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A Responsible FY 2008 Budget: House Republican Substitute Focuses on Spending and Economic Growth

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The budget blueprint reported out of the House Budget Committee last week and supported by Democratic leadership is a study in fiscal irresponsibility. Coming on the heels of a campaign season in which Democrats slammed Republicans' profligacy, the House budget resolution boosts discretionary spending, does nothing to tackle out-of-control entitlement spending, and, worst of all, would impose the largest tax increase ever on the American people. The shortcomings of this budget are thrown into relief by a substitute proposal made this week by Representative Paul Ryan, ranking member of the House Budget Committee, and House Republicans. The Republican budget would freeze non-defense discretionary spending while directing more money to priority areas, take several steps toward entitlement reform, strengthen budget enforcement, and extend the 2001 and 2003 tax cuts that have done so much for the economy. The Republican budget sets a standard that Congress should strive to meet.

The Democrats' Budget. The House budget resolution reported out of committee and scheduled for a floor vote this week makes much of the claim that it would balance the budget in just a few years. And it would accomplish this goal on the backs of taxpayers. Even so, the balanced budget would be temporary because the budget does not take steps to rein in coming increases in Medicare, Medicaid, and Social Security.

To begin with, the budget assumes tax increases of \$900 billion over five years, which would be accomplished in part by allowing the 2001 and 2003 tax cuts to expire. These tax cuts have been successful at promoting economic growth by reducing disincentives to work and encouraging investment. Since their enactment, economic growth has been robust, and the economy has added nearly 8 million new jobs. Allowing these tax cuts to expire risks great damage to the economy and would raise taxes on 4.7 million Americans.¹ In addition, the budget does not provide for an "AMT fix" that would prevent the Alternative Minimum Tax's boom from sweeping in more Americans.

Further, the budget proposes large increases in spending on tax compliance and assumes that the result will be additional revenues squeezed out of taxpayers. But IRS officials are less optimistic, predicting that the increased revenues would be minor—nowhere near enough to pay for the budget's spending increases. Moreover, the last time Congress acted to eke more funds out of the "tax gap," it set the stage for widespread IRS abuses, eventually sparking a taxpayer backlash.² With the

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greater complexity of the tax code today, it is likely that taxpayers would suffer even more.³

The budget would use these increased revenues to pay for increases in non-defense discretionary spending, boosting such spending by \$22.5 billion in FY 2008. Further, the budget assumes that non-defense discretionary spending will rise faster than the projected rate of inflation from FY 2009 through 2012.

At the same time, the budget's pay-as-you-go (PAYGO) provision would allow for increases in entitlement spending if matched by additional tax increases. The budget also includes an additional \$115 billion in "reserve fund" spending that would have to be offset by cuts elsewhere or (more likely) still more tax increases.

A Difference in Vision. The Republican substitute budget differs significantly from the majority's proposal. While it would also balance the budget, by 2012, it would accomplish this without raising taxes. The key to the plan is freezing discretionary spending and starting to reform the big entitlement programs.

On the tax side, the Republican budget would extend the 2001 and 2003 tax cuts, thus avoiding the largest tax increase in history and addressing the risk of economic slowdown. Unlike the majority budget, it assumes an extension of AMT relief, which is all but certain. Finally, it would fix PAYGO so that it applies only to spending increases, focusing, as is appropriate, on the size of government and reducing the risk of entitlement expansions matched with tax hikes.⁴

The Republican budget also takes several important steps to rein in out-of-control spending. First, it

would implement a five-year freeze in non-defense discretionary spending, limiting Congress's ability to boost funds for pet projects and ineffective programs. This freeze would also encourage Congress to prioritize its spending, making the kinds of tradeoffs that families make when they decide how to spend their money. Congress has fallen short in this; non-defense discretionary spending grew 40 percent (21 percent after inflation) from 2001 through 2006. The Republican budget, however, stresses the need for tradeoffs by accommodating increases for important priorities, such as veterans' health care.

No less important, the Republican budget does not shortchange defense. Rather, it meets the President's request for defense funding in FY 2008 and 2009.

The other crucial step in the Republican budget is that it would start down the road to reforming the big entitlement programs. These programs grow on autopilot from year to year and are poised to swamp the budget with the retirement of the baby boomers, pushing the size of government to unprecedented heights and threatening major tax increases. Instead of putting off dealing with entitlements—and thus making it more difficult and expensive to fix them later—the Republican proposal would enact several reforms that would save a projected \$279 billion over 5 years. This is an important step toward addressing the nation's long-term spending crisis.

Finally, the Republican budget includes several measures to prevent Congress from getting around its budget commitments and using gimmicks to boost spending. First, the Republican budget includes funds for emergency appropriations. Emergency funding bills have become so routine, and so loaded with non-emergency spending, that it

1. Tracy Foertsch and Ralph A. Rector, Ph.D., "The 2001 and 2003 Bush Tax Cuts: Economic Effects of Permanent Extension," Heritage Foundation *WebMemo* No. 1361, February 15, 2007, at www.heritage.org/Research/Taxes/wm1361.cfm, and James Sherk, "Jobs, Taxes, and the Goldilocks Economy," Heritage Foundation *WebMemo* No. 1336, February 1, 2007, at www.heritage.org/Research/Economy/wm1336.cfm.
2. See William W. Beach, "Increasing IRS Tax Collection Powers Threatens More IRS Abuse: The New Congress Moves to Close the 'Tax Gap,'" Heritage Foundation *WebMemo* No. 1373, February 27, 2007, at www.heritage.org/Research/Taxes/wm1373.cfm.
3. See Richard W. Rahn, "Tax Traps," *The Washington Times*, March 28, 2007, at www.washingtontimes.com/commentary/20070327-094851-8554r.htm.
4. See Brian M. Riedl, "PAYGO: A Recipe for Steep Tax Increases and Runaway Spending," Heritage Foundation *WebMemo* No. 685, March 14, 2005, at www.heritage.org/Research/Budget/wm685.cfm.

is disingenuous to exclude them from any budget proposal. Second, it includes a presidential line-item veto measure that could have some success in trimming pork from the budget. Finally, as mentioned, it includes a PAYGO provision that focuses on the real problem—growth in spending.

Conclusion. Unlike the House Democrats' budget resolution, the Republican budget substitute embodies a vision of fiscal restraint and economic

growth. It begins to address the difficult problem of unrestrained growth in entitlement spending and maintains the tax cuts that promote continued economic growth. Members of Congress should give the measures of the Republican budget serious consideration and use the proposal as a basis for responsibly getting the budget under control.

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