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THE PRISONER OF OBRA

Operating on the conviction that every cloud must have a silver lining, we have looked for a redeeming virtue in 1990's Omnibus Budget Reconciliation Act -- OBRA90. The going was hard. We did, however, find some salutary elements in the Act that warrant mention.

For one thing, OBRA90 shifts the emphasis in federal budget policy from deficit reduction to curbing spending growth. Deficit targets for the current and succeeding four fiscal years remain in the law, but are much less of a driving force in budget decision making. Standing alone, this downgrading of Gramm-Rudman-Hollings deficit targets might be alarming; with the caps the Act imposes on the principal, broad spending categories in fiscal years 1991-1993 and on total spending in 1994-1995, however, policy makers appear to have recognized that it is government spending, not the budget deficit, that is the fiscal mischief maker.

Another encouraging feature of OBRA90 is that the imposition of caps on government spending downplays spending "baselines" as a factor in decisions about spending for any program. Baseline budgeting keys spending decisions to the previous year's spending and the inflation rate. If last year's spending on a program, when assessed against meaningful criteria, was excessive, baseline budgeting almost certainly will result in even greater excess in this year's spending. Baseline projections of program outlays are useful as indications of how large government programs will become if not changed by legislation. They are not themselves, however, appropriate guides for policy decisions about how much to spend on a program in any particular period. OBRA90's spending caps may indeed have been determined primarily by reference to some baseline or other, but at least for the present these caps appear to have made baselines far less relevant to spending decisions.

If -- and it's a big "if" -- the spending caps remain intact, they will prevent legislated spending excesses that aren't curtailed by sequester in the year they occur from boosting spending in the succeeding fiscal year or years. Any such excess, presumably, will reduce spending caps in the following fiscal year. Gaming the system by delaying budget decision making to the last possible moment will no longer be an effective device for evading the spending ceilings specified in Congressional budget resolutions.

Spending curbs, moreover, are no longer to be merely a matter of language in budget resolutions. The spending caps specified in OBRA90 presumably apply to new budget authority and appropriations, as well. It will no longer be possible for Congress to pretend fiscal prudence merely by resolving not to spend; it must also suit its appropriations to its resolve.

Finally, OBRA90 appears to recognize that the major element of budgetary excess is the seemingly uncheckable expansion of so-called entitlement spending. Under OBRA90's pay-as-you-go, or PAYGO, provisions, new entitlement legislation that is estimated to increase the budget deficit requires the President to issue a sequester order for across-the-board cuts in nonexempt entitlement outlays. Sequester, requiring the same across-the-board cuts, would also be ordered should any tax legislation be estimated to increase the deficit above target. PAYGO is far from an unqualified blessing, but at least it suggests the possibility that Congress recognizes the fiscal and economic peril in unchecked increases in these entitlement outlays.

But we come to bury OBRA 90, not to praise it. The Act suffers three signally important deficiencies. For one thing, at a time when the expansionary steam clearly had gone out of the economy and when the loosening of tax restraints on the economy's growth was sorely needed, the Congress and the Administration combined forces to saddle the American people with the second-largest tax increase in the nation's history. For another, instead of urgently needed, straightforward, meaningful reform of the budget-making process, the Congress and the Administration fashioned an extraordinarily complex set of rules to constrain tax and spending decisions in fiscal years 1991-1995.

Thirdly, OBRA90 excludes Social Security trust fund receipts and outlays from budget reckoning. Doing so makes an artificial and false distinction between payroll taxes and all other taxes in the federal revenue system and between social security retirement benefits and all other federal transfer payments. It gives credence to the mistaken notion that the Social Security trust fund is a real trust fund with real income-producing assets. In short, it perpetuates myths about social security that have always seriously hampered good public policy concerning provision for retirement income.

OBRA also ties the hands of tax policy makers. PAYGO holds tax policy hostage to politically-favored nonexempt

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entitlement programs. However compelling may be the case for revenue-reducing tax legislation, such tax changes will be deterred by the requirement for cutting entitlement programs. To avoid this barrier, tax changes that are estimated to be revenue losers must be accompanied by tax changes that are estimated to raise revenues in equal amounts. In other words, OBRA90 explicitly holds that maintaining the revenue flow is more consequential than addressing substantive tax policy concerns. Moreover, it gives decision-making priority to revenue estimates over the compelling concerns about how the tax structure affects the economy's performance. By the same token, it gives more clout in policy making to the revenue estimating staffs in the Treasury and the Congress than to elected public policy makers.

The current recession seems to be reawakening concern about the effects of public policies on the health of the economy. Although we don't endorse the use of tax policy, let alone spending policy, as a counter-cyclical fiscal tool, we recognize that recessions may heighten policy makers' awareness of the adverse effects of bad tax policy on economic efficiency and growth. A recession, therefore, is an appropriate occasion for thinking about and developing an agenda of constructive tax policy changes that would enhance the economy's potential for growth and competitiveness over the long term.

Some public policy makers appear now to be willing to get down to basics in tax policy. Various members of Congress and Administration spokesmen are making quiet little noises about pro-growth tax agendas. Although some of these policy makers appear to be laboring under the mistaken notion that some sort of fiscal magic and/or the Federal Reserve's going on a money-creating binge can bring the recession promptly to a halt, others recognize that the proper concern of tax, budget, and monetary policy is the efficient growth of the economy over the long haul. Whatever the focus of their concern, however, policy makers must deal with the PAYGO constraint that OBRA90 imposes on any constructive tax initiatives they may wish to undertake.

Particularly distressing is the inhibiting effect of PAYGO on any solidly constructive program of tax reforms aimed at releasing the economic energies of the economy's private sector. That program should aim at reducing the existing tax bias against saving and capital formation, at moderating the tax-imposed increase in the cost of labor services, at diluting the extra tax burden that American multinational businesses bear compared with their foreign competitors, at easing the tax constraints on efficient operation of our financial markets, at invigorating entrepreneurship and innovation, and so on. Any such program is very likely to entail significant revenue losses, as estimated by the Treasury Department and the Joint Committee on Taxation, using static revenue estimating techniques. Requiring that these losses be made up by equal revenue- gaining tax changes or by equal reductions in entitlement program outlays casts up a major roadblock to their being advanced as serious legislative initiatives.

The economic costs of recessions cannot be shrugged off, but the greater those costs, the greater is the urgency in finding a silver lining to the recession cloud. In this instance, the silver lining is that if CBO finds that the recession has lasted or will last two or more quarters, PAYGO may be suspended by a Congressional resolution that becomes law upon the President's signature. Although CBO and OMB concurred that the economy is now experiencing the second quarter of a recession, the Senate voted to reject the suspension of the OBRA90 limits, preferring to retain Congress' self-imposed limits on its ability to discharge its budget-making responsibilities. If the recession continues, perhaps the Senate and the House will come around, however reluctantly to recognition that their first responsibility is to the economic well being of the citizenry, not to that of the federal government.

Good public policy making should not be held hostage until the emergence of bad economic conditions. Constructive tax legislation almost certainly must be revenue-losing legislation. The country sorely needs that legislation; it must be freed from OBRA's prison. Legislation to repeal PAYGO should be a high-priority initiative offered by the President this session.

Even better policy would be to enact Congressman Chris Cox's proposed budget process reforms, H.R. 298, cosponsored by more than 100 House members. Congressman Cox's proposal offers real budget process reform, without the elaborate and mystifying control measures on which OBRA90 relies. Moreover, its proposed changes in the budget-making process are not focused solely on the current and four following fiscal years; they are reforms that should serve very well indeed for many years to come. OBRA90, if effective, sets specific spending limits for specific outlay categories and virtually precludes any shift in fiscal policy emphasis and focus. In contrast, the Cox proposal in no wise constrains the Congress in its choice of priorities regarding the amount and the allocation of total spending among 19 broad budget categories. Nor does the proposal impair Congress's freedom to make and implement basic tax policy decisions.

Congressman Cox has the right formula for initiating the sorely needed constructive reforms of the Congressional budget process. The President would do well to make those reforms a top priority for his domestic agenda.

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President
