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Averting a Budget Crisis Is Not Enough: Criteria for Evaluating Fall Budget Proposals

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Now that Congress has returned from the summer recess, it will have to set funding levels for discretionary programs for fiscal year 2014 (or risk a government shutdown) and raise the debt ceiling (or see the nation default on legally binding financial obligations). In both areas, the House and Senate are far apart.

House Republicans have called for funding appropriated programs at $967 billion, the level set by the 2011 Budget Control Act (BCA) after sequestration, while shifting about $50 billion from non-defense programs to defense.[1] Senate Democrats and the President have called for replacing sequestration in all years with alternative, balanced deficit-reduction policies and setting 2014 appropriations at $1.058 trillion, the BCA cap level *before* sequestration[2] — which would still leave total discretionary funding about 10 percent below the 2010 level, adjusted for inflation.

In addition, the Treasury Department has indicated that in mid-October the government will reach the statutory debt limit. House Speaker John Boehner has demanded more spending cuts in return for raising the debt ceiling, while Democrats and the President argue that risking the full faith and credit of the United States should not be a negotiating tactic.[3]

In all likelihood, policymakers will enact a short-term funding bill before October 1 to give them more time to negotiate final 2014 funding levels, and one hopes they will avoid default. Yet averting these crises *is not itself an adequate benchmark of success.* A key question is whether the compromises that are reached represent sound policy. Here, the outcome is very much in doubt.

Beyond avoiding default and a government shutdown, four criteria should be used to evaluate proposals to resolve the pending budget issues:

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[1] Joel Friedman, *et al.,* "Too Little to Go Around: House Appropriations Plan to Increase Defense and Homeland Security Requires Even Deeper Cuts in Other Programs," Center on Budget and Policy Priorities, June 5, 2013, http://www.cbpp.org/cms/index.cfm?fa=view&id=3969.

[2] Joel Friedman, *et al.,* "Senate Appropriations Allocations for 2014 Reflect Better Approach Than House Plan," June 25, 2013, http://www.cbpp.org/cms/index.cfm?fa=view&id=3982.

[3] Luke Johnson, "John Boehner: No Debt Ceiling Hike without Spending Cuts," Huffington Post, July 23, 2013, http://www.huffingtonpost.com/2013/07/23/john-boehner-debt-ceiling-hike_n_3639675.html.

(1) Do they strengthen the economic recovery, or do they weaken or slow the recovery?

(2) Do they protect low-income Americans and avoid increasing poverty and hardship, a principle embraced by leaders of both parties in past deficit-reduction efforts and by fiscal commission co-chairs Alan Simpson and Erskine Bowles?

(3) Do they permit adequate investment in core public services, including building blocks of economic growth such as infrastructure, education, and research, as well as efforts to expand economic opportunity?

(4) Do they reflect a balanced approach, both between budget cuts and revenue increases and between defense and non-defense funding?

The coming debates hold both opportunities and risks. Members of both parties increasingly understand that sequestration is impeding economic growth and is reducing funding for broadly supported public services and national defense. That should set the stage for compromise. At the same time, the risk exists that policymakers will fail to agree on replacing sequestration or will agree on a replacement package that is imbalanced — that is, one that swaps one set of ill-advised cuts for another, fails to scale back wasteful or inefficient tax expenditures, or increases defense funding while ignoring the shortfall in key non-defense areas.

Supporting the Economic Recovery

The economy continues to grow, but too slowly to restore normal employment levels four years after the recession officially ended. Although the unemployment rate has come down, it remains unacceptably high. Moreover, as Federal Reserve Chairman Ben Bernanke stated recently (and as we have discussed more fully elsewhere), the current unemployment rate overstates the health of our labor markets.[4] Brookings economist Gary Burtless estimates that if current labor market conditions were similar to what they were in 2007, just prior to the Great Recession, 7.4 million more people would be working today.[5] We have made some progress — that gap was 9.7 million people at the beginning of the recovery. But without much faster job growth than we have seen so far, it will take years to get back to normal employment levels.

Sequestration is an important factor holding back the recovery. A recent Congressional Budget Office (CBO) analysis concludes that canceling sequestration for both fiscal years 2013 and 2014 "would increase the level of real (inflation-adjusted) gross domestic product … by 0.7 percent and increase the level of employment by .9 million in the third quarter of calendar year 2014."[6]

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[4] Chad Stone, *et al.,* "SNAP Enrollment Remains High Because the Job Market Remains Weak," Center on Budget and Policy Priorities, revised July 30, 2013, http://www.cbpp.org/cms/?fa=view&id=3996.

[5] Gary Burtless, "How Far Are We From Full Employment?" Brookings Institution, August 27, 2013, http://www.brookings.edu/research/opinions/2013/08/27-full-employment-burtless.

[6] Congressional Budget Office, "How Eliminating the Automatic Spending Reductions Specified by the Budget Control Act Would Affect the U.S. Economy in 2014," July 25, 2013, http://www.cbo.gov/publication/44445.

To be sure, we ought to reduce the projected debt over the next decade and stabilize the debt as a percentage of the economy over the longer term.[7] The best approach would be to replace sequestration with a package that contains sizeable alternative deficit-reduction measures that take effect gradually as the economy and the labor market strengthen as well as temporary, upfront measures to boost job creation now. Such a package could do *more* than sequestration to reduce deficits and stabilize the debt over the mid- and long term. It would cut less than sequestration in 2014 and the next few years, but would reduce deficits by greater amounts than sequestration in the latter years of the decade — and in future decades.[8] If policymakers cannot agree now on a full sequestration-replacement plan, a sound first step would be to replace the next few years of sequestration with alternative deficit reduction that's largely timed to take effect when the economy is stronger.

The debate over raising the debt limit also bears directly on the economic recovery.[9] If policymakers do not raise the debt limit and the government stops making legally required payments for costs that Congress has already approved, the short- and long-term economic consequences could be dire. These could include permanently higher interest rates for the federal government and a large and abrupt drop in federal payments for goods, services, and benefits, which would immediately slow growth and drive up unemployment.

The International Monetary Fund recently advised policymakers to "[repeal] the sequester and [adopt] a more balanced and gradual pace of fiscal consolidation in the short term; expeditiously [raise] the debt ceiling to avoid a severe shock to the U.S. and the global economy; and [implement] a comprehensive and back-loaded set of measures to restore long-run fiscal sustainability."

Speaker Boehner has argued that any increase in the debt ceiling must be paired with an equal amount of spending cuts. This formulation is so restrictive that even the ambitious budget plan from fiscal commission co-chairs Alan Simpson and Erskine Bowles — which would shrink the deficit to less than 1 percent of gross domestic product (GDP) before the end of the decade and put the debt ratio on a clear downward path — would fall far short of meeting it.[10] To meet Boehner's test over the coming decade would require enacting most or all of the more than $5 trillion in budget cuts in the Ryan budget, or their equivalent. The Ryan budget would require deep cuts in basic public services and slash Medicaid and SNAP. Most of the Ryan cuts are unspecified, perhaps because specifying them would reveal how substantively and politically unpalatable they are. Importantly, cuts of this magnitude aren't necessary to stabilize the debt as a percent of the economy, and initiating them while the economy is still weak would endanger the economic recovery.

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[7] Richard Kogan *et al.,* "Long-Term Budget Outlook Remains Challenging, But Recent Legislation Has Made It More Manageable," Center on Budget and Policy Priorities, June 27, 2013, http://www.cbpp.org/cms/index.cfm?fa=view&id=3983.

[8] Richard Kogan and Paul Van de Water, "How Much Deficit Reduction Is Needed Over the Coming Decade? Total Amount and Path of Savings Are Both Important," July 10, 2013, Center on Budget and Policy Priorities, http://www.cbpp.org/cms/index.cfm?fa=view&id=3989

[9] Paul Van de Water, "Don't Play Politics with the Debt Ceiling," *Off the Charts* blog, January 4, 2013, http://www.offthechartsblog.org/dont-play-politics-with-the-debt-ceiling/.

[10] Paul Van de Water, "Boehner Rule" Down But Not Out," *Off the Charts* blog, January 25, 2013, http://www.offthechartsblog.org/boehner-rule-down-but-not-out/.

In short, as the International Monetary Fund recently advised, policymakers should "[repeal] the sequester and [adopt] a more balanced and gradual pace of fiscal consolidation in the short term; expeditiously [raise] the debt ceiling to avoid a severe shock to the U.S. and the global economy; and [implement] a comprehensive and back-loaded set of measures to restore long-run fiscal sustainability."[11]

Protecting Americans with Limited Means

Sequestration does not affect most entitlement programs, such as key programs for low-income individuals and families. (There are some important exceptions, such as Medicare and federal unemployment benefits.) But it does affect important *discretionary* programs that promote opportunity for low-income people, including Head Start,[12] housing assistance,[13] child care assistance, and education funding targeted on low-income students.

As policymakers consider replacing sequestration with alternative deficit reduction, the potential impact on low-income people should be a central concern. Continuing sequestration would result in substantial cuts in important low-income programs. Yet replacing sequestration with harmful cuts in key programs that assist low-income families, such as SNAP or Medicaid — or pairing a debt-ceiling increase with cuts in these programs — could increase poverty and hardship substantially.

Similarly, rolling back the Affordable Care Act as part of a deal to replace sequestration or raise the debt ceiling would increase the ranks of the uninsured and could jeopardize access to health care for millions of Americans. This, too, should not be acceptable.

Large-scale deficit-reduction packages enacted in 1990 and in 1993 and the smaller 1997 package adhered to the principle that deficit reduction should not increase poverty or hardship; indeed, these packages included important antipoverty measures, such as expansions in the EITC and food stamps and the creation of the Children's Health Insurance Program (CHIP). Alan Simpson and Erskine Bowles have reaffirmed the principle that deficit reduction should not worsen poverty or hardship. Despite including substantial entitlement cuts, both the original Simpson-Bowles proposal and later iterations spared most means-tested entitlement programs (including SNAP) and provided for full implementation of the Affordable Care Act.

There is a serious risk, however, that some policymakers will try to target a substantial amount of deficit reduction on low-income programs. The budget plan that the House approved this spring (sometimes referred to as the Ryan budget) secured two-thirds of its $5 trillion in non-defense cuts from programs serving people of modest means.[14] In addition, House leaders have said that the

[11] International Monetary Fund, "Concluding Statement of the 2013 Article IV Mission to The United States of America," June 14, 2013, http://www.imf.org/external/np/ms/2013/061413.htm.

[12] Department of Health and Human Services, "The Numbers Are In: Sequestration Cuts 57,000 Kids from Head Start," August 2013, http://www.hhs.gov/secretary/about/blogs/head-start-numbers.html

[13] Douglas Rice, "Sequestration Could Deny Rental Assistance to 140,000 Low-Income Families," Center on Budget and Policy Priorities, April 2, 2013, http://www.cbpp.org/cms/index.cfm?fa=view&id=3945.

[14] Richard Kogan and Kelsey Merrick, "Chairman Ryan Gets 66 Percent of His Budget Cuts from Programs for People With Low or Moderate Incomes," Center on Budget and Policy Priorities, March 15, 2013, http://www.cbpp.org/cms/index.cfm?fa=view&id=3925.

House will consider a bill in September to cut SNAP by at least $40 billion and reduce or terminate benefits for millions of low-income families and individuals. And many House and Senate Republican members have voted repeatedly to repeal, defund, or otherwise undercut implementation of the Affordable Care Act.

Adequately Funding Public Services

The House budget resolution approved this spring would set total discretionary funding for 2014 at the post-sequestration level, while shifting about $50 billion from non-defense programs to defense and thereby leaving non-defense programs roughly $50 billion below the post-sequestration level. The Senate budget plan, by contrast, would set defense and non-defense discretionary funding at their *pre*-sequestration levels — the levels agreed to in the 2011 Budget Control Act[15] — and replace sequestration with alternative deficit-reduction measures. These starkly different approaches would have significant real-world consequences. For example:

- The House Appropriations Committee has not released an appropriations bill to fund the Departments of Labor, Health and Human Services, and Education in 2014, but under the House budget, funding for these departments is *18.6 percent below the 2013 post-sequestration level*, even before adjusting for inflation. If all programs funded through that bill were cut by this percentage, Head Start would be cut by $1.4 billion, K-12 education by $3.7 billion, and the National Institutes of Health by $5.2 billion below the 2013 post-sequestration levels.

  In 2013, a much smaller ($400 million) cut in Head Start forced 57,000 children from the program and shortened the amount of instruction for thousands more. In contrast, the Senate appropriations bill covering these departments raises funding in these areas above the 2013 post-sequestration level, essentially reversing the sequestration cuts for 2014.[16]

- The bill that the House Appropriations Committee passed this summer for the Department of Housing and Urban Development and the Transportation Department would slash funding for the HOME Investment Partnerships Program and the Community Development Block Grant program (CDBG), setting funding levels well below the 2013 post-sequestration levels.[17] These cuts would come on top of significant reductions in these programs enacted before sequestration took effect. Under the House bill, CDBG formula grants to states and localities would be *47 percent below* the 2013 post-sequestration level, a cut of $1.4 billion (not accounting for inflation); the amount that the House bill provides would be the lowest CDBG funding level, by far, since Congress created the program in the 1970s (after adjusting for inflation). Cuts of this depth would mean sharply reduced resources to help low-income communities repair streets and sewer systems, develop and preserve affordable housing, and provide basic services to seniors and children.

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[15] As reduced by $8 billion by the "fiscal cliff" bill, the American Taxpayer Relief Act.

[16] Some media accounts reported that the House intended to spare Head Start, special education, and the NIH from cuts. If these programs were funded at the 2013 *pre*-sequester level and the subcommittee did not use funding gimmicks, the other programs in these departments would have to be cut by 30 percent below the 2013 *post*-sequester level.

[17] For more information on the differences in funding for HUD programs, see Douglas Rice, "Senate HUD Funding Bill Reverses Harmful Sequestration Cuts in Housing Assistance," Center on Budget and Policy Priorities, July 19, 2013, http://www.cbpp.org/cms/index.cfm?fa=view&id=3993.

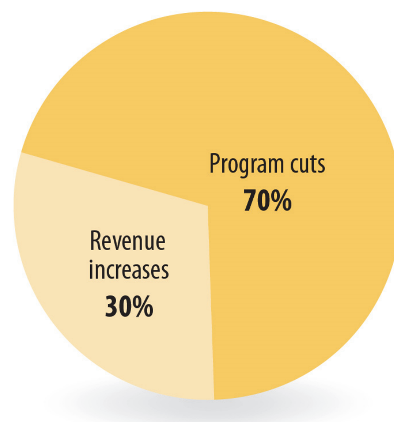
The House bill would also cut HOME funding by 26 percent, or $700 million, as compared to the 2013 post-sequestration level. HOME provides grants to states and localities that communities use, often in partnership with local nonprofit groups, to fund a wide range of activities that build, purchase, or rehabilitate affordable housing or provide direct rental assistance to low-income households. In contrast, the Senate bill would reverse the sequestration cuts in CDBG and HOME.

There are many more examples. For instance, the House appropriations bills would cut funding for the National Science Foundation, the Environmental Protection Agency, and international assistance well below the 2013 post-sequestration levels.[18]

It is important to note that discretionary funding will remain substantially below 2010 levels even if policymakers replace sequestration with alternative cuts and revenue measures. The BCA placed tight limits on both non-defense and defense discretionary funding. Over 2014-2023, total discretionary spending under those limits — even without sequestration — will be $1.6 trillion less than if policymakers had kept funding over that period at the 2010 level, adjusted for inflation, and non-defense discretionary spending will fall by 2017 to its lowest level on record as a percent of GDP, with data going back to 1962.[19]

Figure 1

70% of Recent Policy Savings To Reduce Deficits Have Come From Program Cuts



Note: Recent policy savings come from cuts in 2011 funding, Budget Control Act of August 2011, and American Taxpayer Relief Act of January 2013. Estimates are for 2014-2023 and assume sequestration does not occur.

Source: Center on Budget and Policy Priorities based on Congressional Budget Office and Joint Committee on Taxation data.

Adopting a Balanced Approach to Deficit Reduction

The deficit-reduction efforts of the last few years have been heavily weighted toward spending cuts. Excluding sequestration, some 70 percent of the deficit reduction enacted since 2010 has been from spending cuts, with just 30 percent from revenue increases (see Figure 1). If sequestration remains in place, this ratio will become an even more lopsided 78/22 split over the 2014-2023 period.[20]

Replacing sequestration over the next eight years while making further efforts to improve our longer-term fiscal condition should entail a more balanced approach that avoids significantly under-funding

[18] For information on international assistance funding in the House and Senate bills, see "Comparison of Senate and House FY14 State-Foreign Operations Bills," U.S. Global Leadership Coalition, August 2013, http://www.usglc.org/downloads/2013/08/FY14-State-Foreign-Operations-Appropriations-Analysis.pdf.

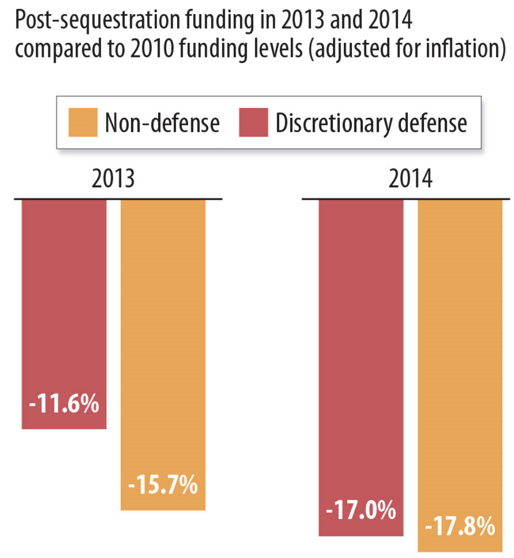
[19] We compare funding to 2010 levels because 2010 was the last fiscal year before Congress began cutting discretionary funding. Note that the fiscal year 2010 appropriations levels do not include funding related to the Recovery Act. Discretionary programs that received additional funds as part of the Recovery Act received those funds as part of their 2009 funding. While some of those funds were *spent* in 2010, they are not reflected in the 2010 *funding* levels.

[20] See Table 2 in Kogan and Van de Water, "How Much Deficit Reduction Is Needed over the Next Decade?"

key public services and eschews budget cuts that would increase poverty or leave more low-income individuals and families without access to health care.

In addition, longer-term tax policy could be on the agenda this fall. While policymakers are unlikely to enact tax reform this year, there could be discussion in budget negotiations of overall parameters for reform, including a revenue target. Given the need to raise revenues as part of a longer-term effort to reduce deficits and replace sequestration, it is critical that any movement toward reforming the tax code be accompanied by a firm agreement to raise additional revenues. Safeguards also will be needed to ensure that significant cuts in key entitlement benefits are not enacted ahead of measures that raise revenues, only to have the revenues then fail to materialize; the deficit-reduction plan that the Senate's bipartisan "Gang of Six" issued in July 2011 contained measures to insure that the entitlement cuts would take effect only if the agreed-upon revenue increases did as well, and vice versa.

Figure 2
Non-Defense Discretionary Cuts Have Exceeded Defense Cuts



Source: CBPP calculations based on data from the Congressional Budget Office.

Including adequate revenues is not the only form of balance needed. On the spending side, relief from sequestration should not be limited to increasing defense funding; it should include relief for non-defense discretionary funding as well. Since 2010, non-defense discretionary programs have been cut more deeply than defense. In 2013, funding for non-defense discretionary programs was 15.7 percent below the 2010 level adjusted for inflation, compared to 11.6 percent below for defense (see Figure 2). If sequestration continues in 2014, cuts to non-defense programs will continue to outpace the defense cuts, though by a smaller margin.

Despite these facts, some policymakers have called for rolling back only the defense sequestration.[21] This not only would leave key domestic needs underfunded but also would weaken pressure to reach agreement on a long-term budget deal. Policymakers specifically designed sequestration to secure half of its savings from non-defense programs and half from defense, so that both parties would be invested in reaching a budget agreement. If only defense is spared, many Republican policymakers will be less motivated to reach a compromise agreement that provides a more comprehensive and lasting solution to our fiscal challenges.

[21] Edward-Isaac Dovere, "At Camp Pendleton, President Obama takes on sequester politics," Politico.com, August 7, 2013, http://www.politico.com/story/2013/08/obama-camp-pendleton-sequestration-speech-95310.html.

SNAP Cuts Would Hurt Poor and Affect Program's Responsiveness in Future Recessions

The farm bill is another important issue before Congress this fall. The House is expected to consider a bill in September that would cut SNAP by at least $40 billion over ten years, with nearly all of the savings coming from benefit cuts. The House bill would eliminate food assistance for at least 4 million people, including at least 2 million poor adults not raising minor children who are out of work, live in areas with high unemployment, and have average incomes of only 22 percent of the poverty line.

The proposed SNAP cuts would hit many low-income households hard at a time when unemployment remains high. These cuts would also make the program less responsive to rising need during future recessions.[a]

[a] Dottie Rosenbaum, Stacy Dean, and Robert Greenstein, "Cuts in House Leadership SNAP Proposal Would Affect Millions of Low-Income Americans," Center on Budget and Policy Priorities, September 6, 2013, http://www.cbpp.org/cms/index.cfm?fa=view&id=4009.