THE COMMITTEE FOR A
RESPONSIBLE FEDERAL BUDGET

Going Big Could Improve the Chances of Success

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The Committee for a Responsible Federal Budget

About

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The Committee for a Responsible Federal Budget is a bipartisan, non-profit organization committed to educating the public about issues that have significant fiscal policy impact. The Committee is made up of some of the nation's leading budget experts including many of the past Chairmen and Directors of the Budget Committees, the Congressional Budget Office, the Office of Management and Budget, the Government Accountability Office, and the Federal Reserve Board.

New America Foundation

Since 2003, the Committee for a Responsible Federal Budget has been housed at the New America Foundation. New America is an independent, non-partisan, non-profit public policy institute that brings exceptionally promising new voices and new ideas to the fore of our nation's public discourse. Relying on a venture capital approach, the Foundation invests in outstanding individuals and policy ideas that transcend the conventional political spectrum. New America sponsors a wide range of research, published writing, conferences and events on the most important issues of our time.

Going Big Could Improve the Chances of Success

Introduction

As the Joint Select Committee on Deficit Reduction (Super Committee) tries to identify $1.2 - $1.5 trillion in savings to meet its mandate, it should consider Going Big instead. While forging bipartisan consensus on even $1.2 trillion in saving is no easy task, a Go Big approach of saving two to three times as much could actually *increase* the chances of success.

Many lawmakers, business groups, experts, and other organizations from both sides of the political spectrum support the need for a bold approach to control rising debt and strengthen the economy, including 44 Senators, 155 business groups, and dozens of other experts and former government officials. (See CRFB's Go Big website at http://crfb.org/go-big.)

But a Go Big approach is not just what is needed to get control of the debt from a policy perspective, a comprehensive approach can also improve the chances of success from three main factors:

- **Political Trade-Offs.** Putting everything on the table, especially the drivers of future debt, would allow the political trade-offs necessary to tackle entitlement and tax reforms to be considered.

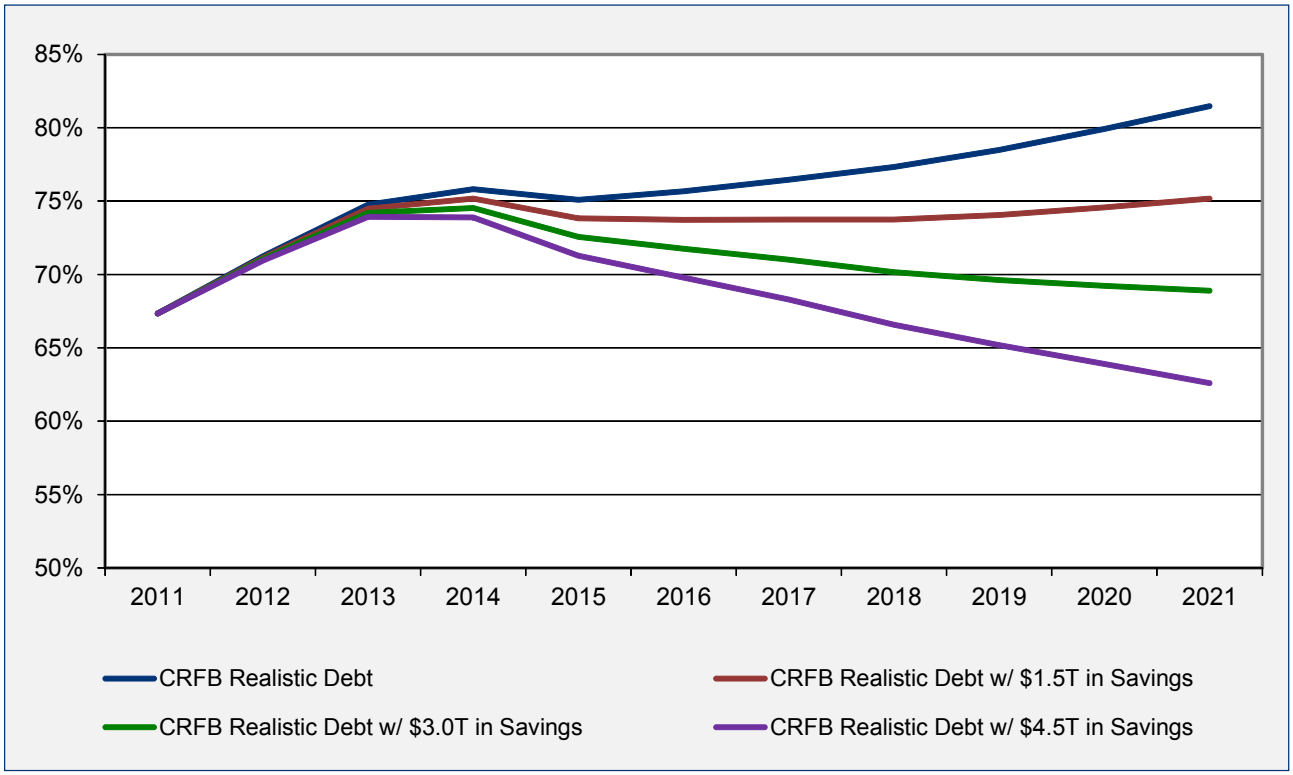
- **Shared Sacrifice.** A comprehensive approach would promote a sense of shared contributions, improving political support while reducing push-back from constituencies and interest groups who would otherwise feel singled out.

- **Economic and Political Gains of Debt Reduction.** Stabilizing the debt would boost confidence, strengthen the economy over the longer-term, provide greater certainty and an improved business environment, and reassure markets and credit agencies—none of which would be matched by a smaller deal.

"Go Big" and the Debt

From a policy perspective, there is no question that Going Big is preferable. Compared to realistic projections of what the future debt path might look like, the Super Committee will have to double or triple its current mandate to identify savings of $1.5 trillion in order to put debt on a clear, downward path by the end of the decade.

FIG 1. Illustrative Debt Paths (Percent of GDP)



Note: For details on CRFB Realistic Baseline, see http://crfb.org/document/analysis-cbos-august-2011-baseline-and-update-crfb-realistic-baseline.

The benefits of a comprehensive fiscal plan that stabilizes and reduces debt this decade, and continues to do so over the long-term, are numerous. A large enough package would buoy business, market, and consumer confidence—both from an improved economic outlook and renewed faith in the U.S. political system to address critical challenges. A stable and declining debt path could significantly strengthen the economy over the long-term, as falling public borrowing needs made way for greater private sector access to capital. There are also intergenerational benefits to consider from a lower debt burden on future generations. Perhaps most importantly, putting debt on a stable and downward path would significantly reduce, if not eliminate, the risk of a fiscal crisis.

Political Tradeoffs

It is difficult to imagine any real plan crafted from spending cuts alone or revenues from the well-off alone, regardless of what either side might say or want. It is also extremely difficult to figure out how to break the logger-jam about revenues and entitlements in a smaller deal.

While it is mathematically possible to put a package together on paper that adds up to $1.2 trillion in savings relying heavily on one side of the budget, as groups on both sides of the political spectrum have done, the politics do not lend themselves to a one-sided deal. Democrats are highly unlikely to agree to significant spending cuts or put meaningful entitlement reform on the table without a commitment to include revenues as part of a package. For their part, Republicans have consistently opposed proposals to raise revenues outside the context of comprehensive tax reform and without meaningful entitlement reform.

Putting together a spending cut only package of $1.2 trillion in savings requires the inclusion of policies that Democrats have either rejected or indicated they were only willing to accept as part of a package that included revenues. Similarly, proposals that have been put forward achieving $1.2 trillion in savings with a significant revenue component contain tax provisions that Republicans have rejected or would only consider as part of comprehensive tax reform. While both approaches work on paper, neither provides a useful roadmap for the Super Committee to follow to reach a bipartisan agreement.

If the Super Committee takes an incremental approach of going through the options for savings one at a time to identify areas of agreement, it will be extremely difficult to come to agreement on more than about $800 billion in debt reduction without tackling the biggest problem areas of the budget – entitlements and the tax code.

Such a plan could theoretically be developed by using all the mandatory savings that have been identified in past budget negotiations, accounting for roughly $300 billion. Additional savings could be achieved by adopting the chained CPI for indexing all parts of the budget for an additional $250 billion in savings and possibly a small amount of additional discretionary savings, though there will be resistance to further reductions on both the domestic and defense side of discretionary spending. It may be possible to achieve a modest amount of additional savings from user fees and closing smaller tax loopholes, but any significant amount of additional revenues would create a large pushback from Republicans if not in the context of comprehensive tax reform.

Even then, putting together an $800 billion plan requires optimistic assumptions about what is politically possible. It is not politically possible to achieve significant savings without tackling entitlement costs, and, thus, negotiations to achieve a smaller deal may well hit the wall, or have to resort to using gimmicks such as counting savings from the drawdown of troops that is already in place and incorporated into realistic budget projections.

Conversely, a Go Big approach satisfies conditions from both sides of the political spectrum. In fact, it may be the *only* way to satisfy both Democratic and Republican demands. It's a package deal: revenues come with entitlement reforms and vice versa. Bringing these areas of the budget into the fray could improve the chances of agreeing on a much larger package of savings than one that met the $1.2 trillion savings mandate. It is difficult to see how introducing entitlement and tax reforms into the discussions does not push up the overall savings *significantly*.

A larger package would by necessity include the tradeoffs and compromises necessary to reach a bipartisan agreement. Crafting a larger package would have to include changes to entitlements since that is where the bulk of federal dollars go. Moreover, with the past round of savings concentrating on discretionary spending, there is far less room to find new savings there. And the largest programs and major drivers of the debt – Social Security, Medicare, and Medicaid – would have to be included. But, Democrats will not consider these without a commitment to a package with revenues. The President made this position explicit in his submission to the Super Committee, stating he "will veto any bill that takes one dime from the Medicare benefits seniors rely on without asking the wealthiest Americans and biggest corporations to pay their fair share," and Congressional Democrats have repeated that position.

Republicans have rejected numerous proposals to increase revenues through rifle shot tax changes, but have on several occasions indicated a willingness to consider additional revenues if they are part of an overhaul of the current tax system to make it more pro-growth. This is the approach taken by the Simpson-Bowles Fiscal Commission, the Domenici-Rivlin proposal, and the Gang of Six, all of which received bipartisan support. Increased revenues from comprehensive tax reform was a key element of the "grand bargain" discussed by President Obama and House Speaker John Boehner this past summer.

A comprehensive reform of the tax code would effectively replace the 2001/2003/2010 income and estate tax cuts that are scheduled to expire at the end of next year, so any tax reform must be viewed in context of the positions that have been taken on extension of those tax cuts. In particular, President Obama has stated that he would veto an extension of the tax cuts for taxpayers with incomes above $250,000 a year. Democrats, therefore, have no incentive to agree to a tax reform plan that doesn't result in at least $800 billion in revenues relative to extension of all the tax cuts, which is the amount that would be achieved if the tax cuts President Obama has threatened to veto are allowed to expire.

In addition, Republicans also are far more likely to consider revenues when paired with structural entitlement reforms that would ensure that revenues would be used to finance deficit reduction rather than supporting unsustainable programs. To qualify as serious entitlement reforms will require more savings than what the President proposed in his submission to the Super Committee. In our analysis, we estimated that the President's submission saved only about $540 billion from mandatory programs while completely ignoring the need to shore up Social Security.[1]

Speaker of the House John Boehner (R-OH) has reaffirmed the need for serious entitlement reforms in recent weeks when referring to the grand bargain that he and the President were working toward over the summer, but which never came to fruition. He has stated that $800 billion in new revenues were on the table only if the President was "willing to make fundamental changes in our entitlement programs."

As Figure 2 illustrates, when all areas of the budget are taken into consideration, the package that would achieve at best $800 billion in savings under an incremental approach would easily exceed $2 trillion and approach $3 trillion. At that point, Super Committee members would have a powerful incentive to take extra steps if necessary to stabilize the debt.

[1] See the Committee for a Responsible Federal Budget, "Analyzing the President's Submission to the Super Committee." September, 20, 2011. http://crfb.org/document/analyzing-presidents-submission-super-committee.

FIG 2. Illustrative Scenarios and Associated Savings

Budget Category	Incremental Approach	Go Big Approach
Government Wide	**$250 billion** from chained CPI	**$250 billion** from chained CPI
Possible Discretionary Savings	**$100 - $200 billion** from modestly slower growth in BCA caps	**$300 - $400 billion** from slower growth in BCA caps
Possible Health Care Savings	Negligible savings because of unlikelihood that lawmakers tackle health spending unless in context of large package	**$600 - $900 billion** from reforms to Medicaid state gaming, payments to drug companies, TRICARE, increase means-testing of premiums, increasing Medicare cost-sharing, Medigap restrictions, raise Medicare eligibility age, and other payment cuts; plus tort reform, Medicare premiums, and considering premium support
Possible Other Mandatory Savings	**$150 - $250 billion** from reforms to farm subsidies, federal civilian and military retirement and benefits, Fannie and Freddie, and other programs	**$300 - $350 billion** from savings in $600 billion scenario, plus in-school interest subsidies for undergraduates and various user fees
Possible Social Security	Unlikely to be reformed in a smaller package	**$150 - $300 billion** from raising the taxable maximum, indexing the retirement age to longevity, and slowing the growth of benefits for higher-earners
Revenues	Negligible savings because of unlikelihood that lawmakers tackle revenues unless in context of large package	**$800 billion - $1.2 trillion** from comprehensive reform that lowers rates and broadens tax base
Net Interest	**$100 billion**	**$450 - $600 billion**
Total Savings	**$600 - $800 billion**	**$3 - $4 trillion**
Debt in 2021 (% GDP) Compared to Current Policy Baseline*	**78% - 79%**	**65% - 69%**

Note: Numbers may not add due to significant rounding.
*Current policy baseline assumes all 2001/2003/2010 income and estate tax cuts extended, AMT patches, yearly "doc fixes", and war drawdown. See http://crfb.org/document/analysis-cbos-august-2011-baseline-and-update-crfb-realistic-baseline for more information.

Shared Sacrifice

Achieving hundreds of billions of dollars will no doubt involve difficult decisions on the part of lawmakers that will generate controversy and opposition from affected parties. However, expanding the size and scope of the overall package could promote a sense of shared sacrifice and fairness on behalf of the American public and key interest groups, making it more likely that they would accept changes if they knew that everyone was contributing to the solution.

An incremental approach would give advocates for parts of the budget that are affected a legitimate argument that they are bearing an unfair burden, since their share of the deficit reduction package will almost certainly be much greater than their share of the budget. Opponents of specific savings would all be able to argue that their program could be spared and the savings made up with relatively modest savings in areas left out – notably, entitlement programs and revenues. A Go Big approach that achieves savings in all parts of the budget neutralizes that argument.

Fiscal Commission co-chairs Erskine Bowles and Alan Simpson frequently note that by making their plan larger, it was actually easier to garner support. In an op-ed published in the Washington Post on October 2nd they wrote:

> *When we presented our co-chairmen's proposal to the rest of the fiscal commission in November, Washington insiders were shocked that we so aggressively exceeded our mandate. They were sure that the proposal would need to be scaled back to get a majority vote. It turned out that the opposite was true. The more comprehensive we made it, the easier our job became. The tougher our proposal, the more people came aboard.*
>
> *Commission members were willing to take on their sacred cows and fight special interests — but only if they saw others doing the same and if what they were voting for solved the country's problems. This spirit of shared sacrifice gained us broad bipartisan support, spanning from Democratic Sen. Dick Durbin to Republican Sen. Tom Coburn. We would not have garnered that type of support had we not taken on defense, domestic programs, the solvency of Social Security, health care, and spending in the tax code all at once.*

Going Small: Lots of Pain for Not So Much Gain

A small package of savings would be comprised of provisions which have savings that are relatively modest in the context of the overall size of the deficit, but which nonetheless are likely to generate intense opposition from affected constituencies. Such changes could include reforms to federal retirement programs, agriculture policy, pension funding, and other areas. While a package of this type would offer some improvement to our fiscal situation, it would not offer the economic benefits of a declining debt path or renewed confidence by businesses, markets, or the American public. The public would see a package of tough choices *and* a debt burden that continues to grow. In essence, it would deliver *political pain for not so much gain*.

A small package would necessitate policymakers having to return to debt reduction in the near future, either prudently or in response to a fiscal crisis. It would be a job not yet completed and could easily prompt additional downgrades for the U.S. by rating agencies if they conclude that our political system is not capable of enacting the policy changes necessary to put the country on a sustainable course. By delaying a full solution to the problem, policymakers risk exhausting their current political capital, which could make forging agreement on yet another debt reduction package that much more difficult.

Moreover, it would leave in place considerable policy uncertainty since it would quickly become apparent that further spending cuts and/or revenue increases would be necessary. Consequently, an incremental approach would not be able to benefit from one of the stronger arguments in favor of deficit reduction – the near term sacrifices that each party must accept for deficit reduction will protect their respective interests in the future. That argument only works for a Go Big package which stabilizes the debt.

Democrats have an interest in controlling the rise of debt because it leads to higher interest payments, which crowd out other areas of the budget and potential new areas to invest in and devote scarce public resources towards. Moreover, the experience of the past year demonstrates that large deficits and a growing debt burden create pressure for repeated cuts in domestic programs. Hence, a compelling case can be made that controlling the central drivers of future deficits, notably entitlements, serves their interests.

Republicans, on the other hand, have an interest in controlling rising debt and spending levels because they threaten the economy with higher taxation down the road. The conservative icon Milton Friedman noted many years ago that low taxes and high deficits and debt today mean higher taxes in the future. So to the extent that health care and retirement costs threaten to continue pushing spending, deficits, and debt up, the threat of higher taxes in the future will be present.

A package achieving $1.2 trillion in savings would mean that progressives would have to accept cuts in programs they care about and conservatives would have to accept higher revenues, while still facing the ongoing threat of deeper cuts and further tax increases. Only a Go Big approach can sufficiently address both concerns, and it could make the process of forging a consensus ultimately less challenging if both side's long-term objectives were being met.

The American public is hungry for a grand bargain. They want an agreement that truly solves the problem, not another deal to kick the can down the road. As Fiscal Commission Co-Chairman and CRFB Board Member Al Simpson has said, "Small ideas have no ability to inspire."

The Super Committee already has its work cut out for it in its quest to recommend $1.2 - $1.5 trillion in savings. Fortunately, Go Big can boost their chances of success while also setting the country on a path to a sustainable fiscal future.