United States Senate Budget Committee

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Murray's Deficit Reduction Goal Flawed And Dangerous

In a recent letter to the Democrat Conference, the new Chairman of the Senate Budget Committee, Senator Patty Murray, released a memo assessing the nation's fiscal situation. The memo asserted that over the last two years, Congress reduced deficits by $2.4 trillion, including "almost $1.5 trillion" in 2011 alone. These figures echoed claims made by President Obama at a press conference 10 days earlier: "We've made progress towards that goal [of reducing deficits by $4 trillion]. Over the past two years, I've signed into law about $1.4 trillion in spending cuts. Two weeks ago, I signed into law more than $600 billion [in tax increases]… When you add the money it will save in interest payments on the debt, all together that adds up to a total of about $2.5 trillion in deficit reduction over the past two years."[1]

The $1.4 trillion figure cited by Democrat leaders is important. In her memo, the Chairman heavily relies on this number to derive a set of other estimates, including an assertion that Congress has thus far achieved a 4:1 ratio of spending cuts to tax increases. Using these estimates, the Chairman concludes that a) our nation hardly requires any more deficit reduction, and b) the little additional deficit reduction we need to do should come at least as much from tax hikes as from savings.

Because it is central to claims made by both the Chairman and the President, this paper examines the validity of the $1.4 trillion estimate as a measure of deficit reduction and finds it deeply—indeed, dangerously—in error.

The $1.4 trillion estimated savings relies on four false assumptions, each of which is discussed below. Most importantly, this figure props up a false impression that we are making swift and significant progress towards fiscal health, when, in fact, we remain on an increasingly unstable and unsustainable course that is hurting growth and threatening Americans' financial future.

False Assumption #1: The correct starting point for analysis is August 2010.
The $1.4 trillion estimate of deficit reduction is calculated from extrapolating a Congressional Budget Office (CBO) discretionary baseline published in August 2010. The Chairman's memo justifies setting August 2010 as a starting point because it is "the last baseline of record prior to the implementation of a series of discretionary spending cuts." That seems an arbitrary reason to select this date, but it also produces an extremely rosy estimate of deficit reduction.

[1] On January 22 the President repeated the $1.4 trillion figure in a *Statement of Administration Policy* regarding H.R. 325.

For instance, picking August 2010 hides the fiscal impact of the President's health care law, enacted in March 2010. This is curious since supporters claimed it was "the greatest deficit reduction effort in two decades."[2] Why would the Chairman's model not choose a starting point that reflected the changes in future deficits caused by the health care legislation? Perhaps it is because that legislation sharply increases both spending and taxes over the 2013 through 2022 timeframe considered in the Chairman's memo.

CBO's latest estimates of the health care law shows that, on net, mandatory spending increases by $890 billion[3] and revenue increases by $1.1 trillion[4] over the current 10-year window. The selection of the starting point in the Chairman's study conceals these massive increases in entitlement spending and taxes. In turn, this allows the Chairman's memo to set forth a ratio of spending reduction to tax increases (4:1) that supports a tax increase agenda.

Perhaps the strongest reason to reject August 2010 as a starting point is that it produces a spending baseline that is abnormally high. There are a number of reasons why it is very high. One example, to illustrate the problem, is that the August 2010 baseline includes spending for the decennial census. Thus the model creates a baseline that assumes we perform the decennial census every year. Consequently, the $1.4 trillion includes approximately $80 billion in "savings" just by conducting the census every tenth year as required under Article 1 of the Constitution. It does not make sense to use an abnormally high estimate as a benchmark—unless you want to produce an abnormally high estimate of deficit reduction.

Regardless of what starting point is chosen, it turns out the results of the model are extremely sensitive to this decision. For instance, if one were to use the last baseline of record prior to the Democrats taking control of Congress (January 2007) the model would indicate that, since then, Congressional action on discretionary spending alone has *increased* deficits by $470 billion. (Note this paper does not support this claim since any estimate produced by the Chairman's model is flawed.)

False Assumption #2: Net deficit reduction can be measured solely by changes in spending caps.
The $1.4 trillion estimate of deficit reduction looks solely at changes made to appropriated spending subject to statutory budget caps. However, this is only one area of spending—which accounts for less than a third of all government outlays. It ignores other congressional actions that have, and will continue to, significantly *increase* spending that offsets any potential savings from lowering the budget caps. For instance, just in the last two years, we boosted spending on unemployment compensation by $69 billion, backfilled the Social Security Trust Fund by an additional $116 billion, and just spent another $55 billion[5] responding to Hurricane Sandy. Assuming one accepts the $1.4 trillion estimate (again, this paper does not), these three items alone knock the $1.4 trillion estimate down by $240 billion. But even this list is not exhaustive and doesn't contemplate the additional spending Congress will continue to do outside the caps. It

[2] See statement of Speaker Nancy Pelosi, March 25, 2009.
[3] CBO, letter to Speaker John Boehner, July 24, 2012.
[4] US House Committee on Ways and Means, July 25, 2012. See http://waysandmeans.house.gov/news/documentsingle.aspx?DocumentID=304547
[5] Does not include "disaster" spending allowed under the budget caps. Does include $9.7 billion in supplemental funds provided for the National Flood Insurance Program.

also does not take into account mandatory programs like food stamps, which are exempt from the caps and largely exempt from the fallback sequester. Asserting Congress has cut overall spending by $1.4 trillion by ignoring increased spending elsewhere is absolutely wrong.

False Assumption #3: Congress abides by spending limits.
What about the approximately one third of spending that is subject to spending caps? The Chairman's memo asserts that we've *already* reduced our deficit by "almost $1.5 trillion" because those caps were put in place. However, not a single dime of those asserted savings has actually occurred. The estimate assumes that over the next ten years, Congress will abide by the statutory spending limits—a characteristic rarely attributed to any Congress. Indeed, on six different occasions during the last Congress alone, the Democrat-led Senate (including the Chairman) voted to ignore budget discipline and waive the Budget Act. Is the Chairman now suddenly committed to defending, rather than voting again to waive, budgetary spending limits? Have Senate Democrats now abandoned their fight against the discretionary caps? Until the majority in the Senate ceases to lay siege to spending discipline, no one should treat future spending reductions as if they have already occurred.[6]

False Assumption #4: CBO estimates of discretionary spending predict future spending.
CBO's discretionary baseline is not intended to be an estimate of what is likely to happen in the future: "The CBO baseline is **NOT *a prediction*** of budgetary outcomes" [emphasis in original].[7] Yet, the Chairman's memo, by asserting we will have spent $1.4 trillion less than would have been spent otherwise, implicitly ascribes to CBO's baseline such predictive qualities. Her model uses an extrapolated CBO discretionary baseline from 2010. This insinuates that this was CBO's prediction of what would be appropriated in the future. By law, CBO does not try to guess what appropriations will be. The $1.4 trillion savings estimate is based on a subtle falsehood, that a set of numbers published by CBO in 2010 were predictions. They were not.

The Big Mistake: Focusing on deficit reduction instead of debt.
As has just been demonstrated, the $1.4 trillion deficit reduction figure is inaccurate. But even if we had achieved this amount of deficit reduction, it would do very little to alter our long-term course and continue to leave the economy in a state of weakened growth due to our extraordinarily large debt burden.

What is the correct number? That is the wrong question. The only reason we worry about deficits is because they increase our debt. It is our debt, not deficits, which threatens working Americans by discouraging private investment, curtailing hiring, and depressing wages.

Our goal as a nation—morally, socially, and economically—must be to balance the federal budget. We can surely accomplish that goal in 10 years. Instead, under the Chairman's scenario, the gross federal debt will rise by as much as $8 trillion over the next 10 years, with the long-term outlook even more dire, as entitlement and welfare spending continue to explode and as

[6] The President has also been of little help in setting and defending lower discretionary spending levels. He follows a cycle of: (1) fighting Republican demands for net spending reductions; (2) claiming credit for them once they are imposed on him; and (3) working to reverse them before they actually occur.
[7] Congressional Budget Office, *Baseline Basics: CBO Development and Presentation of the Current-Law Budget Outlook*, presentation to Senate Committee on the Budget staff, 2013.

interest payments climb past $1 trillion annually. This is a bleak future in which high rates of poverty, dependency, and long-term joblessness are the new and permanent normal.

The Chairman's memo grievously understates the scope and urgency of our fiscal dilemma. In 2010, when our gross debt was $13 trillion, Admiral Mike Mullen, Chairman of the Joint Chiefs of Staff, stated that our debt was the greatest threat to our national security. In December, only a few months ago, Mullen indicated time has only made our situation worse. He is correct. We spent $3.5 trillion last year, the second highest ever. That was $1.1 trillion more than we brought in. Today our debt is $16.4 trillion, or 102 percent of GDP. That is $133,000 for every household in the United States, a post-World War II record. Our high debt is suppressing growth to the extent that our economy *shrank* in the last quarter of 2012. We are in bad shape and it is getting worse. Next week CBO will produce a revised baseline that will likely show our spending and debt continuing to increase every single year at an unsustainable rate.

Yet, based on a deeply flawed assessment of deficit reduction, some Senators, as well as the President, seem to be concluding that we are close to having our fiscal house in order. The President's inadequate goal of getting, at least on paper, to "primary balance" (where revenues are not sufficient to pay the interest on our debt) will leave our gross debt stuck at approximately 100 percent of GDP. That level of debt that will continue to drag down the economy, keep millions of people unemployed every year, and leave us gravely vulnerable to the next economic shock.

That is not a path that will help the poor, the middle class—or anyone. It is a dangerous path, a path that leaves our country vulnerable to catastrophe.

1:1?

One of the few estimates in the Chairman's memo not connected to the $1.4 trillion figure is a calculation that both the President's Fiscal Commission and the Senate "Gang of Six" budget proposals would have achieved deficit reduction at a spending cut to revenue increase ratio of 1:1. This is used as a justification for demanding at least equal tax hikes to spending reductions in the future. Is this estimate accurate?

The memo does not provide enough information to reproduce the calculation for either plan. However, it does assert that 51 percent of the Commission's deficit reduction came from additional revenue. Here is what Bowles and Simpson said in May of 2011: "The ratio of spending cuts to revenue increases in the plan can be calculated in several different ways depending on which baseline is used, how interest savings are accounted, and other factors. Depending on which measures are used, revenues account for between 25 percent and 50 percent of the deficit reduction in the plan."