held by the public.*

This aspect of Enzi-Whitehouse could prompt Congress to favor loan guarantees over direct loans, even when the former produce modestly higher deficits over time by requiring extra government payments to banks to induce banks to participate in the program.

[12] The government values direct loan assets by accounting for not just the principal amount of the direct loan, but also the extent to which the interest rates it charges are above or below Treasury interest rates, the extent to which the portfolio of loans is likely to suffer from defaults (since some defaults are inevitable), and the extent to which defaults can be partially offset by, for example, garnishing later tax refunds.