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The Futility of the Gang of Six Budget Plan

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The budget showdown in Congress is being described as a "crisis," "looming catastrophe," "approaching disaster" -- pick your hyperbole. But anything that happens on August 2 will pale in comparison to the real fiscal disaster that is several years down the road. Policymakers need to take the long view in pursuing a fix.

The decade-long expansion of government spending during the 2000s created a future trajectory of government spending that is unsustainable and in dire need of attention. A "balanced approach" to the debt problem involving both revenue increases and spending reductions might sound terrific on CNN, but it yields more government spending on net than the historical norm. A better approach would be to determine the proper share of government spending in terms national economic output, specify that share ahead of time, and enforce a balanced budget funding process -- as House members have just voted for.

The Congressional Budget Office projects that government spending is scheduled to increase to 24 percent of GDP by 2020. It has averaged about 20 percent between 1960 and 2005 -- not counting recent years when massive economic stimuli distorted the government share. That means exhorting policymakers to adopt a "balanced" approach -- such as the "Gang of Six plan" now drawing plaudits from editorial pages and the White House -- is really promoting a new and higher federal spending norm as a percentage of GDP.

There are other questionable features of the rhetoric used to sell the Gang of Six plan. It mentions allowing the Bush tax cuts to expire for those making more than $250,000 annually, and overhauling the tax code to "maintain or improve" progressivity of the tax code. The crowning piece of rhetoric: "This is the sort of pro-growth tax reform that could help energize the economy."

Why is this approach fundamentally wrong? First, increasing tax rates on entrepreneurs and job creators will achieve exactly the opposite result -- galvanizing sloth and energizing capital flight. And "improving progressivity" (a bit of ideological wordplay -- why not just say "*increasing* progressivity?") will reinforce those outcomes because making the tax code more progressive will place higher hurdles before low-income individuals to increase their work-hours and incomes.

The Gang of Six proposal also shifts government-wide inflation indexing to use the chained Consumer Price Index. In particular, it would cause income tax brackets to rise more slowly -- leading to increases in marginal tax rates on all taxpayers. It would also reduce Social Security benefits of current beneficiaries on an inflation-adjusted basis. But it means that not all changes to Social Security are independent of budget reform, as the proposal claims.

The proposal would repeal the CLASS Act -- a classic Washington two-step. The CLASS Act is a proposal under the new health care reform law to extend voluntary long-term care coverage to all workers, financed out of a payroll tax. This program is widely acknowledged to be so badly designed that it is fundamentally unworkable and could never be established; most healthy workers won't sign on, which would increase the program's cost to others and make it financially unsustainable.

It's a classic example of achieving spurious budget savings by eliminating programs that don't, and never could, exist -- thereby placing a larger weight on revenue increases in the reform as a whole.

Finally, the plan only accomplishes $500 billion of savings scheduled (read: back-loaded) over the next 10 years. The rest of it is just procedural provisions to "seek future budget savings." It achieves few real and significant budget savings today.

Elsewhere, I've opined that a budget deal yielding just $4 trillion in budget savings is unlikely to improve the U.S. fiscal condition by 2020. Given how little the Gang of Six plan achieves, any debt limit increase that it facilitates is likely to persist for a long time. On balance, it's likely to lock us into a worsening fiscal and economic condition during coming decades.

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