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Before the
Task Force on Federal Expenditure Limits
Committee on Rules

U.S. House of Representatives

February 6, 1980

Mr. Chairman, I welcome this opportunity to comment on the proposals before you that would amend the Congressional Budget Act of 1974 to place a limit on the growth of federal expenditures.

I believe that the Congressional Budget Act of 1974 has already given the Congress the tools to control expenditure growth. Members of Congress now have to vote on the budget's totals as well as on its parts. A case can be made, however, that the forces in favor of increasing the parts are far stronger than those supporting a limit on the whole. The bills before you today attempt to redress this perceived imbalance in one of two ways: by including a formula in the Budget Act that would create a limit that the Congress would have to live within or explicitly reject, or by requiring that the Congress first vote on budget totals and then limit the parts to those totals. Each of these strategies could create problems, particularly during recessions. Neither strategy, moreover, will guarantee that spending control or reductions are brought about in thoughtful, effective ways. I personally believe that for this to happen the Congress will have to abandon one-year-at-a-time budgeting and adopt a multiyear process within the framework of the Congressional Budget Act so that legislative savings can be achieved over a series of years.

Cause for Concern

Strong arguments can be made for lower levels of federal expenditures. The relative size of the federal sector has grown substantially over the last 30 years as a result of increased benefit payments to individuals along with rising federal grants to finance a wide variety of state and local government services. Federal outlays rose from an average of 18.2 percent of gross national product (GNP) during the 1950s, to 19.5 percent during the 1960s, to 21.2 percent during the 1970s. If current high levels of international tension persist, pressures for increased defense expenditures will not subside. In this environment, unless expenditures for other programs are reduced, the relative size of the federal sector could continue to grow in the 1980s.

Many believe that this growth in federal spending is wasteful or even harmful and should be reduced in order to leave more room for private spending. Moreover, concern with the growth of federal spending serves as a proxy for a more general concern with the growth of government power and the pervasiveness of government regulations.

The growth of federal spending in recent years has been financed partly by allowing inflation to increase the individual tax burden and partly by persistent federal deficits. President Carter's 1981 budget allows the tax burden to grow to a postwar high; one has to go back to 1944 to find federal revenues at a greater percentage of GNP.

In fiscal year 1980, moreover, the federal budget will be in deficit for the eleventh straight year, the nineteenth time in the last twenty years, the forty-second time in fifty years. While deficits and surpluses are possible with either large or small budgets, many feel that rapid expenditure growth makes it more difficult to achieve a budget balance.

The Case for a Limit

The case for placing a limit on the growth of federal expenditures rests on the contention that our present political system is biased toward increased spending. Those who believe this is true point to the fact that the benefits of a particular federal program tend to be concentrated on a relatively small group, each member of which stands to gain substantially from the program, while the costs are spread over a large number of taxpayers each of whom will lose only a little. Hence, elected officials are in a difficult position: if they vote against a program increase or champion a cut, they will encounter the vocal and well-organized opposition of the program's beneficiaries without earning more than a weak nod of approval from those who see their share of total taxes reduced by a small amount.

But while taxpayers are willing to go along with a slight increase in their taxes for a particular program, they are most upset when they see their tax bills rising dramatically from the effect of many small increases. Thus, at any one time two types of majorities exist in the electorate and in the Congress.

Program by program, majorities exist to maintain or increase funding. But when the programs are added together to form a unified budget, a majority favors reducing the total level of funding.

Cutting down the individual parts to fit within a desired whole is what budgeting is all about. Those who believe that the current process is biased toward increased expenditures feel that in the Congress the specific majorities in favor of greater funding for individual programs tend to win out over the general majority in favor of a reduced total expenditure level.

## The New Budget Process

The thesis that our system has a built-in bias toward spending had considerable validity as long as spending and tax bills were voted on one at a time and the Congress had no opportunity to debate or vote on the overall size of the budget or the magnitude of the deficit. But since the Congressional Budget Act of 1974, the Congress has required itself to consider and adopt overall spending totals and to vote explicitly on the planned deficit or surplus. Under the new procedures, those who would add to spending must visibly increase the total of expenditures and the deficit or must propose compensating cuts.

It is still too early to tell what effect this new process will have on spending and deficits. The fragmentary evidence that we have can be read both ways.

The process was implemented during the most severe recession since the 1930s. Much of the expenditure growth and deficits of the past four years can be attributed to the effect of the recession on the budget and the planned fiscal policy that the Congress adopted to speed the recovery. Many believe that expenditures would have grown faster and deficits have been even larger if the budget process had not required explicit votes on spending totals and the deficits.

There are signs that the process does provide the tools for controlling expenditure growth. Last session, for the first time, the Senate voted to invoke the budget process' reconciliation procedure by requiring six committees to cut outlays by $3.6 billion. While this step was dropped in conference because it was felt that House Committees had already agreed with a House Budget Committee request to consider a series of legislative savings, a precedent has been set.

Strengthening the reconciliation process is an alternative to setting formal expenditure limits that this Committee might want to consider. Allen Schick has suggested that the reconciliation process be tied to the first concurrent resolution on the budget. Under such a procedure, the House, in the first budget resolution, could mandate that one or more of its Committees report out legislation prior to the consideration of the second concurrent resolution that would result in lower spending for entitlement programs or other forms of uncontrollable spending. The various authorizing committees would retain their authority to determine which legislative savings were reported, and the House and Senate would still be free to reject or pass any proposed legislation.

## Advantages and Disadvantages of Various Limiting Procedures

The bills before you are superior to many of the Constitutional amendments that have been introduced in this Congress, in that by retaining simple majority voting on budget matters they would not prevent a Congressional majority from doing what it wants to do. Past attempts at budgetary reform illustrate the futility of trying to prevent the Congress from doing what a majority wants to do. In 1946, as part of the Legislative Reform Act of that year, a budget process was created in which fixed budget totals were set early in the Congressional year. Within a year the Congress determined that such a system would not work and it was abandoned.

### Bills That Contain a Formula

The formulas of the various proposals before the Congress can be grouped into three categories: (1) those that set a fixed maximum percentage growth rate for expenditures; (2) those that tie the maximum growth rate of expenditures to the growth of the economy; and (3) those that limit expenditures to a percentage of the economy.

Fixed percentage growth rate formulas--such as those of H.R. 309, 864, 865, 866, 867 and 868--would either require dramatic cuts in real spending levels during periods of high inflation, or would not significantly limit expenditure growth during periods of low inflation. The other two types of formula could severely restrict the Congress's ability to respond to a recession.

Federal budgetary expenditures are sensitive to economic conditions; for each percentage point rise in the unemployment rate, total outlays will increase from $5 to $7 billion as payments for unemployment insurance, Social Security, food stamps, and other countercyclical programs grow. Unless the Congress chose to set aside the limit, other programs would have to be cut to make room for these additional monies.

Some of the bills, such as H.R. 5371 and H.R. 6021, tie the limit to a measure of the size of the economy--GNP--which falls in recession. Thus, at the very time when you might want greater expenditures to stimulate the economy, these formulas would require cuts. Tables 1 and 2 give some idea of the magnitude of the required cuts that would be brought on by a hypothetical severe recession. We tested the formulas of three of the bills under two sets of economic assumptions: those that underlay the five-year current policy projections of the Second Concurrent Resolution for Fiscal Year 1980, and a hypothetical recession in calendar years 1980 and 1981 of the magnitude of the 1974-1975 downturn. These estimates are for illustrative purposes only; they were made assuming that the economic targets were achieved either through tax policy or other forces in the non-federal

TABLE 1. HOW THREE EXPENDITURE LIMITATION FORMULAS BECOME MORE RESTRICTIVE AS THE ECONOMY DECLINES FOR FISCAL YEARS 1981 THROUGH 1984: IN BILLIONS OF DOLLARS

| | Actual 1979 | Second Concurrent Resolution 1980 | Projections 1981 | 1982 | 1983 | 1984 |
|---|---|---|---|---|---|---|
| Higher Projected Outlays Caused by Increased Unemployment | 0 | 0 | 11.4 | 16.0 | 18.4 | 20.3 |
| Amount by Which Limit is More Restrictive Because of Lower GNP | | | | | | |
| H.R. 4610 | -- | 0 | 0 | 10.2 | 46.6 | 55.6 |
| H.R. 5371 | -- | -- | 37.9 | 45.0 | 49.9 | 55.9 |
| H.R. 6021 | -- | -- | 51.3 | 63.1 | 69.2 | 76.9 |
| Total Amount by Which Limit is More Restrictive | | | | | | |
| H.R. 4610 a/ | -- | 0 | 11.4 | 26.2 | 65.0 | 75.9 |
| H.R. 5371 a/ | -- | -- | 49.3 | 61.0 | 68.3 | 76.2 |
| H.R. 6021 b/ | -- | -- | 62.7 | 79.1 | 87.6 | 97.2 |

a/ From outlays only.
b/ From the sum of outlays and tax expenditures.

SOURCE: Congressional Budget Office.

TABLE 2. ECONOMIC ASSUMPTIONS ASSOCIATED WITH THE PROJECTIONS OF TABLE 1

| | Actual 1979 | Second Concurrent Resolution 1980 | Projections 1981 | Projections 1982 | Projections 1983 | Projections 1984 |
|---|---|---|---|---|---|---|
| Economic Assunptions Underlying the Five-Year Current Policy Projection for Second Concurrent Resolution for Fiscal Year 1980 | | | | | | |
| Nominal GNP Calendar Years | 2,336.0 | 2,571.0 | 2,888.2 | 3,246.7 | 3,616.5 | 4,018.8 |
| Nominal GNP Fiscal Years | 2,291.1 | 2,500.5 | 2,804.7 | 3,147.7 | 3,512.0 | 3,903.5 |
| Unemployment Rate Fiscal Years | 5.9 | 7.2 | 7.2 | 7.0 | 6.7 | 6.4 |
| CPI Fiscal Years | 10.1 | 9.8 | 8.8 | 8.0 | 7.2 | 6.8 |
| Economic Assunptions Underlying a Hypothetical Recession of the Magnitude of the 1974-1975 Downturn | | | | | | |
| Nominal GNP Calendar Years | 2,336.0 | 2,526.6 | 2,685.5 | 3,004.9 | 3,348.3 | 3,721.9 |
| Nominal GNP Fiscal Years | 2,291.1 | 2,504.0 | 2,624.5 | 2,922.4 | 3,260.5 | 3,624.1 |
| Unemployment Fiscal Years | 5.9 | 6.8 | 8.9 | 9.4 | 9.2 | 9.1 |
| CPI Fiscal Years | 10.1 | 9.8 | 8.8 | 8.0 | 7.2 | 6.8 |

sector, and that the Congress chose not to set aside the expenditure limit. As you can see, the cuts in expenditures required by the decline in GNP are much greater than the higher outlays resulting from increased unemployment. It would seem, therefore, that periods such as this year, when most economic forecasters foresee a recession, would be a particularly difficult time to implement any formula tied to GNP. The Committee might want to substitute an economic indicator such as Trend GNP or Potential GNP that does not follow economic cycles.

Tying expenditures to predicted GNP would create intense pressures on the budget committees and on organizations such as CBO to produce optimistic GNP projections so that additional money might be spent. For example, in the CBO forecast that was just released last week nominal GNP was projected to be between $2,860 and $3,086 billion in calendar year 1981. This is a range over which there can be reasonable disagreement. But depending on which end of the range was used in applying the formula, total outlays under H.R. 5371 could shift by $47.5 billion and the total of outlays and tax expenditures under H.R. 6021 could shift by $64.4 billion.

## Perverse Incentives of Limitations

Strictly enforced limitations on federal spending would probably not reduce pressures for new federal activities, but might well change their form. The Congress could avoid the budget limits altogether by using the regulatory power of the federal government to force the private sector or states and localities to bear the cost of new programs. Employers, for example, could be asked to bear the major cost of national health insurance. New off-budget agencies or government-sponsored corporations could be created. Increasing use could be made of federal loan guarantees or other devices to allocate private credit to activities deemed especially desirable by the federal government. A limit that applied solely to the spending side of the budget would also be likely to encourage the use of tax subsidies to particular activities. Indeed, even without such a limit, subsidies granted through the tax code have been increasing at a faster rate than outlays in recent years--to an estimated $182 billion in fiscal year 1980.

One effect of the new budget process has been to draw Congressional attention to the current magnitude of tax expenditures, off-budget agencies, and credit activities of the federal government and to increase efforts to bring these activities within the purview of the budget process. CBO believes that Congressional control of the full range of federal activities would be enhanced by bringing off-budget spending agencies back on budget, by compiling a credit budget showing various loan and loan-guarantee activities of the government, and by reviewing tax expenditures on the same basis as direct expenditures. The credit control proposals of Representatives Giaimo, Holt, and Manetta, and the tax expenditure proposal of Representative Giaimo are steps in the right direction and should be seriously considered by the Congress.

Changing the Order of Decisions

If the Committee believes that the majorities in favor of limiting the growth in budget totals need help from the budget process, it could go the route of amending the Budget Act to require that votes be taken on the totals prior to votes on the functions.

This approach has been suggested in different forms by Representatives Gephardt and Holt. It would have the advantage over strict formulas of giving the Congress the flexibility to set its own limit each year. At the same time, by highlighting the votes on the totals, it might create downward pressure on expenditure growth.

It must be remembered, however, that the parts and the whole cannot be separated. I believe it would be a mistake to have a binding vote on the totals prior to taking up the parts. Such a procedure could result in unrealistically small budget resolutions that would have to be amended several times during the fiscal year as specific spending and tax bills were approved. If this occurred, the entire Congressional budget process would lose its credibility. To avoid the problem you might want to consider the following sequence of votes: a vote on the budget totals, votes on the parts of the budget resolutions, a second vote on the budget totals to reconcile the parts with the whole, and a vote on final passage. This procedure would highlight the totals more than the current one and could exert downward pressure on spending.

How to Bring About Cuts

Mandating slower expenditure growth as reflected in the figures of budget resolutions will not necessarily bring about a true reduction in the growth of the budget. Any expenditure limit will have to be accompanied by other changes in the way the Congress passes its budget. The major force that has driven budgetary growth in the past two decades, and promises to drive it in the next decade, is the growth in entitlements and other types of spending that are difficult to modify in the short run. The level of expenditures for entitlements cannot be changed unless the basic authorizing statute is modified. The current mood to increase spending for defense procurement by a substantial amount means that in the next few years defense outlays will begin to rise because of budget authority granted now.

As long as the budget process operates one year at a time, therefore, it will be difficult to achieve significant cutbacks without causing major hardships, leaving projects unfinished, and disappointing expectations. If the Congress is to cut spending in an orderly way, it must plan at least three years ahead and must seriously consider phasing out and restructuring programs and reducing the rate of growth of entitlements. The Long Amendment to the Debt Limit bill last year was a first step toward multiyear planning, but the Congress has yet to adopt an organized and coordinated plan for making cuts over several years.

While a multiyear approach would allow the Congress to plan cuts, a formula restricting overall growth in the next budget would force last-minute, unplanned cuts as changing economic conditions caused federal outlays to rise and revenues to fall. Any reform to place a limit on federal budget outlays should therefore be accompanied by the adoption of multiyear targets to facilitate the orderly achievement of the required budget totals.