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President's Budget Would Restrain Entitlements and Domestic Discretionary Spending

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President Bush's budget request for fiscal year (FY) 2009 restrains domestic discretionary spending, halves earmarks, extends the tax cuts, and reforms Medicare to contain its surging costs. Unfortunately, Congress is not likely to address major entitlements or tax cuts in an election year. Instead, Congress will most likely shorten the congressional calendar; address the appropriations bills; and possibly reauthorize the State Children's Health Insurance Program (SCHIP), farm subsidies, and No Child Left Behind. Therefore, the most legislatively relevant aspects of the President's budget may be where he draws the veto lines on must-pass legislation.

Yet, it is vital that Members of Congress heed the President's call to address the long-term costs of Social Security, Medicare, and Medicaid. The budget deficit is projected to hit \$390 billion in FY 2012 and \$788 billion in FY 2018, but even those totals are a small fraction of the long-term costs of ignoring entitlements.¹ In the absence of reform, lawmakers would eventually have to choose between permanently raising taxes by a staggering 10.3 percent of GDP (the equivalent to \$11,000 per household today) or eliminating every other federal program in order to fund Social Security, Medicare, and Medicaid.² The President's budget focuses mostly on Medicare reform, which faces the most serious funding challenges. Responsible lawmakers should seriously examine the President's proposals to bring long-term sustainability to entitlement spending.

General Observations. The following is a list of observations and recommendations concerning the President's proposals and the larger budget picture:

1. **The 2012 budget deficit is not the issue.** President Bush has pledged to put federal finances on the path toward a balanced budget by 2012. However, whether the federal government runs a deficit of \$100 billion, \$50 billion, or zero dollars in 2012 is not particularly important. Even if Washington enacts the necessary short-term budgetary tweaks, spending on Social Security, Medicare, and Medicaid would quickly push the budget back into a deficit shortly thereafter. If lawmakers put entitlement spending on a sustainable path, the short-term budget picture will take care of itself.
2. **The President's budget includes responsible restraints on domestic discretionary spending.** The President's budget request increases total discretionary spending by a generous 4.9 percent. It balances larger increases for defense, homeland security, international programs, and veterans' programs by limiting the growth of domestic discretionary spending to just under 1 percent. Domestic discretionary spending—

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which has leapt by 48 percent (22 percent after inflation) from 2001 through 2008—can certainly afford this near-freeze for one year.³ Congress should offset any additional, high-priority spending with cuts to lower-priority programs.

In particular, the 46 House “Blue Dog” Democrats, who describe themselves as deficit hawks and fiscal conservatives, should applaud the President’s call to limit domestic discretionary spending. The Blue Dogs have emphasized Pay-As-You-Go (PAYGO) rules that limit budget deficit increases caused by tax cuts and entitlement spending hikes. They should not ignore the discretionary spending hikes that also add to the budget deficit.

3. **The President excludes the war against terrorism and the patch for the Alternative Minimum Tax (AMT).** The President’s budget includes only a partial estimate of funding for the war on terrorism in FY 2009, and no estimate for years thereafter. While its costs are difficult to project, the President should have included at least a ballpark estimate for the sake of long-term budgetary planning (allowing that evolving circumstances may alter the estimate over time). Of course, Congress should fully fund the remaining FY 2008 funding request for the war against terrorism and begin examining the estimated costs for FY 2009. While there are legitimately differing views on American foreign policy, all lawmakers should agree that defunding the troops and putting them in harm’s way would be a dangerous and irresponsible way to express those views.

Additionally, the President’s budget excludes any revenue effects from extending the patch beyond 2008. During the 2007 AMT debate,

President Bush argued successfully that Congress should not raise other taxes as the price for maintaining current AMT policy. Consistent with last year’s view, his budget request proposes to extend the patch in 2008 without revenue offsets. But after 2008, he proposes a revenue-neutral AMT patch; in effect, he proposes that Congress raise revenues elsewhere to offset the revenues from the patch. In other words, President Bush follows his own advice for 2008 but recommends that Congress raise taxes after he leaves office. There is no way to square that circle logically. This approach to AMT is basically a gimmick to make future budget deficits appear smaller.

4. **The budget extends the tax cuts.** The President proposes making permanent the successful 2001 and 2003 tax cuts. By increasing incentives to work, save, and invest, reduced tax rates played a key role in the expanded business investment, job growth, and the stock market gains of recent years. Furthermore, tax revenues currently stand at 18.8 percent of GDP—well above the historical average—and are projected by the CBO to rise to a record 22.8 percent of GDP by 2050, even if the tax cuts are made permanent.⁴ Letting the tax cuts expire—or worse, repealing them—would hit millions of Americans with a major tax increase. Raising tax rates would harm families and businesses, and the resulting economic slowdown would minimize any revenue increase. Furthermore, the uncertainty of whether tax rates will soon increase is undoubtedly preventing some businesses and investors from undertaking new multi-year investments—and, consequently, contributing to the current economic slowdown.

1. Brian Riedl, “Notes on the New 10-Year Budget Baseline,” Heritage Foundation *WebMemo* No.1795, February 4, 2008, at www.heritage.org/Research/Budget/wm1795.cfm.
2. Brian Riedl, “Federal Spending by the Numbers,” Heritage Foundation *WebMemo* No. 1390, March 8, 2007, at www.heritage.org/Research/Budget/wm1390.cfm.
3. Calculated by The Heritage Foundation using Office of Management and Budget, “Budget of the United States Government Fiscal Year 2009: Historical Tables,” Table 8.7, at www.whitehouse.gov/omb/budget/fy2009/hist.html.
4. Congressional Budget Office “The Long-Term Budget Outlook,” December 2007, pp. 44–46, at www.cbo.gov/ftpdocs/88xx/doc8877/12-13-LTBO.pdf, plus accompanying data from the CBO. The 22.8 percent figure does not assume that lawmakers will adjust the AMT threshold. Assuming the Bush tax cuts are made permanent and the AMT is adjusted annually, the CBO’s 2050 revenue projections are 19.4 percent of GDP, which is still well above the historical average.

The federal budget's problems do not stem from Americans being undertaxed, but rather from Washington spending too much. In order to prevent one of the largest tax increases in American history, Congress should follow the President's lead by extending the current tax policies.⁵

5. **The President should enforce his earmark pledge.** Last year, Congress ignored its own reform pledges by including 11,738 earmarks in the appropriations bills—the second-highest total ever—at a cost of \$21 billion.⁶ President Bush has pledged to veto any appropriations bill that does not cut in half both the number and cost of earmarks.

Earmarking is a corrupting process. Earmarks give individual lawmakers a pot of tax dollars to distribute to organizations of their choosing. Consequently, politics and campaign contributions now play a larger role in the distribution of government grants at the expense of statutory formulas and priorities and competitive application processes. Lobbyists promote their matchmaker role, effectively auctioning government grants to the highest bidder. The FBI has launched several corruption investigations to determine whether lawmakers based earmark decisions on personal profit.

Since 1996, the number of annual earmarks has leapt from 958 to 11,738.⁷ Taxpayers should welcome President Bush's veto threats to rein in earmarks.

6. **The President's budget does not jeopardize social spending.** In what has become an annual ritual, the release of the President's budget has been followed by interest groups decrying alleged cuts to social and education spending. The facts do not match the rhetoric.

By any reasonable standard, President Bush is the biggest antipoverty, health, and education spender in American history. Under President Bush, federal antipoverty spending has topped 3 percent of GDP for the first time ever. Federal education spending has leapt 9.7 percent annually—compared to 2 percent annually under President Clinton. Health research and regulation has grown by 9.5 percent annually.⁸

Under the FY 2009 budget request, discretionary education funding would increase an additional 3.5 percent, health research spending would be approximately frozen, and antipoverty spending would increase 4.2 percent.⁹ Given how much these programs have already expanded in recent years, the President's proposal is more than sufficient.

7. **The budget addresses Medicare overspending.** Medicare spending has leapt by 51 percent over the past four years and is projected to continue growing at unsustainable rates for several decades. The President's proposal would lower Medicare's growth rate to 5 percent annually and shave one-third off the program's staggering 75-year unfunded liability of \$34 trillion. Failing to take up the President's Medicare challenge would mean kicking the can down the road, when the necessary reforms will become even more expensive. Moreover, Medicare's perilous spending trends have triggered a provision from the 2003 Medicare Modernization Act requiring President Bush to offer reform legislation to rein in the program. There is no better time for Congress and the White House to come together on this vital issue.
8. **The budget addresses key reauthorizations.** This year, Congress may once again try to reau-

5. See Brian Riedl, "Ten Myths About the Bush Tax Cuts," Heritage Foundation *Background* No. 2001, January 29, 2007, at www.heritage.org/Research/Taxes/bg2001.cfm.

6. The Office of Management and Budget is tracking earmarks at <http://earmarks.omb.gov/by-tracking/summary.html>.

7. Earmark data from 1996 is calculated by Citizens Against Government Waste, at www.cagw.org.

8. Office of Management and Budget, "Budget of the United States Government: 2009 Historical Tables," Table 3.2, at www.whitehouse.gov/omb/budget/fy2009/hist.html. Antipoverty spending is calculated as budget functions 604 (housing aid), 605 (food aid), 609 (other income support), as well as Medicaid and SCHIP for health care.

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thorize SCHIP. President Bush proposed increasing the program's funding by \$19 billion over five years, which is more responsible than the \$35 billion increase passed by Congress, much of which would cover non-poor families and would displace private insurance coverage.¹⁰

The President's budget also does not include the large increases in farm subsidies and related taxes passed by Congress last year. Driven by the ethanol boom, farm incomes and net worths are shattering records. Furthermore, more than half of all farm subsidies go to large commercial farms, which report an average income of \$200,000 and a net worth of nearly \$2 million.¹¹ There is no reason to raise taxes and enlarge the budget deficit in order to expand farm subsidies even more.

Finally, the No Child Left Behind Act may be reauthorized this year. The President's budget does not include a comprehensive reauthoriza-

tion proposal but *does* include another hike in discretionary education spending.

Conclusion. Given the Democratic control of Congress, and the short election-year calendar, it is easy to dismiss the legislative relevance of the President's budget proposals. However, the President can still use his veto authority to restrain domestic discretionary spending, rein in earmarks, and prevent reauthorizations from busting the budget. His budget draws a line in the sand on those costs and tax increases. In the long-run, the most important part of the budget is the President's challenge to Congress to finally address the unsustainable long-term costs of entitlements. The longer lawmakers wait to enact the necessary reforms, the more painful those reforms will be.

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10. For more on SCHIP, see The Heritage Foundation's SCHIP briefing room, at www.heritage.org/research/healthcare/schip.

11. For more on farm subsidies, see Brian M. Riedl, "How Farm Subsidies Harm Taxpayers, Consumers, and Farmers, Too," Heritage Foundation *Background* No. 2043, June 20, 2007, at www.heritage.org/Research/Agriculture/bg2043.cfm.