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# FIVE-YEAR DISCRETIONARY CAPS WOULD BE UNWISE AT THIS TIME
## Proposed Caps Would Lead to Overly Deep Cuts and Could Hinder Enactment of Large-scale Deficit Reduction

by Robert Greenstein, Richard Kogan, and James Horney

The President has again proposed enactment of binding caps for each of the next five years on overall levels of funding and expenditures for discretionary programs (i.e., programs that are non-entitlements). Under the proposal, the cap for each fiscal year through 2011 would be set at the overall levels for discretionary programs proposed for that year in the budget that the President submitted to Congress in February. The Republican Study Committee, a group that includes many of the most conservative members of the House of Representatives, also has proposed caps on discretionary programs for the next five years, at levels equal to the discretionary funding levels contained in the RSC's budget plan.

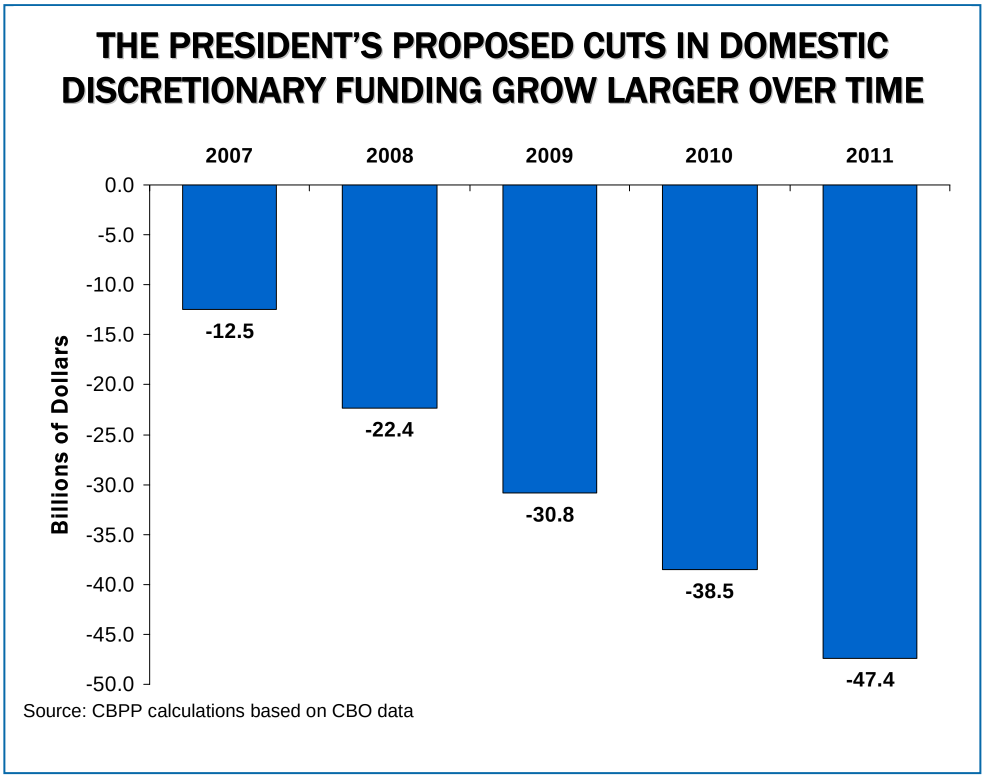
The House and Senate Republican leaderships have pledged that their respective bodies will consider budget process legislation sometime in the next few months. Caps on discretionary programs may be considered for inclusion in that legislation.

Although discretionary caps could be set at whatever level is agreed to when legislation establishing such caps is considered, this analysis uses for illustrative purposes the levels proposed in the President's budget. (The levels proposed by the RSC would be lower than these amounts.) It is worth noting that the overall level of discretionary funding for 2007 endorsed in the budget resolution that the Senate passed on March 16 is higher than the cap that the President is proposing for 2007.

### Caps Proposed by the President Would Require Deep Cuts in Domestic Discretionary Programs

The caps proposed by the President would necessitate steep cuts in domestic discretionary programs over the next five years, unless defense and international programs are funded at levels well below those the President has requested.

- Under the President's budget, overall funding for domestic discretionary programs (programs other than those related to defense or international affairs) would be reduced by $152 billion over the next five years. This is the amount by which these programs would have to be cut under the proposed caps, unless defense and international affairs programs were funded at levels below those reflected in the budget. (The $152 billion figure represents the amount by which the funding levels in the President's budget fall below the CBO baseline, which is CBO's estimate of the amounts needed to maintain current levels of service in these programs and equals the fiscal year 2006 funding levels for these programs, adjusted for inflation. The funding levels the President has proposed fall somewhat further below the OMB baseline; they are $183 billion below OMB baseline levels. The difference reflects the fact that OMB assumes somewhat higher levels of inflation then CBO does.[1])




- Under the President's budget, the reductions in domestic discretionary programs would grow larger with each passing year, reaching $47 billion a year in 2011. (See chart above.) By that year, expenditures for domestic discretionary programs would fall to their lowest level, measured as a share of the economy, since 1962.

One might ask whether Congress would adhere to the Administration's defense requests. Under this proposal, Congress would have to do so for several years. Under the rule the Administration is proposing, there would be two sets of caps in 2007 and 2008, one applying to programs in the "national defense" part of the budget and the other applying to all other discretionary programs.[2]

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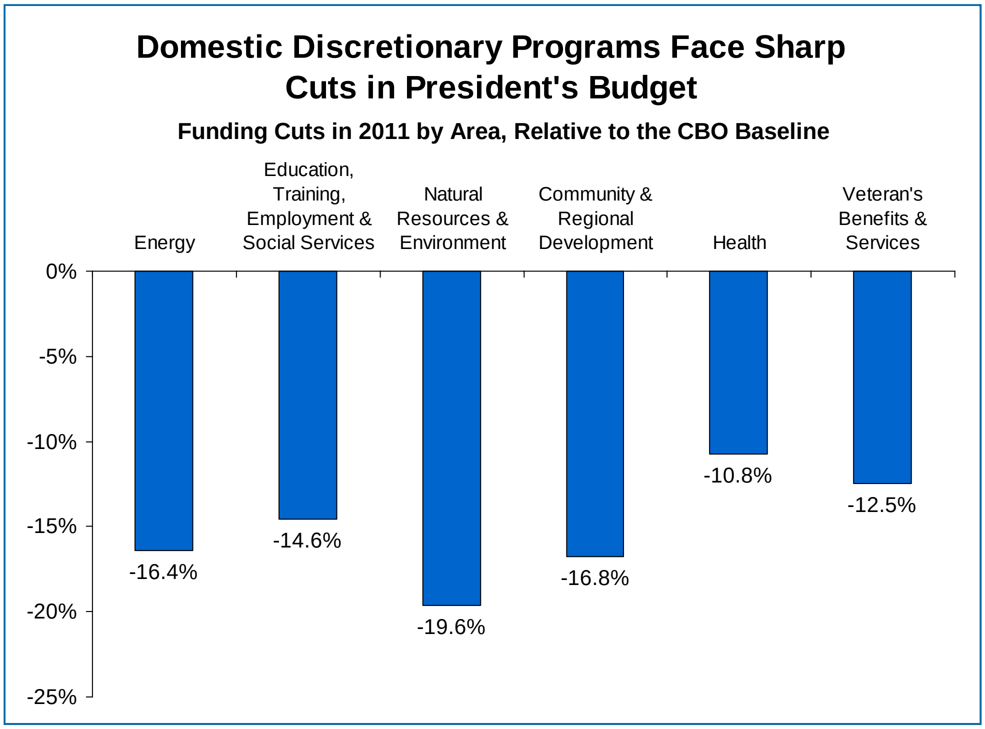
[1] This analysis uses a CBO baseline that has does not assume that the same level of emergency discretionary funding enacted for 2006 (for the war in Iraq and Afghanistan, hurricane relief, and for other purposes) will be provided for 2007 and each succeeding year. For comparability, emergency funding proposed by the President for 2007 is also excluded from the analysis.

[2] The national defense function includes the military activities of the Department of Defense (and so excludes the civilian operations of the Army Corps of Engineers). It also includes the nuclear weapons programs of the Department

Starting in 2009, there would be a single set of caps. In other words, the Administration would establish temporary "firewalls" between its proposed defense and non-defense budgets in 2007 and 2008; Congress would not be permitted to re-order priorities between these two parts of the budget until 2009.




### Proposed Caps Depart from the Successful Experience in the 1990s

The cuts the proposed caps would necessitate depart sharply in two respects from the experience with discretionary caps in the 1990s, when such caps proved effective. First, the caps in effect through most of the 1990s were part of larger, carefully balanced deficit-reduction packages. Both in 1990 when discretionary caps were first established and in 1993 when they were extended, discretionary caps were instituted as part of broad deficit-reduction legislation that combined restraint on discretionary programs with increases in taxes (particularly for those who could best afford to pay more) and reductions in entitlement spending (in part by reducing Medicare payments to health-care providers). The discretionary caps of the 1990s also were accompanied by "Pay-As-You-Go" rules that required both entitlement expansions *and* tax cuts to be offset fully. In short, the discretionary spending caps of the 1990s were part of a larger program of shared sacrifice that was spread across the population and that played a major role in addressing the large deficits of that era.

The President's new cap proposal is different. The President's budget singles out domestic discretionary programs for hefty cuts[3] without producing any overall deficit reduction. Taken as a whole, the President's budget would make deficits *larger* than they otherwise would be, primarily because of its proposed tax cuts. The stiff cuts in domestic discretionary programs that the

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of Energy, some Coast Guard and FEMA operations (these agencies are part of the Department of Homeland Security), and certain FBI activities, among other non-Defense Department programs.

[3] The President's budget does include smaller cuts in entitlement programs. The Congressional Budget Office estimates the President's entitlement proposals would reduce spending by $27 billion over five years ($47 billion if the cost of the President's proposed Social Security private account plan is excluded).

proposed caps would lock in would be used *not* to reduce the deficit but to finance a portion of the cost of the tax cuts.[4]

Second, the cuts in domestic discretionary programs that would be required under the proposed caps would be nearly *eight times as deep* (measured as a share of the economy) as the domestic discretionary program cuts instituted under the discretionary caps enacted in 1990 and 1993.

## Why the Proposed Caps Are Ill-Advised

This analysis finds the President's proposed caps on discretionary programs are ill-advised. The caps would be inequitable. They also would be likely to do more to hinder fiscal discipline than to advance it. The proposed caps have at least five basic flaws.

- **The cuts they would require are too severe**. As noted, the budget calls for funding cuts in domestic discretionary programs that total $152 billion over five years and reach $47 billion in 2011. Funding for 14 of the 15 domestic discretionary program areas (or budget functions) would be cut over the next five years; every area except science, space, and technology would be hit. Among the domestic program categories that would sustain hefty cuts are education, environmental protection, national parks, medical research, veterans health care, and housing and homeless programs, among numerous others.

  For example, the President's budget envisions cuts in environmental and natural resource programs of nearly 20 percent by 2011. (In other words, funding for these programs in 2009 would fall 20 percent — or $6.8 billion — below the CBO baseline, which equals the 2006 funding level adjusted for inflation.) As another example, veterans programs that are not entitlements (principally veterans' health care) would be cut 12.5 percent, or almost $5 billion, in 2011.

- **These cuts are *not* part of a balanced package.** As noted, the discretionary spending restraints enacted in the early 1990s were part of broader deficit-reduction efforts that entailed shared sacrifice. Members of Congress who favored increased discretionary spending, Members who sought entitlement expansions, and Members who wanted tax cuts all agreed to forgo their favored proposals in return for restraint on all parts of the budget.

  The new discretionary cap proposal is offered in a different context. Not only would there be no restraint on the revenue side of the budget, but nearly all of the recent tax cuts would be extended and made permanent. (Over the next ten years, the cost of the extending the 2001 and 2003 tax cuts — a policy reflected in the President's budget — would total $3.3 trillion, including the costs of extending Alternative Minimum tax relief and of the added interest payments on the debt.) As a result, the cuts in domestic discretionary programs would not contribute to deficit reduction, but would instead be used to help finance tax cuts.

[4] See "The President's Budget: A Preliminary Analysis," Center on Budget and Policy Priorities, revised February 10, 2006.

| The Discretionary Caps Agreed to in 1990 and 1993 Were Adhered to, the More Severe Caps Passed in 1997 Were Not, and the Proposed Caps Are Even More Severe | | | |
|---|---|---|---|
| Change in expenditures for domestic discretionary programs | Actual Change from 1990 through 1998 (actual results, which were consistent with caps) | Assumed change from 1998 through 2002 under caps enacted in 1997 [a] | Proposed change from 2006 to 2011 under President's budget plan |
| As a share of GDP | -0.1% of GDP | -0.6% of GDP | -0.8% of GDP |
| Average annual growth rate, adjusted for inflation and population | +0.5% per year | -2.7% per year | -3.9% per year |

a. Assumes the subdivisions between defense, international, and domestic programs set for t h in the 1997 budget agreement. Under that agreement, defense and domestic programs were assumed to be squeezed equally hard, although that was not required as a matter of statute. In practice, funding for all types of discretionary programs — defense, international, and domestic — exceeded the plan by increasingly large amounts starting in fiscal 1999.

- **The proposed discretionary caps would likely make it *harder* to secure agreement in coming years on a major deficit-reduction package**. One lesson of the 1990s is that passing large-scale deficit-reduction measures entails putting all parts of the budget on the table and having various Congressional factions agree to accept deficit-reduction measures affecting their favored parts of the budget in return for the application of such measures to the other parts of the budget as well. To craft large-scale deficit reduction measures that can pass and be sustained, discretionary programs, entitlement programs, and taxes all need to contribute.

  Yet the proposed five-year discretionary caps are so austere with regard to domestic programs that further cuts in discretionary spending over the next five years would almost certainly be out of the question. That would make it considerably more difficult to craft a major deficit-reduction package after the 2006 election, since there would be nothing left to give on the domestic discretionary side of the budget to help induce those who favor continued tax cuts to agree to start restoring the federal revenue base.

  The proposed five-year discretionary caps consequently are likely to set back the cause of deficit reduction, which badly needs a large, multi-year deficit reduction package that covers all parts of the budget. For reasons of both equity and fiscal responsibility, the proposed caps consequently appear worse than no caps at all.

- **History shows that unrealistically severe discretionary caps get blown away and may *weaken* fiscal discipline.** In 1990 and 1993, discretionary caps that placed realistic restraints on discretionary programs were enacted. Those caps were honored.[5] In 1997, far more austere caps were established as part of the 1997 Balanced Budget Act, which sought to produce a balanced budget by 2002 under the budget assumptions in use at that time. These caps were so tight that Congress could not live with them, and they were blown away. The ultimate result was no meaningful restraint at all on discretionary spending. (See the table above.)

[5] The caps allowed emergency expenditures under circumscribed conditions. Through 1998, emergency funding was used only for the Gulf War and major natural disasters.

The lesson is that reasonable caps negotiated as part of a balanced deficit-reduction package that contains shared sacrifice can be effective, but caps that are too severe are not sustained, especially when they are not part of a larger, balanced set of deficit-reduction policies. (Another factor that weakened Congress' ability to adhere to the austere caps set in 1997 — which would have required substantial reductions in discretionary programs — was that Congress simultaneously began passing tax cuts that were not offset and that violated the "Pay-As-You-Go" rules, then part of federal law. If fiscal discipline is not enforced in other parts of the budget, it is difficult to enforce rules that require cuts in discretionary programs.)

The caps that the President is proposing would entail reductions in domestic discretionary programs noticeably *deeper* than those called for under the unrealistic caps that were enacted in 1997 and could not be sustained.[6]

## Conclusion

Enactment of five-year caps on discretionary programs at this time would be both inequitable and unwise. The caps proposed by the President are designed to lock in substantial reductions in a broad array of domestic discretionary programs. But these cuts would not be part of a comprehensive, balanced approach to deficit reduction, as the five-year caps established in the early 1990s were. Under the President's budget, the domestic cuts would not be matched with cuts in defense and international spending or by increases in revenues that would contribute to deficit reduction. Instead, the cuts in domestic spending the President's budget proposes would only partially offset the cost of the tax cuts and increases in defense spending the President is seeking. Even if the discretionary caps were adhered to, enactment of the other policies the President has proposed would increase the deficit over the next five years by more than $250 billion.

In addition, the establishment of the President's proposed discretionary caps at this time would likely make it harder in the next few years to craft a large bipartisan deficit-reduction measure that seeks shared sacrifice from all parts of the budget. Advocates of cuts in domestic discretionary programs would already have achieved their goal, making it harder to induce them to support cuts in defense and international programs or increases in revenues in return for constraints on domestic programs. Conversely, advocates of domestic discretionary programs would be unlikely to support any deal that calls for even deeper cuts in those programs.

Adoption of the proposed caps thus would be ill-advised. Both from the standpoint of fiscal responsibility and from the standpoint of advancing the well-being of the American public in areas ranging from the environment to education to health and safety to aiding the less fortunate, the proposed caps would be likely to do more harm than good.

[6] It also may be noted that the Senate voted during its recent consideration of the budget resolution for 2007 to increase total funding for discretionary programs in 2007 to a level more than $6 billion above by the President's proposed cap level for that year (not counting emergency funding proposed in the Senate budget plan or the President's budget).