

# Slate

FIXING IT

## Fiscal Policy

Fully account for the budget, stick to the budget, and work with the other party.

By Jason Furman

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The fiscal damage to the United States over the last seven years is calculable. It is precisely \$3,889,136,064,463, according to the Bush administration's Office of Management and Budget, which totaled up the budgetary cost to date of all the tax cuts and spending increases enacted over the past seven years. Of that nearly \$4 trillion total, the administration estimates that 46 percent is tax cuts, 31 percent is defense and homeland-security spending, and 23 percent is everything else, including the prescription-drug benefit.

Even if the next president repealed the tax cuts, canceled the prescription-drug benefit, and returned defense spending to prewar levels, the added debt from eight years of these policies would not vanish—and we would be left paying roughly \$100 billion annually just in added interest. Fully fixing it could take years or even decades. Here is how the next administration could at least start us down that path:

*Step 1: Fully account for all costs in the budget.* While it will take a long time to dig ourselves out of the current budgetary mess, quantifying the exact size of the mess should be the first order of budgetary business in the next administration. Budget documents have become increasingly detached from reality. Year after year, we are "surprised" by the large budgetary costs. In February 2006, for example, the president submitted [a budget](#) with \$485 billion of defense funding for 2008. Just two years later, 2008 has arrived and the [president's budget](#) is now requesting \$693 billion for the same year. That whopping \$208 billion underestimate of defense spending in 2008 exceeds total spending on the wars in Iraq and Afghanistan this year. That same February 2006 budget called for precisely \$0 in relief from the Alternative Minimum Tax in 2008, compared with the \$60 billion

actually being spent on such relief.

The next administration could unilaterally end this practice by including all future costs in their budget. Ideally, the budget would specify how the costs would be paid for as well. But if that is too much to hope for, I would still rather see the budget admit that AMT relief will cost money than pretend that it will be paid for in some unspecified manner.

Such a step would be in the new administration's interest because it would increase the projected deficit, a problem they could fairly claim they inherited from their predecessors. And starting from this point would make it easier for them to claim any progress in fixing the problems.

*Step 2: Stick to these costs, with a veto pen if necessary.* The next president can draw up a budget on his or her own. But any actual spending or tax decisions need to be passed by Congress. The president has only a limited ability to pressure Congress into raising taxes or cutting spending in order to reduce the deficit. But he or she can draw a firm line and promise to veto any legislation that raises the deficit. And if Congress continues to largely abide by this principle, [as it has](#) since Democrats took control in 2007, then the process will be that much easier.

This would not preclude putting universal health care first on the agenda, as Ezra Klein [wisely suggests](#), but it does require that one of the principles underlying this priority be that it is fully paid for without increasing the deficit.

Per Step 1, it would obviously be better for the next administration to set realistic goals and stick to them rather than make heroic claims about deficit reduction premised on implausible and unlikely-to-be-enforced promises about unrealistically low levels of spending in areas like Iraq and the AMT.

*Step 3: Be ready to work together with the other party to reduce the deficit.* Any one party or branch of government has it within its power to stop the deficit from worsening. But it is hard to imagine a feasible or desirable process to actually reduce the deficit that does not involve both parties and both branches of government. In the past, a number of different bipartisan processes have worked—a commission for Social Security in 1983, a summit at Andrews Air Force Base in 1990, and informal negotiations in 1997. But no process will work without a substantial amount of bipartisan buy-in and a few ideas to start the discussion. Here are some of mine:

- *Health care, health care, health care.* The long-run deficit is almost entirely the result of [the rapid growth of health spending](#) in both public programs like Medicare and private health insurance. Ultimately, a lasting solution will implement systemwide reforms that change the incentives facing both providers and patients. But there are some simpler steps we could take right now in Medicare. One is to end the practice of paying private managed-care plans more than we pay for people in the government's insurance plan, a step [endorsed](#) by Congress' Medicare Payment Advisory Commission. Another is to use a combination of better clinical guidelines, carrots, and sticks to reduce [Medicare spending in high-spending areas](#).
- *Taxes.* Fixing our fiscal situation will require higher revenues than we have seen in recent years. One easy step would be allowing the Bush tax cuts for high-income households to lapse in 2010. But this will not be enough. For other steps, policymakers should consider the more economically efficient tax increases [supported by](#) economists like former Bush Council of Economic Advisers Chairman N. Gregory Mankiw, such as a carbon tax (or cap-and-trade system with auctioned permits), increased sin taxes on items like cigarettes, and a broader tax base by, for example, [reforming the deductibility of the mortgage interest](#). Finally, we should curb the rapid proliferation of corporate loopholes and corporate shelters—for example, by reducing the ability of companies to report different amounts of profits to their shareholders and the Internal Revenue Service and by no longer allowing American multinationals to deduct the cost of overseas investments without fully paying taxes on the profits they generate.
- *Social Security.* Social Security is a smaller source of the fiscal challenge than health care or tax cuts. But it is also a large and important program with [well-understood reform options](#). Two of my favorite options are raising that amount of Social Security payroll that is taxable and indexing benefits and/or taxes to the [changing ratio of beneficiaries to workers](#).
- *Changing the official measure of inflation.* Social Security, the tax system, and other aspects of the economy are all indexed to a measure of inflation that is widely acknowledged to overstate the increase in the cost of living. If the government switched to [a newer, more accurate measure](#), it would reduce the growth of Social Security benefits for retirees and raise tax collections—both in a manner consistent with the intentions of policymakers. The budgetary savings from such a policy would accumulate over time.
- *Defense.* Defense spending, excluding direct spending on the wars in

Afghanistan and Iraq, has increased by an inflation-adjusted \$129 billion since 2000. I am no defense expert—that was Monday's topic—but I suspect that while substantial new sums are needed to meet our new challenges, much of this could be funded by scaling back on weapons systems originally designed to fight pitched battles on the plains of Europe. [See Phillip Carter and Fred Kaplan](#) for more.

- *Everything else.* Compared with health care, taxes, Social Security, and defense, everything else, including farm subsidies, earmarks, student-loan subsidies, and a \$2 million scientific program to research grizzly bears, is relatively small but in some cases worth addressing—if only to create more confidence in the budget process.

*Step 4: Don't forget what really counts.* The stabilization of the long-run deficit is inevitable—policymakers have no choice but to abide by the iron laws of arithmetic. But the most important budgetary issues are the choices policymakers make about how much to invest in research, how much to spend ensuring that everyone has health insurance, and what is done to make our nation more secure. Making these choices will be easier if we start to fix our bigger fiscal problems.

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