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Senate Proposal for Balanced Budget Amendment Would Require Extreme Budget Cuts

By Richard Kogan and Cecile Murray[1]

The constitutional balanced budget amendment (BBA) that the Senate may consider this year risks serious harm to the economy by requiring a balanced budget even during an economic downturn. Moreover, this particular BBA would inflict substantially greater damage, because it also would prevent the federal government from meeting the nation's basic needs even when the economy is healthy. That's because the proposed amendment — introduced by Senate President *Pro Tem* Orrin Hatch (R-UT) and cosponsored by every Republican senator — would enshrine in the Constitution a severe cap on total federal spending set at 18 percent of gross domestic product in the prior completed calendar year.[2]

This cap would compel policymakers to cut all programs by an average of more than *one-fourth* when it takes effect — we are assuming 2023. The total amount of cuts required would amount to $8 trillion over the next decade; starting in 2023, the cuts would be about half a trillion dollars a year *deeper* than those that would be made under the severe budget plan the House Budget Committee's Republican majority passed earlier this year. If the cuts required by the Senate Republican BBA proposal were made equally across all programs, Social Security would be cut $2.3 trillion over the ten-year period, and defense would be cut more than $1 trillion on top of the cuts that have already occurred and are scheduled to occur as a result of the 2011 Budget Control Act's annual funding caps and sequestration. As a result, defense spending would fall by 2026 to its lowest level as a percent of the economy *since 1940*, before the United States entered World War II.

The cuts would be equally severe in non-defense discretionary programs, such as education, transportation, law enforcement, environmental protection, and medical and scientific research. By

[1] Kelsey Merrick contributed to an earlier version of this piece.

[2] Senator Orrin Hatch introduced Senate Joint Resolution 6 on February 4, 2015. This constitutional amendment sets a spending cap for each fiscal year equal to 18 percent of gross domestic product in the prior completed *calendar* year. The cap will therefore be less than 18 percent of GDP whenever nominal GDP is growing. Under the Congressional Budget Office's (CBO) most recent economic assumptions, the cap would vary from year to year and would be 16.8 percent of GDP in fiscal year 2023 and in eight of the next ten fiscal years.

2026, spending for those programs would plummet to an exceptionally low percent of the economy — a level likely not seen *since the early 1930s*.[3]

Policymakers could, of course, limit the cuts in some programs, but then they would have to cut other programs even more sharply. For instance, if they exempted Social Security from cuts, they would have to cut other programs by well over one-third, on average, in 2023. If they exempted Social Security, Medicare, and defense, all other programs would need to be cut by nearly two-thirds.

In short, beyond the other serious problems that a balanced budget amendment would engender, the spending level mandated by the Senate Republican BBA proposal is starkly inadequate. It would require spending dramatically below the levels (as a percent of gross domestic product or GDP) achieved in the Reagan Administration even though, due to the retirement of the baby-boom generation and increases in health care costs, among other factors, government spending now needs to be higher, not lower, than in the 1980s to address the nation's needs.

Proposal Imposes Severe Budget Caps Plus Zero-Deficit Requirement

Under the proposal, the first year in which the budget would have to be balanced might be fiscal year 2023.[4] As difficult as that would be, the proposal also prohibits any tax increases and, as noted, limits federal spending to 18 percent of GDP in the prior completed calendar year, which would be about 16.8 percent of GDP in the current fiscal year (see footnote 2). These three requirements could be waived only by a two-thirds vote of both the Senate and the House.[5]

The proposed spending limit — which would apply to *all* federal spending, whether for military engagements, natural disasters, epidemics, interest payments, or ongoing programs — is so low that it would produce a budget surplus of about $315 billion in 2023 and growing surpluses in subsequent years, unless tax cuts were enacted alongside these severe budget cuts. Indeed, it would leave room for *$1.4 trillion* in new tax cuts by 2026. It's unclear whether the severely restrictive spending limit was designed to facilitate tax cuts even in the face of a balanced budget requirement.

The spending limit is so low, in fact, that:

- During the Reagan Administration, the federal government would have breached the spending limit that the Senate Republican BBA would set by an average of 5.8 percent of GDP, which is equivalent to "excess" spending of $1.1 trillion in 2016 alone. Moreover, the level of spending under President Reagan occurred before any baby boomers had retired and when spending throughout the U.S. health care system (including the private sector) was just over half of today's level as a percent of GDP. It also was before the September 11 terrorist attacks led to the creation of a new category of homeland security spending, and before the

[3] CBPP estimate. Specific CBO and Office of Management and Budget historical data on non-defense discretionary programs are available only back to 1962.

[4] The Senate's BBA specifies that its requirements would take effect in the fifth fiscal year after its ratification. If Congress approved the amendment this year, ratification by three-quarters of the states could conceivably be completed by the end of calendar year 2017. If so, the amendment would take effect for fiscal year 2023.

[5] Deficits and spending in excess of the cap (apparently for any program) could occur under somewhat less restrictive conditions if the United States has declared war, which it last did in 1941, or is engaged in a serious military conflict.

wars in Iraq and Afghanistan led to increases in veterans' health-care costs that will endure for decades.

- During the second term of the Clinton Administration, when the federal government ran surpluses for the only time since 1969, spending would nevertheless have breached the limit by an average of 1.6 percent of GDP, equivalent to $300 billion in 2016 alone.
- The House Budget Committee's 2017 budget plan would breach the limit in the Senate Republican BBA proposal by $514 billion in 2023 and by about $2 trillion over the four-year period 2023-2026. The BBA proposal thus would require massive cuts *on top of* those in the House budget plan, which itself calls for $6 trillion of spending cuts over ten years. That plan would cut programs for low- and moderate-income Americans by $3.7 trillion over ten years (or 42 percent by 2026), by repealing health reform's insurance subsidies and its Medicaid expansion and then cutting an additional $1 trillion from Medicaid, making deep cuts to SNAP (formerly food stamps) and Pell Grants, and dramatically shrinking non-defense discretionary programs far below sequestrations levels.[6]

Proposal Would Require $8 Trillion in Cuts Through 2026

We examined the impact if a 16.8-percent-of-GDP spending cap took effect in fiscal year 2023, as would occur if Congress approved the constitutional amendment now and the requisite number of states ratified it by the end of next year. To meet the cap in 2023 and subsequent years (while assuming budget balance rather than large surpluses), Congress would have to cut spending on federal programs — that is, all spending except interest on the debt — by an average of *26 percent* in 2023 (see Figure 1), which translates to $8.0 trillion in program cuts through 2026. (Counting the interest savings generated by the lower deficits and ultimately a balanced budget, total spending over this period would be $8.8 trillion lower.)

The cuts through 2026, if spread proportionally over all programs, would be as follows:

- Social Security would be cut about $2.3 trillion.
- Medicare would be cut about $1.5 trillion.
- Medicaid, the Children's Health Insurance Program (CHIP), and health reform's exchange subsidies would be cut more than $1.0 trillion.
- Veterans' disability payments, pensions, and other entitlement benefits would be cut $215 billion.
- Key safety-net programs — Supplemental Security Income (SSI) for the elderly and disabled poor, SNAP, the school lunch and other child nutrition programs, and the refundable portions of the Child Tax Credit and Earned Income Tax Credit — would be cut $436 billion.

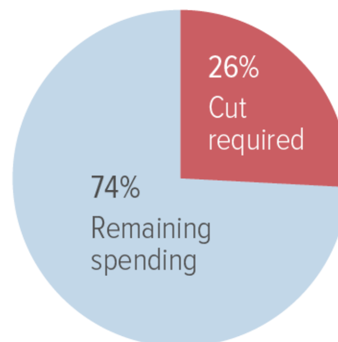
[6] See Richard Kogan and Isaac Shapiro, "House GOP Budget Gets 62 Percent of Budget Cuts from Low- and Moderate-Income Programs," CBPP, March 28, 2016, http://www.cbpp.org/research/federal-budget/house-gop-budget-gets-62-percent-of-budget-cuts-from-low-and-moderate-income.

- Defense would be cut more than $1.0 trillion, falling from its current level (including war spending) of 3.2 percent of GDP to 1.8 percent of GDP by 2026, *a level not seen since before World War II.*
- Non-defense discretionary (i.e., non-entitlement) programs would be cut about $1.1 trillion. Funding for these programs would fall from the current 3.3 percent of GDP to 1.9 percent of GDP by 2026, *likely the lowest level since the early 1930s.* This area of the budget includes education, housing, veterans' health care, transportation, law enforcement, biomedical and other scientific research, job training, natural resources and environmental protection, and the Treasury.

FIGURE 1

Senate GOP Balanced Budget Amendment (BBA) Would Slash Program Spending by 26 Percent

Average cut in all federal programs required by 2023



Note: Proposal (S.J. Res. 6) is a constitutional BBA that would limit overall spending. Figure assumes amendment takes effect in 2023.

Source: CBPP analysis of Congressional Budget Office data

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Policymakers would not have to cut all programs by the same percentage and likely would not do so. But if they exempted certain programs from cuts, they would have to cut others even more deeply. For example:

- If Social Security were exempt, the average cut to all other programs would rise from 26 percent in 2023 to 37 percent. The Medicare cuts alone would grow to almost $2.1 trillion through 2026, for instance, and the Medicaid, CHIP, and health reform subsidy cuts would grow to about $1.5 trillion.
- If Social Security and Medicare were exempt, the cuts to all other programs would rise to 49 percent in 2023. Veterans' benefit programs would be cut $406 billion through 2026, the key safety-net programs mentioned above would be cut $821 billion, and defense and non-defense discretionary programs would each be cut roughly $2 trillion, falling in each case to 1.2 percent of GDP by 2026.
- If Social Security, Medicare, *and* defense were exempt, the cuts to all other programs would rise to 65 percent in 2023.[7] Veterans' benefit programs would be cut $539 billion through 2026, key safety-net programs slashed by $1.1 trillion, and non-defense discretionary spending cut more than $2.7 trillion, bringing it down to 0.8 percent of GDP by 2026.

These figures (and those in Table 1) assume that all programs not exempt from cuts are cut by the same proportion. Figure 2 illustrates how these different scenarios all would sharply reduce non-defense discretionary spending by 2026.

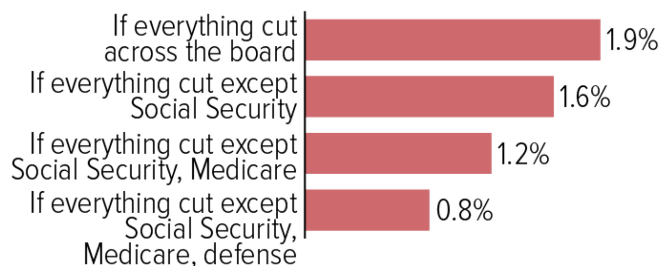
[7] If only defense were exempt, other programs would need to be cut by 30 percent in 2023. If only Social Security and defense were exempt, the required cut to other programs would be 45 percent.

FIGURE 2

Senate GOP Balanced Budget Amendment (BBA) Deepens Fall in Non-Defense Discretionary (NDD) Funds

NDD, already projected to shrink as percent of gross domestic product under current law...

...would shrink even more under proposed BBA



Note: Proposal (S.J. Res. 6) is a constitutional BBA that would limit overall spending. Figures assume across-the-board cuts to meet BBA requirement.

Source: CBPP analysis of Congressional Budget Office data

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Even a BBA Without a Spending Cap Would Require Deep Cuts

A more standard version of a balanced budget amendment, such as the one the House considered in 2011 (H.J. Res. 2), would not impose a harsh spending cap. But it would require that federal outlays not exceed federal receipts in any fiscal year, and even that proposal would require massive budget cuts, assuming taxes are not raised to help balance the budget. If such a standard BBA took effect in fiscal year 2023, then in order to balance the budget that year and subsequent years, policymakers would have to cut program spending by 20 percent in 2023, which translates to $6 trillion in program cuts through 2026.

If Congress cut all programs across the board:

- Social Security would be cut more than $1.7 trillion through 2026.
- Medicare would be cut $1.1 trillion.
- Defense spending would be cut almost $800 billion, falling from its current 3.2 percent of GDP to 2.0 percent by 2026, a level not seen since 1940.
- Veterans' disability payments, pensions, and other entitlement benefits would be cut $163 billion.

Exempting any program from cuts would require even larger cuts in the others:

- If Social Security were exempt, the average cut to all other programs would rise from 20 percent in 2023 to 28 percent. The Medicare cuts alone would grow to almost $1.6 trillion through 2026, for instance.
- If Social Security and Medicare were exempt, the cuts to all other programs would average 37 percent in 2023. Veterans' benefit programs would be cut about $307 billion through 2026, key safety-net programs — SSI, SNAP, the school lunch and other child nutrition programs, and the refundable portions of the Child Tax Credit and Earned Income Tax Credit — would be cut more than $600 billion, and defense and non-defense discretionary programs would fall to 1.5 and 1.6 percent of GDP by 2026, respectively.
- If Social Security, Medicare, and defense were exempt, the cuts to all other programs would average 50 percent in 2023. Veterans' benefit programs would be cut $408 billion through 2026, key safety-net programs would be cut $825 billion, and non-defense discretionary spending would be cut $2 trillion, falling to 1.3 percent of GDP by 2026.

TABLE 1

Senate Republican Proposal: Additional Budget Cuts Required to Balance the Budget and Adhere to the Spending Cap in 2023 and Subsequent Years

	No program spared from cuts		Social Security spared from cuts		Social Security and Medicare spared from cuts		Social Security, Medicare, and defense spared from cuts	
	in 2023	thru 2026	in 2023	thru 2026	in 2023	thru 2026	in 2023	thru 2026
Percent cut for unprotected programs	26%		37%		49%		65%	
Total required program cuts	**1,251**	**7,966**	**1,251**	**7,966**	**1,251**	**7,966**	**1,251**	**7,966**
Cuts to Selected Programs:								
Social Security	356	2,270	0	0	0	0	0	0
Medicare	228	1,466	319	2,051	0	0	0	0
Medicaid/CHIP/ health reform exchanges	166	1,054	232	1,474	311	1,987	413	2,636
SSI, SNAP, child nutrition, & refundable parts of CTC and EITC	69	436	97	610	130	821	172	1,090
Federal retirement	52	325	72	455	97	612	128	813
Veterans' disability compensation & other entitlement benefits	34	215	47	301	64	406	84	539
Defense (including war costs)	164	1,042	230	1,457	308	1,962	0	0
[resulting level as a % of GDP by 2026]		1.8%		1.5%		1.2%		2.5%
Non-defense discretionary	174	1,099	243	1,537	326	2,070	432	2,747
[resulting level as a % of GDP by 2026]		1.9%		1.6%		1.2%		0.8%

Note: Program cuts do not include associated interest savings. Cuts are assumed to be distributed equally across the board except to those programs specified as spared from cuts.
Source: CBPP analysis of Congressional Budget Office data.

Appendix: Methods and Assumptions

Approach. The analysis in this paper starts from the baseline projection that the Congressional Budget Office (CBO) issued on March 24, 2016 (https://www.cbo.gov/sites/default/files/51118-2016-03-BudgetProjections.xlsx), with certain small adjustments explained in previous analyses.[8] The resulting CBPP baseline produces deficit estimates very close to those of CBO's baseline. Over the next ten years, CBPP projects total deficits that are 2 percent below CBO's. The deficit projections for 2026 are virtually identical. From there, our analysis assumes spending cuts will be phased in over the five-year period 2019-2023 sufficient to balance the budget in fiscal year 2023 at the level of the spending cap specified in the Senate BBA proposal.

There are both economic and budgetary advantages to phasing in the necessary cuts starting in 2019 rather than instituting them all at once in 2023:

- If phased in over time, the cuts are less likely to drag the economy into an immediate recession.
- If the cuts start in 2019, deficits and debt will be lower in 2019-2022 than they would otherwise have been. A lower debt at the end of 2022 means that interest costs will be lower in 2023, which goes a small part of the way to balancing the budget and therefore reduces the needed program cuts in 2023 and subsequent years. (This advantage is partly offset by the higher interest costs generated by our assumption that policymakers will enact tax cuts to eliminate the surpluses that the deep spending cuts required by the BBA proposal would produce under existing tax law.[9] This assumption is discussed further in the next section.)
- In this analysis, we make the simplifying assumption that the percentage cut in discretionary 2023 *outlays* shown in Table 1 can be achieved by the same percentage cut in 2023 *funding*. In actuality, many programs, especially procurement, construction, and education programs, disburse one year's funding over two or more years. For those programs, even *eliminating* funding in one year does not stop all expenditures in that year, because funds appropriated in prior years are still being disbursed to fulfill obligations validly incurred in those years. As a result, cutting discretionary expenditures is best accomplished if the program cuts start in earlier years. Even with this earlier start, the discretionary outlay savings that Table 1 shows for 2023 would almost certainly require slightly higher percentage cuts than those shown here. In that respect, our figures slightly understate the severity of the proposed BBA and outlay cap.

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[8] See for example the Technical Note at the end of Robert Greenstein, Joel Friedman, and Isaac Shapiro, "Program Spending Historically Low Outside Social Security and Medicare, Projected to Fall Further," CBPP, February 24, 2016, http://www.cbpp.org/research/federal-budget/program-spending-historically-low-outside-social-security-and-medicare.

[9] Policymakers might opt to have the tax cuts become effective *before* 2022, when surpluses would otherwise first appear, in order to package them with the very large program cuts necessitated by the spending limits and thus make the latter more politically palatable. If the tax cuts do start before 2022, the higher debt accumulated before 2022 would lead to higher interest costs thereafter, necessitating slightly bigger spending cuts than we have modeled. For example, the across-the-board program cut needed in 2023 would rise from the 25.9 percent we model to 26.5 percent.

Calculations of cuts. In calculating the spending cuts need to hit the outlay cap, we assume they start in 2019.[10] We "stair-step" them upwards until 2023, so that the 2020 cuts are twice the size of the 2019 cuts, the 2021 cuts are three times the 2019 cuts, and so on through 2023. We fix the nominal value of the starting program cuts in 2019 at the level that, with interest savings also accounted for, will reduce spending to the specified outlay cap levels in 2023.

Supposing revenues are held at baseline (current-law) levels, such spending cuts would produce a significant, permanent surplus. We assume that a tax cut is enacted sufficient to eliminate surpluses that would otherwise appear. In this model, those surpluses would appear first in 2022, totaling $1.5 trillion over the five-year period 2022 to 2026, so our assumed tax cuts eliminate these surpluses in 2022 and subsequent years. As a result, revenues equal the levels of the spending limits in each year from 2022 onward, so that the budget is balanced at those levels.

After 2023, the spending cuts grow as needed to keep total outlays at the specified cap levels. This growth in spending cuts after 2023 is just above the growth rate of GDP; in this analysis, the required program cuts reach about $1.25 trillion, or 5.1 percent of GDP, in 2023, and rise to 5.5 percent of GDP by 2026. The $1.25 trillion in policy cuts in 2023 is accompanied by more than $100 billion in interest savings in that year, which together remove the $1,358 billion in excess spending for that year.

Finally, it should be noted that the ultimate magnitude of the budget cuts needed is not affected much by the precise year in which the budget must first be balanced. If budget balance were required in 2022 rather than 2023, the necessary cuts would have to start bigger in 2019. But the size of the program cuts would reach a level in 2022 very similar to the cuts for 2023 that we model: 25 percent on average, instead of the 26 percent for 2023 that we calculate in this analysis. Similarly, if the budget did not need to be balanced until 2024 or later, the cuts could be smaller at first than under our model (because they would have more years to stair-step up) but would eventually reach a slightly larger size in the year in which the budget is first balanced.

In short, there is no ultimate relief to be gained either by accelerating or delaying the BBA's effective date, since balancing the budget by 2023 happens to require cutting programs by much the same percent as would balancing either somewhat earlier or somewhat later.[11]

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[10] This date is consistent with our assumption that the states might complete ratification of the Senate proposed BBA by the end of 2017. When Congress next convened, in January 2018, it would be faced with designing a budget for fiscal year 2019, which begins on October 1, 2018.

[11] A substantial amount of federal benefit payments occur monthly, such as veterans' disability compensation. Under current law, in that program and some others, if the monthly payment is due to fall on a weekend, it is accelerated to the prior Friday. Occasionally, this acceleration moves a monthly payment forward from one fiscal year to the prior one; as a result, while most fiscal years have 12 such monthly payments in those programs, some have 11 or 13. Fiscal year 2023 has 12 monthly payments, but 2022 has 13 such payments and 2024 has 11. Anomalies of this sort could lead to strange peaks or valleys in the amounts of spending cuts needed to adhere to the Senate's proposed spending limits. In evaluating whether assuming a target year *other than* 2023 would seriously change the depth of the needed spending cuts, we therefore first assume that Congress would repeal the provisions of law that cause these occasional timing shifts; that is, we adjust current law to have 12 monthly payments in every fiscal year. Note that the budget plan designed this spring by the House Budget Committee also makes such an assumption. Indeed, it is a normal policy assumption to make when faced with arbitrary budget targets such as a balanced budget in every year or a constitutional spending limit.