

THE NEED FOR CONSTITUTIONAL BUDGET REFORM

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House Committee on the Judiciary
The Need for the Balanced Budget Amendment

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Chairman Goodlatte, Ranking Member Conyers, and members of the committee:

Thank you for inviting me here to discuss the need for a constitutional amendment to help rescue the federal government's finances.

I am an associate professor of political science and business administration at the University of Rochester, where I hold the Ani and Mark Gabrellian Professorship. In addition, I am a senior affiliated scholar with the Mercatus Center at George Mason University. I have studied fiscal policy throughout my career and am the author of numerous works in this area, including *Rules and Restraint: Government Spending and the Design of Institutions*, published by the University of Chicago Press.¹

My three-part message today is this:

- First, the United States faces fiscal pressures that threaten our economy, and it would be a serious mistake to let relatively low deficits today lull us into a sense of complacency about the future.
- Second, the short-run focus in politics, combined with Congress's institutional prerogatives, make it difficult for legislators to implement durable reforms to address these fiscal threats.
- Third, a constitutional amendment, if well designed, can provide the foundation for credible and sustainable fiscal policy.

¹ This testimony is based in part on arguments developed more fully in David M. Primo, "Making Budget Rules Work, 2014 Edition" (Mercatus Research, Mercatus Center at George Mason University, 2014). This testimony also draws in part from previous testimony: David M. Primo, "Should the Constitution Be Amended to Address the Federal Deficit?" (Testimony before the House Committee on the Judiciary, Subcommittee on the Constitution, Mercatus Center at George Mason University, Arlington, VA, May 13, 2011); David M. Primo, "Constitutional Solutions to Our Escalating National Debt: Examining Balanced Budget Amendments" (Testimony before the House Committee on the Judiciary, Mercatus Center at George Mason University, Arlington, VA, July 24, 2014); David M. Primo, "First Principles of Congressional Budgeting" (Testimony before the House Committee on the Budget, Mercatus Center at George Mason University, Arlington, VA, July 28, 2015).

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TODAY'S DEFICITS ARE THE CALM BEFORE THE DEBT STORM

When I first testified on this subject in 2011, the nation's fiscal problems were receiving significant attention from Congress, the White House, debt-rating agencies, and the American people.² Since then, the federal budget deficit has declined to about 3 percent of GDP (the standard European Union countries are held to) in fiscal year 2016, down from about 10 percent of GDP in 2009.³ Perhaps because of this decline, in late 2015, one Washington observer commented, "anxiety about the federal deficit . . . seems to be fading everywhere—in Congress, among voters, and on the 2016 campaign trail."⁴ This statement seems as true today as it was then.

Today's deficits may seem manageable, but they are expected to rise in the coming decade to 5 percent of GDP, according to a recent CBO estimate.⁵ Moreover, these numbers must be understood against the backdrop of recent deficit spending that has caused the national debt held by the public to more than double in the past decade, increasing from 35 percent of GDP in 2007 to 77 percent of GDP in 2016.⁶

As figure 1 shows, the long-term trajectory for the federal debt is ominous. After a lull in the next few years, CBO estimates that the debt is projected to hit 150 percent of GDP by 2047, and the Treasury Department estimates that the national debt will reach an unimaginable 250 percent of the nation's economic output by 2091.⁷

The current path is unsustainable and threatens the well-being of Americans, especially those in future generations who will bear the brunt of the economic pain caused by our inaction today.⁸ As the Treasury Department warns, "Delaying fiscal adjustments for too long raises the risk that growing federal debt would increase interest rates, which would, in turn, reduce investment and ultimately economic growth." The CBO plainly states, "Large and growing federal debt over the coming decades would hurt the economy and constrain future budget policy."⁹ While economists disagree about how much debt is too much debt for the health of the economy,¹⁰ researchers at the International Monetary Fund have found that the negative effects of debt on economic growth are particularly pernicious when debt is *increasing* as a share of GDP (i.e., is growing faster than the economy)—exactly the situation in which this country will find itself in the coming decades, as figure 1 shows.¹¹

² In my 2011 written testimony, I argued, "The recent bipartisan attention to the challenges we face is heartening. The dangers of our debt and deficit levels are no longer the province of commissions whose reports gather dust. Instead, we have elected officials taking a stand and proposing bold changes to the status quo. . . . Voters are also paying attention. In a poll conducted by Pew Research Center and *The Washington Post* in April 2011, an astonishing 95% of respondents agreed that the federal budget deficit was a problem, and 81% agreed that action was needed now." Primo, "Should the Constitution Be Amended." Soon after my testimony, in August 2011, Standard & Poor's downgraded US federal debt in part because of the inability of the federal government to provide a "credible solution to the rising US government debt burden." See Standard & Poor's, "Research Update: United States of America 'AAA/A-1+' Ratings Placed on CreditWatch Negative on Rising Risk of Policy Stalemate" (RatingsDirect report, July 14, 2011), 2.

³ Office of Management and Budget, *Historical Tables, Budget of the US Government, Fiscal Year 2018*, "Summary of Receipts, Outlays, and Surpluses or Deficits (-) as Percentages of GDP: 1930–2022," table 1.2.

⁴ Janet Hook, "Deficit Concern Fades in Congress, among Voters and on the 2016 Trail," *Wall Street Journal*, December 22, 2015.

⁵ Congressional Budget Office, *The 2017 Long-Term Budget Outlook* (March 2017).

⁶ Office of Management and Budget, *Historical Tables, Budget of the US Government, Fiscal Year 2018*, "Federal Debt at the End of the Year: 1940–2022," table 7.1.

⁷ Congressional Budget Office, *2017 Long-Term Budget Outlook*, 3; United States Department of the Treasury, *The Financial Report of the United States: FY 2016* (January 2017), 6.

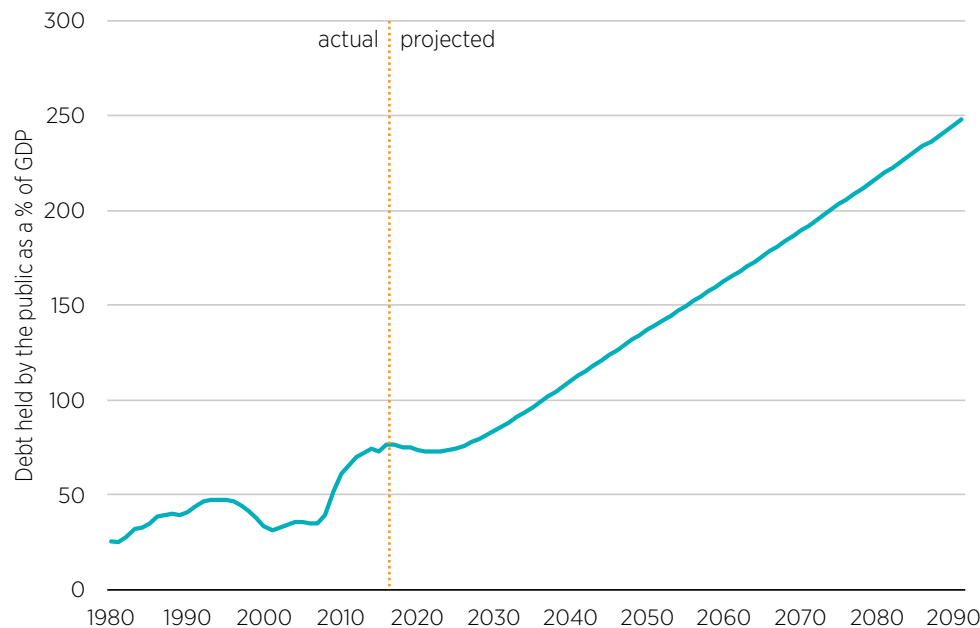
⁸ The Treasury Department defines sustainable fiscal policy as "one where the ratio of debt held by the public to Gross Domestic Product (GDP) (the debt-to-GDP ratio) is stable or declining over the long term." US Treasury, *Financial Report of the United States*, 5.

⁹ Congressional Budget Office, *2017 Long-Term Budget Outlook*, iii.

¹⁰ Carmen M. Reinhart, Vincent R. Reinhart, and Kenneth S. Rogoff, "Public Debt Overhangs: Advanced Economy Episodes Since 1800," *Journal of Economic Perspectives* 26, no. 3 (2012).

¹¹ Andrea Pescatori, Damiano Sandri, and John Simon, "Debt and Growth: Is There a Magic Threshold?" (IMF Working Paper WP/14/34, International Monetary Fund, February 2014).

FIGURE 1. US DEBT HELD BY THE PUBLIC, 1980–2091



What’s worse, the longer Congress waits to act, the more difficult reform will be. To give you a sense of magnitude, CBO estimates that preventing the nation’s debt from rising relative to the size of the economy over the next 40 years requires a permanent shift in expenditures and revenues of 1.9 percent of GDP (\$1,100 per person), starting today. If we wait 10 years to take action, the bill goes up to 2.9 percent of GDP (approximately \$1,900 per person in today’s dollars).¹²

Put another way, a delay means that Americans will need to give up a bigger piece of the nation’s economic pie to stabilize the country’s finances—a slice that may exceed the growth of the economy—on top of facing the consequences of lower economic growth due to excessive debt levels in the meantime.

THE PATH TO REFORM: POLITICAL AND PROCEDURAL HURDLES

To get on a stable fiscal path and stay there, Congress needs to act quickly and credibly. The solutions, which must include reforms to entitlements such as Medicare and Social Security, will not be easy to implement. Congressional reelection motivations make it tempting for lawmakers to leave difficult decisions about programs like these for tomorrow.¹³ Waiting until there is the “political will” to act typically means waiting until a crisis occurs.

Even if these political hurdles can be overcome, Congress faces still another obstacle—itsself. Article I, section 5 of the Constitution reads, in part, “Each House may determine the rules of its proceedings.” This single line constitutes a major obstacle for legislators attempting to enforce budget rules. More generally, Congress, unlike a corporation, cannot write a contract that binds future members. This is true with respect to both substantive reforms—such as changes to entitlements—and process reforms—such as changes to budget rules. Congressional budget rules are routinely gamed, ignored, or changed, which is not surprising given the lack of strong enforcement mechanisms available to legislators. What Congress does today, a future Congress can undo tomorrow.

¹² Congressional Budget Office, *2017 Long-Term Budget Outlook*, 22, 25, and author’s calculations.

¹³ For more details on how the nature of the country’s fiscal problems makes reform difficult given the reelection motivations of politicians, see Primo, “Making Budget Rules Work.”

A WELL-DESIGNED CONSTITUTIONAL AMENDMENT CAN PROVIDE THE FOUNDATION FOR CREDIBLE AND SUSTAINABLE FISCAL POLICY

A well-designed constitutional amendment would place permanent, truly enforceable limits on Congress's ability to tax and spend. A constitutional amendment would counteract the temptation to circumvent rules, and it would also provide a foundation on which a new budget process could be built. Just as importantly, it would create an environment under which the question for members would no longer be *whether* to fix the nation's fiscal problems, but, rather, *how* to do so.

The promise of a constitutional amendment as an enforcement mechanism lies in its durability, but this durability is also a peril: bad rules can be locked in just as good rules can be. While there are many ways such a constitutional amendment could be structured, all worthwhile proposals should possess certain features. Table 1 lists 10 principles for budget rule design, and I will highlight some of them in what follows.

TABLE 1. TEN PRINCIPLES OF BUDGET RULE DESIGN

- 1. Use budget rules to change the terms of the debate.** Budget battles will be fought differently if fiscal responsibility is a requirement, not an option.
- 2. Apply rules permanently and to the entire federal budget.** Temporary rules or rules exempting certain programs won't help in the long run.
- 3. Focus on spending.** Washington cannot address the looming budget crisis without gaining control of the unsustainable spending growth that drives it.
- 4. Build flexibility into rules by "smoothing."** Tie budget rule targets or limits to a multiyear period or long-term economic performance to accommodate economic downturns or other transitory events.
- 5. Build flexibility into rules by incorporating limited, carefully constructed emergency provisions.** Account for major disruptions like war.
- 6. Be precise to prevent loopholes and gimmicks.** History proves that if there is a way around a rule, a legislator will find it.
- 7. Pay careful attention to "starting points."** Consider cutting inflated spending levels (e.g., from stimulus) prior to pegging permissible increases to the current budget.
- 8. Fight against faux fiscal discipline and resist the temptation to compromise on rule design.** You are better off with no rule than a badly designed one.
- 9. Use a commission as a supplement to, not a replacement for, a budget rule.** Commissions are great for specifics, but they can't produce change without some other external pressure.
- 10. Incorporate well-designed rules into the US Constitution.** While there are pros and cons to constitutional rules, without this external enforcement, budget rules will always be vulnerable to legislators' propensity to break them.

Source: These principles are drawn from David M. Primo, "Making Budget Rules Work, 2014 Edition" (Mercatus Research, Mercatus Center at George Mason University, 2014).

First, a constitutional amendment should be flexible enough to account for major disruptions, like war. To avoid allowing “emergencies” to become routine, Congress should be permitted to waive the amendment’s spending or deficit limits only with the agreement of a large supermajority. In addition, any funds borrowed under an emergency waiver should be paid back within a set amount of time—say 10 to 15 years.

At the same time, the amendment should be precise enough to prevent end runs around its provisions. It should clearly define spending and revenue, for example, and specify how each will be calculated. These definitions should not be left to implementing legislation.

Finally, the amendment should account for economic ups and downs by setting targets or limits based on a multiyear period or on long-term economic performance. A key advantage of this smoothing approach, which has been adopted in countries like Germany and Switzerland, is that it necessitates fewer sudden changes to government programs.

An amendment that has economic shock absorbers and is hard to evade—but is possible to waive temporarily in the case of a true emergency—would help make fiscal stability, not political uncertainty, the new norm in American politics.

WHAT THE CRITICS GET WRONG

Of course, nothing is perfect, and skeptics of constitutional budget rules criticize them in two important ways. First, they point to specific design flaws, such as a requirement that budgets be perfectly balanced each year.¹⁴ These sorts of critiques reinforce the need for careful rule design, but they do not justify the outright rejection of constitutional reform. Instead of requiring perfect balance, for instance, an amendment could mandate a multiyear smoothing approach, as discussed earlier.

Others worry about US Supreme Court overreach if the court is given the authority to adjudicate disputes about the amendment.¹⁵ These concerns about judicial involvement can be addressed by limiting remedies and clarifying which parties have standing. Moreover, the clearer a rule is, the less leeway the justices will have in interpreting it.

CONCLUSION

In closing, amending the US Constitution is a serious step for the country, and one fraught with political and procedural challenges. We are much less likely to achieve credible, long-term budget changes, however, without such a provision. While successes in budgeting do occur on occasion—for instance, when President Bill Clinton and House Speaker Newt Gingrich worked together to balance the budget in the 1990s—these successes have typically been short-lived (just like that balanced budget). A constitutional amendment can help make future budget agreements durable and reduce political uncertainty.

Thank you again for inviting me to testify today. I welcome your questions.

¹⁴ See, for example, Ramesh Ponnuru, “A Balanced Budget Amendment: Still a Terrible Idea,” *Bloomberg News*, February 18, 2013.

¹⁵ See, for example, Robert H. Bork, “On Constitutional Economics,” *Regulation* 7, no. 5 (1983); Kathleen Sullivan, “Constitutional Amendmentitis,” *American Prospect Magazine* 6, no. 23 (1995).