The Corner

Important Institutional-Reform Ideas

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While slowing the growth of (or, ideally, cutting) spending is key to changing the financial path we are on, Congress also needs to implement meaningful budget-process reforms that cannot be undone when the spotlight shifts to other issues. Fortunately, many of the budget rules that could help — such as spending caps and a balanced-budget amendment — are close at hand.

See for instance the Maximizing America's Prosperity, or "MAP" Act recently introduced by Rep. Kevin Brady, the vice chairman of the Joint Economic Committee. The act is essentially a package of budget-process reforms intended to keep Congress's hand out of the cookie jar. The MAP Act is worth highlighting since it is almost certainly the most well thought out of the various spending-cap proposals.

First, the MAP spending caps, which would be enforced by automatic spending cuts (sequestration), use "potential GDP" rather than historical or projected GDP to determine the level of spending in any given year. Dan Mitchell at the Cato Institute testified before Congress yesterday on why this is the way to go:

> How to define GDP. The obvious answer is to use GDP, but which GDP? If you select estimates of future GDP, you create an opening for gimmickry since lawmakers might pressure CBO or OMB for an exaggerated estimate to facilitate more spending. Another option would be to use an average of the past couple of years of GDP. That would give a firm number, but it might create complications if the economy is coming out of boom or recovering from a downturn. This is why "potential GDP" might be the best option. Potential GDP is a technical concept based on what GDP would be at full employment without price inflation. It is a widely used number that CBO calculates for 10 fiscal years into the future. Why use "potential GDP"? A spending cap based on traditional GDP allows spending to rise rapidly under booms only to force large spending cuts during recessions. That tends to be politically unsustainable, as we saw under Gramm-Rudman. Moreover, state spending caps tied to some measure of state GDP have largely failed because of this reason. Potential GDP eliminates this problem by smoothing out the fluctuations of the business cycle and thus curbing excessive spending growth during booms and not attempting to force politically difficult spending restraint during recessions.

Second, the MAP caps apply to "primary spending" (meaning all non-interest spending). Mitchell again explains why it matters:

> America's real fiscal problem is entitlements. So-called mandatory spending already is the lion's share of

> the federal budget and entitlement programs will consumer ever-larger shares of our economic output as the baby boom generation retires and outlays skyrocket for Social Security, Medicare, and Medicaid. A cap that only applies to discretionary spending would be akin to visiting a doctor after an auto accident and getting treated for a sprained wrist while ignoring a ruptured spleen. So does that mean a spending cap should apply to all spending? That certainly would be a better option than a discretionary cap, but that means net interest – payments to service the publicly-held debt – would be included. Notwithstanding recent threats by the Treasury Secretary to deliberately and unnecessarily default on those obligations, interest on the debt is the one part of the budget that is truly uncontrollable. It is more reasonable, therefore, to target "primary spending," which is everything other than net interest. One bid advantage of this approach is that a cap on all spending creates a "tax trap" that may prevent the extension of current tax policy or future tax cuts.

Interestingly, Senator Corker has attracted several Democratic sponsors to his version of spending-cap legislation, so it seems that this is one idea that could actually make it through a Reid-controlled Senate.

Another great feature of the MAP Act is a permanent continuing resolution:

> A permanent CR would fund government at 90% of the appropriation for the previous fiscal year if Congress fails to pass necessary spending bills on time. Thus, "big spenders" could no longer threaten a government shutdown to push for more spending.

The whole thing is here.

P.S. Mitchell also has a troubling post about whether Speaker Boehner's Budget Control Act inadvertently creates a tax hike trap

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