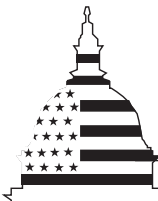


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# BUDGET PROCESS

## Considerations for Updating the Budget Enforcement Act

Statement of Susan J. Irving  
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**Abstract**

It is a pleasure to join you as you think about how to extend and adapt the Budget Enforcement regime. The discretionary spending limits and pay-as-you-go (PAYGO) mechanism established by the Budget Enforcement Act (BEA) will expire in fiscal year 2002. Perhaps this timing is appropriate: although most of us would argue that some controls are necessary even in a time of surplus, the details will be different in a time of surplus than a time of deficit. Among the issues your staff asked me to cover is whether and if so how the budget process can be designed to help avoid what has been described as the year-end train wreck. Later in this statement I will talk about some of the particular ideas that have been proposed in this area. First, however, I'd like to talk a bit about what a process can and cannot do. A process can surface important issues; it can seek to focus the debate on the important choices. But it is not a substitute for substantive debate. A process can force agreement where one does not exist. We ask a great deal of our budget process. We use it to determine aggregate fiscal policy and to allocate resources across different claims. We use it to drive program management. In the context of the Government Performance and Results Act of 1993, we turn to the budget to tell us something about the cost of obtaining a given level of results. Asking the process to take on the job of avoiding a train wreck may be more than can reasonably be expected. A year-end train wreck is the result of failing to reach agreement or at least a compromise acceptable to all parties earlier in the year. Although it is possible that reaching agreement on some broad parameters early on could facilitate a smoother process, it is not clear that such an agreement will always prevent gridlock. It may just come earlier. The details of implementing broad agreements are often the subject of heated debate.

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Mr. Chairman, Mr. Spratt, Members of the Committee:

It is a pleasure to join you as you think about how to extend and adapt the Budget Enforcement regime. The discretionary spending limits and pay-as-you-go (PAYGO) mechanism established by the Budget Enforcement Act (BEA) will expire in fiscal year 2002.<sup>1</sup> Perhaps this timing is appropriate: although most of us would argue that some controls are necessary even in a time of surplus, the details will be different in a time of surplus than a time of deficit.

Among the issues your staff asked me to cover is whether—and if so how—the budget process can be designed to help avoid what has been described as the year-end “train wreck.” Later in this statement I will talk about some of the particular ideas that have been proposed in this area. First, however, I’d like to talk a bit about what a process can and cannot do. A process can surface important issues; it can seek to focus the debate on the important choices. But it is not a substitute for substantive debate—no process can force agreement where one does not exist.

We ask a great deal of our budget process. We use it to determine aggregate fiscal policy and to allocate resources across different claims. We use it to drive program management. In the context of the Government Performance and Results Act of 1993, we turn to the budget to tell us something about the cost of obtaining a given level of results. Asking the process to take on the job of avoiding a “train wreck” may be more than can reasonably be expected.

A year-end “train wreck” is the result of failing to reach agreement—or at least a compromise acceptable to all parties—earlier in the year. Although it is possible that reaching agreement on some broad parameters early on could facilitate a smoother process, it is not clear that such an agreement will always prevent gridlock—it may just come earlier. The details of implementing broad agreements are often the subject of heated debate.

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<sup>1</sup>Although the overall discretionary spending caps expire in 2002, the Highway and Mass Transit outlay caps established under Transportation Equity Act for the 21st Century (TEA-21) continue through 2003, and the conservation caps established as part of the fiscal year 2001 Interior Appropriations Act were set through 2006. In addition, the sequestration procedure applies through 2006 to eliminate any projected net costs stemming from PAYGO legislation enacted through fiscal year 2002.

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BEA, when first developed and later when it was extended, was a process established to enforce a previously reached substantive agreement. As we move from seeking to reduce the deficit to debating how much of the surplus should be used, agreement on a broad fiscal policy posture might help. How much of the surplus should be used to meet demands for tax cuts and/or spending increases and how much for debt reduction? The Congress and the President seem to have reached a tacit agreement that the Social Security surplus should be used for debt reduction. While this agreement sets the outside parameters for the budget debate, it does not settle either the distribution between tax cuts or spending increases or the allocation of either one. It is already evident that, by itself, this broad framework is unlikely to make for smooth sailing.

While an orderly process may be important, and avoiding a “train wreck” desirable, I believe there are other important issues to consider in designing the budget process. As I have testified before, the budget represents the decisions made about a large number of often conflicting objectives that citizens want the government to address. We should not be surprised that it generates controversy. As BEA expires and you move from fighting current deficits to prudent management of surpluses, you face a wealth of options and choices. I appreciate the invitation to talk about some of these today. Some of these points are discussed more fully in our recent BEA compliance report<sup>2</sup> that we prepared at your request, Mr. Chairman.

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## Principles for a Budget Process

In the past, we have suggested four broad principles or criteria for a budget process.<sup>3</sup> A process should

- provide information about the long-term impact of decisions, both macro—linking fiscal policy to the long-term economic outlook—and micro—providing recognition of the long-term spending implications of government commitments;
- provide information and be structured to focus on important macro trade-offs—e.g., between investment and consumption;

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<sup>2</sup> *Budget Issues: Budget Enforcement Compliance Report* (GAO-01-777, June 15, 2001).

<sup>3</sup> For a fuller discussion of these criteria, see *Budget Process: Evolution and Challenges* (GAO/T-AIMD-96-129, July 11, 1996), *Budget Process: History and Future Directions* (GAO/T-AIMD-95-214, July 13, 1995), and *Budget Process: Comments on H.R. 853* (GAO/T-AIMD-99-188, May 12, 1999).

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- provide information necessary to make informed trade-offs between missions (or national needs) and between the different policy tools of government (such as tax provisions, grants, and credit programs); and
  - be enforceable, provide for control and accountability, and be transparent, using clear, consistent definitions.

The lack of adherence to the original BEA spending constraints in recent years, the nearing expiration of BEA, and the projection of continued and large surpluses in the coming years suggest that now may be an opportune time to think about the direction and purpose of our nation's fiscal policy. In a time of actual and projected surpluses, the goal of zero deficit no longer applies. Rather, discussion shifts toward how to allocate surpluses among debt reduction, spending increases, and tax cuts. Only then can limits on subcategories of spending be set. Will the entire social security surplus be "saved"? What about the Medicare Part A surplus? In our work on other countries that also have faced the challenge of setting fiscal policy in times of surplus, we found that as part of a broad fiscal policy framework some countries adopted fiscal targets such as debt-to-gross domestic product (GDP) ratios to serve as guides for decision-making.

Complicating the discussion on formulating fiscal policy in a time of surplus is the fact that the long-term picture is not so good. Despite current projections that show surpluses continuing over the 10-year budget window, our long-term budget simulations show a resumption of significant deficits emerging after the anticipated demographic tidal wave of population aging hits. These demographic trends serve to emphasize the importance of the first principle cited above—the need to bring a long-term perspective to bear on budget debates. Keeping in mind these principles and concerns, a number of alternatives appear promising.

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## Alternatives for Improving the Budget Process

There is a broad consensus among observers and analysts who focus on the budget both that BEA has constrained spending and that continuation of some restraint is necessary even with the advent of actual and projected surpluses. Discussions on the future of the budget process have primarily focused on revamping the current budget process rather than establishing a new one from scratch.

Where discussion has moved beyond a general call for continued restraint to specific control devices, the ones most frequently discussed are (1) extending the discretionary spending caps, (2) extending the PAYGO mechanism, and (3) creating a trigger device or a set of rules specifically

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designed to deal with the uncertainty of budget projections. A new budget process framework could encompass any or all of these instruments.

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## Extending Caps on Discretionary Spending

BEA distinguished between spending controlled by the appropriations process—“discretionary spending”—and that which flowed directly from authorizing legislation provisions of law—“direct spending,” sometimes called “mandatory.” Caps were placed on discretionary spending—and the Congress’ compliance with the caps was relatively easy to measure because discretionary spending totals flow directly from legislative actions (i.e., appropriations laws). There is broad consensus that, although the caps have been adjusted, they have served to constrain appropriations. This consensus combined with the belief that some restraints should be continued has led many to propose that some form of cap structure be continued as a way of limiting discretionary appropriations. However, the actions in the last 2 years have also led many to note that caps can only work if they are realistic; while caps may be seen as tighter than some would like, they are not likely to bind if they are seen as totally unreasonable given current conditions.

Further, some have proposed that any extension of BEA-type caps be limited to caps on budget authority. Outlays are controlled by and flow from budget authority—although at different rates depending on the nature of the programs. Some argue that the existence of both budget authority and outlay caps has encouraged provisions such as “delayed obligations” to be adopted not for programmatic reasons but as a way of juggling the two caps. The existence of two caps may also skew authority from rapid spendout to slower spendout programs, thus pushing more outlays to the future and creating problems in complying with outlay caps in later years. Extending only the budget authority cap would eliminate the incentive for such actions and focus decisions on that which the Congress is intended to control—budget authority, which itself controls outlays. This would be consistent with the original design of BEA.

Eliminating the outlay cap would raise several issues—chief among them being how to address the control of transportation programs for which no budget authority cap currently exists, and the use of advance appropriations to skirt budget authority caps. However, agreements about these issues could be reached—this is not a case where implementation difficulties need derail an idea. For example, the fiscal year 2002 budget proposes a revision to the scorekeeping rule on advance appropriations so that generally they would be scored in the year of enactment. If the Budget Committees and CBO agree, this change could eliminate the practice of

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using advance appropriations to skirt the caps. The obvious advantage to focusing decisions on budget authority rather than outlays is that the Congress would not spend its time trying to control that which by design is the result of its budget authority decisions—the timing of outlays.

There are other issues in the design of any new caps. For example, for how long should caps be established? What categories should be established within or in lieu of an overall cap? While the original BEA envisioned three categories (Defense, International Affairs, and Domestic), over time categories were combined and new categories were created. At one time or another caps for Nondefense, Violent Crime Reduction, Highways, Mass Transit, and Conservation spending existed—many with different expiration dates. Should these caps be ceilings, or should they—as is the case for Highways and Conservation—provide for “guaranteed” levels of funding? The selection of categories—and the design of the applicable caps—is not trivial. Categories define the range of what is permissible. By design they limit trade-offs and so constrain both the Congress and the President.

Because caps are phrased in specific dollar amounts, it is important to address the question of when and for what reasons the caps should be adjusted. This is critical for making the caps realistic. For example, without some provision for emergencies, no caps can be successful. At the same time, there appears to be some connection between how realistic the caps are and how flexible the definition of emergency is. As discussed in last year’s compliance report, the amount and range of spending considered “emergency” has grown in recent years. There have been a number of approaches suggested to balance the need to respond to emergencies and the desire to avoid making the “emergency” label an easy way to raise caps. In the budget resolution for fiscal year 2001 [H. Con. Res. 290], the Congress said it would limit emergencies to items meeting five criteria: (1) necessary, essential, or vital (not merely useful or beneficial), (2) sudden, quickly coming into being, and not building up over time, (3) an urgent, pressing, and compelling need requiring immediate action, (4) unforeseen, unpredictable, and unanticipated, and (5) not permanent, temporary in nature. The resolution further required any proposal for emergency spending that did not meet all the criteria to be accompanied by a statement of justification explaining why the requirement should be accorded emergency status. The fact that this provision was ignored during debates on fiscal year 2001 appropriations bills emphasizes that no procedural hurdle can succeed without the will of the Congress. Others have proposed providing for more emergency spending—either in the form of a reserve or in a greater appropriation for

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the Federal Emergency Management Agency (FEMA)—under any caps. If such an approach were to be taken, the amounts for either the reserve or the FEMA disaster relief account would need to be included when determining the level of the caps. Some have proposed using a 5- or 10-year rolling average of disaster/emergency spending as the appropriate reserve amount. Adjustments to the caps would be limited to spending over and above that reserve or appropriated level for extraordinary circumstances. Alternatively, with additional up-front appropriations or a reserve, emergency spending adjustments could be disallowed.<sup>4</sup>

Even with this kind of provision only the commitment of the Congress and the President can make any limit on cap adjustments for emergencies work. States have used this reserve concept for emergencies, and their experiences indicate that criteria for using emergency reserve funds may be useful in controlling emergency spending.<sup>5</sup> Agreements over the use of the reserve would also need to be achieved at the federal level.

This discussion is not exhaustive. Other issues would come up in extending BEA. Previously, we have reported on two issues—the scoring of operating leases and the expansion of user fees as offsets to discretionary spending; because I think they need to be considered, let me touch on them briefly.

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## Miscellaneous Discretionary Challenges: Leases and User Fees

We have previously reported that existing scoring rules favor leasing when compared to the cost of various other methods of acquiring assets.<sup>6</sup> Currently, for asset purchases, budget authority for the entire acquisition cost must be recorded in the budget up front, in the year that the asset acquisition is approved. In contrast, the scorekeeping rules for operating leases often require that only the current year's lease costs be recognized and recorded in the budget. This makes the operating lease appear less costly from an annual budgetary perspective, and uses up less budget authority under the cap. Alternative scorekeeping rules could recognize

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<sup>4</sup>The administration's fiscal year 2002 budget submission included a proposal to set aside a reserve for emergency needs in the annual budget and appropriations process, arguing that this would limit the need for emergency supplementals to extremely rare events.

<sup>5</sup>*Budgeting for Emergencies: State Practices and Federal Implications* (GAO/AIMD-99-250, Sept. 30, 1999).

<sup>6</sup>*Budget Issues: Budget Scorekeeping for Acquisition of Federal Buildings* (GAO/T-AIMD-94-189, Sept. 20, 1994).

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that many operating leases are used for long-term needs and should be treated on the same basis as purchases. This would entail scoring up front the present value of lease payments covering the same period used to analyze ownership options. The caps could be adjusted appropriately to accommodate this change.

Many believe that one unfortunate side effect of the structure of the BEA has been an incentive to create revenues that can be categorized as “user fees” and so offset discretionary spending—rather than be counted on the PAYGO scorecard. The 1967 President’s Commission on Budget Concepts recommended that receipts from activities that were essentially governmental in nature, including regulation and general taxation, be reported as receipts, and that receipts from business-type activities “offset to the expenditures to which they relate.” However, these distinctions have been blurred in practice. Ambiguous classifications combined with budget rules that make certain designs most advantageous has led to a situation in which there is pressure to treat fees from the public as offsets to appropriations under BEA caps, regardless of whether the underlying federal activity is business or governmental in nature. Consideration should be given to whether it is possible to come up with and apply consistent standards—especially if the discretionary caps are to be redesigned. The administration has stated that it plans to monitor and review the classification of user fees and other types of collections.

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## Extending and Refining PAYGO

The PAYGO requirement prevented legislation that lowered revenue, created new mandatory programs, or otherwise prevented direct spending from increasing the deficit unless offset by other legislative actions. As long as the unified budget was in deficit, the provisions of PAYGO—and its application—were clear. The shift to surplus raised questions about whether the prohibition on increasing the deficit also applied to reducing the surplus. Although the Congress and the executive branch have both concluded that PAYGO does apply in such a situation, any extension should eliminate potential ambiguity in the future.

This year, the administration has proposed—albeit implicitly—special treatment for a tax cut. The budget states that the President’s tax plan and Medicare reforms are fully financed by the surplus and that any other spending or tax legislation would need to be offset by reductions in spending or increases in receipts. It is possible that in a time of budget surplus, the Congress might wish to modify PAYGO to permit increased direct spending or lower revenues as long as debt held by the public is planned to be reduced by some set percentage or dollar amount. Such a

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provision might prevent PAYGO from becoming as unrealistic as overly tight caps on discretionary spending. However, the design of such a provision would be important—how would a debt reduction requirement be specified? How would it be measured? What should be the relationship between the amount of debt reduction required and the amount of surplus reduction (i.e., tax cut or direct spending increase) permitted? What, if any, relationship should there be between this calculation and the discretionary caps?

While PAYGO constrained the creation or legislative expansion of direct spending programs and tax cuts, it accepted the existing provisions of law as given. It was not designed to trigger—and it did not trigger—any examination of “the base.” Cost increases in existing mandatory programs are exempt from control under PAYGO and could be ignored. However, constraining changes that increase the cost of entitlements and mandatoriness is not enough. Our long-term budget simulations show that as more and more of the baby boom generation retires, spending for Social Security, Medicare, and Medicaid will demand correspondingly larger shares of federal revenues. The growth in these programs will increasingly restrict budgetary flexibility. Even if the Social Security surpluses are saved and used for debt reduction, unified deficits are projected to emerge in about two decades, and by 2030 Social Security, Medicare, and Medicaid would require more than three-fourths of federal revenues.<sup>7</sup>

Previously we suggested some sort of “lookback” procedure to prompt a reexamination of “the base.” Under such a process, the Congress could specify spending targets for PAYGO programs for several years. The President could be required to report in his budget whether these targets either had been exceeded in the prior year or were likely to be exceeded in the current or budget years. He could then be required to recommend whether any or all of this overage should be recouped—and if so, to propose a way to do so. The Congress could be required to act on the President’s proposal.

While the current budget process contains a similar point of order against worsening the financial condition of the Social Security trust funds,<sup>8</sup> it

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<sup>7</sup> *Long-Term Budget Issues: Moving From Balancing the Budget to Balancing Fiscal Risk* (GAO-01-385T, Feb. 6, 2001).

<sup>8</sup> 2 U.S.C. 632 (i), and *Medicare Reform: Issues Associated With General Revenue Financing* (GAO/T-AIMD-00-126, Mar. 27, 2000).

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would be possible to link “tripwires” or triggers to measures related to overall budgetary flexibility or to specific program measures. For example, if the Congress were concerned about declining budgetary flexibility, it could design a tripwire tied to the share of the budget devoted to mandatory spending or to the share devoted to a major program.

Other variations of this type of tripwire approach have been suggested. The 1999 Breaux-Frist proposal (S. 1895) for structural and substantive changes to Medicare financing contained a new concept for measuring “programmatically insolvency” and required congressional approval of additional financing if that point was reached. Other specified actions could be coupled with reaching a tripwire, such as requiring the Congress or the President to propose alternatives to address reforms or, by using the congressional budget process, requiring the Congress to deal with unanticipated cost growth beyond a specified tripwire by establishing a point of order against a budget resolution with a spending path exceeding the specified amount. One example of a threshold might be the percentage of GDP devoted to Medicare. The President would be brought into the process as it progressed because changes to deal with the cost growth would require enactment of a law.

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## Improving the Recognition of Long-Term Commitments

In previous reports we have argued that the nation’s economic future depends in large part upon today’s budget and investment decisions.<sup>9</sup> In fact, in recent years there has been increased recognition of the long-term costs of Social Security and Medicare.<sup>10</sup>

While these are the largest and most important long-term commitments—and the ones that drive the long-term outlook—they are not the only ones in the budget. Even those programs too small to drive the long-term outlook affect future budgetary flexibility. For the Congress, the President, and the public to make informed decisions about these other programs, it is important to understand their long-term cost implications.

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<sup>9</sup>See *Budget Process: Evolution and Challenges* (GAO/T-AIMD-96-129, July 11, 1996) and *The Deficit and the Economy: An Update of Long-Term Simulations* (GAO/AIMD/OCE-95-119, Apr. 26, 1995), among others.

<sup>10</sup>*Budget of the United States Government, Fiscal Year 2002*, OMB, Apr. 9, 2001; *The Budget and Economic Outlook: Fiscal Years 2002-2011*, CBO, Jan. 2001; GAO-01-385T, Feb. 6, 2001; and *Medicare: Higher Expected Spending and Call for New Benefit Underscore Need for Meaningful Reform* (GAO-01-539T, Mar. 22, 2001).

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While the budget was not designed to and does not provide complete information on long-term cost implications stemming from some of the government's commitments when they are made, progress can be made on this front. The enactment of the Federal Credit Reform Act in 1990 represented a step toward improving both the recognition of long-term costs and the ability to compare different policy tools. With this law, the Congress and the executive branch changed budgeting for loan and loan guarantee programs. Prior to the Credit Reform Act, loan guarantees looked "free" in the budget. Direct loans looked like grant programs because the budget ignored loan repayments. The shift to accrual budgeting for subsidy costs permitted comparison of the costs of credit programs both to each other and to spending programs in the budget.

Information should be more easily available to the Congress and the President about the long-term cost implications both of existing programs and new proposals. In 1997 we reported that the current cash-based budget generally provides incomplete information on the costs of federal insurance programs.<sup>11</sup> The ultimate costs to the federal government may not be apparent up front because of time lags between the extension of the insurance, the receipt of premiums, and the payment of claims. While there are significant estimation and implementation challenges, accrual-based budgeting has the potential to improve budgetary information and incentives for these programs by providing more accurate and timely recognition of the government's costs and improving the information and incentives for managing insurance costs. This concept was proposed in the Comprehensive Budget Process and Reform Act of 1999 (H.R. 853), which would have shifted budgetary treatment of federal insurance programs from a cash basis to an accrual basis.

There are other commitments for which the cash- and obligation-based budget does not adequately represent the extent of the federal government's commitment. These include employee pension programs, retiree health programs, and environmental cleanup costs. While there are various analytical and implementation challenges to including these costs in budget totals, more could be done to provide information on the long-term cost implications of these programs to the Congress, the President, and the interested public. At the request of this Committee, we are continuing to address this issue.

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<sup>11</sup> *Budget Issues: Budgeting for Federal Insurance Programs* (GAO/AIMD-97-16, Sept. 30, 1997).

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## Dealing With the Uncertainty of Projections

As the budgeting horizon expands, so does the certainty of error. Few forecasters would suggest that 10-year projections are anything but that—projections of what the world would look like if it continued on a line from today. And long-term simulations are useful to provide insight as to direction and order of magnitude of certain trends—not as forecasts. Nevertheless, budgeting requires forecasts and projections. Baseline projections are necessary for measuring and comparing proposed changes. Former Congressional Budget Office (CBO) Director Rudy Penner suggested that 5-year and 10-year projections are useful for and should be used for different purposes: 5-year projections for indicating the overall fiscal health of the nation, and 10-year projections for scorekeeping and preventing gaming of the timing of costs.

No 10-year projection is likely to be entirely correct; the question confronting fiscal policymakers is how to deal with the risk that a projection is materially wrong. This year some commentators and Members of the Congress have suggested dealing with this risk by using triggers. Triggers were part of both Gramm-Rudman-Hollings (GRH) and BEA. The GRH triggers were tied to deficit results and generally regarded as a failure—they were evaded or, when deficits continued to exceed the targets, the targets were changed. BEA triggers have been tied to congressional action rather than to deficit results; sequesters have rarely been triggered—and those were very small. This year the discussion of triggers has been tied specifically to the tax debate and to whether the size of the tax cut in future years should be linked to budget results in those years. There could be several variations on this trigger: actual surplus results, actual revenue results (this with the intent of avoiding a situation in which spending increases can derail a tax cut), and actual debt results. There is little consensus on the effectiveness of any triggers.

Although the debate about triggers has been tied to the tax debate in 2001, there is no inherent reason to limit the discussion to taxes. Some might wish to consider triggers that would cause decisionmakers to make proposals to address fiscal results that exceed some specific target, such as debt or spending as a share of GDP.

Former CBO Director Robert Reischauer suggested another way of dealing with the fact that forecasts/projections become less certain the further they go into the future. Under his proposal, a declining percentage of any projected surplus would be available—either for tax cuts or for spending increases. Specifically, 80 percent of the surplus would be available to legislators in years 1 and 2, 70 percent in years 3 and 4, 60 percent in years 5 and 6, until reaching the 40-percent level in years 9 and 10. The

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consequence of not adhering to these limits would be an across-the-board sequester. When a new Congress convenes, it would be given a new budget allowance to spend based on a new set of surplus projections.

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## Other Ideas Proposed to Smooth the Process

Others have suggested that mechanisms such as a joint budget resolution and/or an automatic continuing resolution could avert the year-end disruption caused by an inability to reach agreement on funding the government. Biennial budgeting is also sometimes suggested as a better way to budget and to provide agencies more certainty in funding over 2 years. Let me turn now to these ideas.

Since agreement on overall budget targets can set the context for a productive budget debate, some have suggested that requiring the President's signature on budget resolutions would facilitate the debate within such a framework. Proposals to replace the Concurrent Resolution with a Joint Resolution should be considered in the light of what the budget resolution represents. Prior to the 1974 act only the President had a budget—that is, a comprehensive statement of the level of revenues and spending and the allocation of that spending across “national needs” or federal mission areas. Requiring the President to sign the budget resolution means it would not be a statement of congressional priorities. Would such a change reduce the Congress' ability to develop its own budget and so represent a shift of power from the Congress to the President? Whose hand would it strengthen? If it is really to reduce later disagreement, would it merely take much longer to get a budget resolution than it does today? It could be argued that under BEA the President and the Congress have—at times—reached politically binding agreements without a joint budget resolution.

The periodic experience of government “shutdowns”—or partial shutdowns when appropriations bills have not been enacted has led to proposals for an automatic continuing resolution. The automatic continuing resolution, however, is an idea for which the details are critically important. Depending on the detailed structure of such a continuing resolution, the incentive for policymakers—some in the Congress and the President—to negotiate seriously and reach agreement may be lessened. What about someone for whom the “default position” specified in the automatic continuing resolution is preferable than the apparent likely outcome? If the goal of the automatic continuing resolution is to provide a little more time for resolving issues, it could be designed to permit the incurrence of obligations to avoid a funding gap, but not the outlay of funds to liquidate the new obligations. This would

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allow agencies to continue operations for a period while the Congress completes appropriations actions.

Finally, you asked me to discuss proposals for biennial budgeting. Some have suggested that changing the appropriations cycle from annual to biennial could (1) provide more focused time for congressional oversight of programs, (2) shift the allocation of agency officials' time from the preparation of budgets to improved financial management and analysis of program effectiveness, and (3) enhance agencies' abilities to manage their operations by providing more certainty in funding over 2 years. Given the regularity with which proposals for biennial budgeting are made, I believe that at least some will consider the upcoming necessity to decide whether to extend BEA as an opportunity to again propose biennial budgeting.

Whether a biennial cycle offers the benefits sought will depend heavily on the ability of the Congress and the President to reach agreement on how to respond to uncertainties inherent in a longer forecasting period, for there will always be uncertainties. How often will the Congress and the President feel the need to reopen the budget and/or change funding levels?

Budgeting always involves forecasting, which in itself is uncertain, and the longer the period of the forecast, the greater the uncertainty. Our work has shown that increased difficulty in forecasting was one of the primary reasons states gave for shifting from biennial to annual cycles.<sup>12</sup> The budget is highly sensitive to the economy. Economic changes during a biennium would most likely prompt the Congress to revisit its decisions and reopen budget agreements. Among the issues that would need to be worked out if the Congress moves to a biennial budget cycle are how to update the CBO forecast and baseline against which legislative action is scored and how to deal with unexpected events. The baseline is important because CBO scores legislation based on the economic assumptions in effect at the time of the budget resolution. Even under an annual system there are years when this practice presents problems: in 1990 the economic slowdown was evident during the year, but consistent practice meant that bills reported in compliance with reconciliation instructions were scored based on the assumptions in the budget resolution rather than updated assumptions. If budget resolutions were biennial, this problem of

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<sup>12</sup>Since the mid-1960s, 18 states have changed their budget cycles: 11 from biennial to annual, 2 from annual to mixed, 4 from annual to biennial, and 1 from biennial to annual and back to biennial.

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outdated assumptions would be greater—some sort of update in the “off-year” likely would be necessary.

In any consideration of a biennial budget, it is important to recognize that even with annual budgets, the Congress already has provided agencies with multiyear funding to permit improved planning and management. As you know, it is not necessary to change the frequency of decisions in order to change the length of time funds are available. Nearly two-thirds of the budget is for mandatory programs and entitlements on which decisions are not made annually. Even the remaining portion that is on an annual appropriations cycle is not composed entirely of 1-year appropriations that expire on September 30 of each year. The Congress routinely provides multiyear or no-year appropriations when it seems to make sense to do so. Thus, to the extent that biennial budgeting is proposed as a way to ease a budget execution problem, the Congress has shown itself willing and able to meet that need under the current annual cycle.

If BEA is extended in conjunction with biennial budgeting, a whole host of technical issues needs to be considered. Would biennial budgeting change the timing of the BEA-required sequestration report? How would sequestrations be applied to the 2 years in the biennium and when would they occur? For example, if annual caps are continued and are exceeded in the second year of the biennium, when would the Presidential Order causing the sequestration be issued? Would the sequestration affect both years of the biennium? Would forecasts and baselines be updated during the biennium? These are just a few of the many questions that would need to be resolved.

Regardless of the potential benefits, the decision on biennial budgeting will depend on how the Congress chooses to exercise its constitutional authority over appropriations and its oversight functions. We have long advocated regular and rigorous congressional oversight of federal programs. Annual enacted appropriations have long been a basic means of exerting and enforcing congressional policy. Oversight has often been conducted in the context of agency requests for funds. A 2-year appropriation cycle would change—and could lessen—congressional influence over program and spending matters since the process would afford fewer scheduled opportunities to affect agency programs and budget.

Biennial budgeting would bring neither the end of congressional control nor the guarantee of improved oversight. It would require a change in the nature of that control. If the Congress decides to proceed with a change to

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a biennial budget cycle—including a biennial appropriations cycle—careful thought will need to be given to implementation issues.

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## Conclusion

To affect decision-making, the fiscal goals sought through a budget process must be accepted as legitimate. For many years the goal of “zero deficit”—or the norm of budget balance—was accepted as the right goal for the budget process. In the absence of the zero deficit goal, policymakers need an overall framework upon which a process and any targets can be based. Goals may be framed in terms of debt reduction or surpluses to be saved. In any case, compliance with budget process rules, in both form and spirit, is more likely if end goals, interim targets, and enforcement boundaries are both accepted and realistic.

Enforcement is more successful when it is tied to actions controlled by the Congress and the President. Both the BEA spending caps and the PAYGO enforcement rules were designed to hold the Congress and the President accountable for the costs of the laws enacted each session—not for costs that could be attributed to economic changes or other factors.

Today, the Congress and the President face a different budgetary situation than in the past few decades. The current budget challenge is not to achieve a balanced unified budget. Rather, budgeting today is done in the context of projections for continued and growing surpluses followed over the longer term by demography-driven deficits. What process will enable policymakers to deal with the near term without ignoring the long term? At the same time, the challenges for any budget process are the same: What process will enable policymakers to make informed decisions about both fiscal policy and the allocation of resources within the budget?

Extending the current BEA without setting realistic caps and addressing existing mandatory programs is unlikely to be successful for the long term. The original BEA employed limited actions in aiming for a balanced budget. It left untouched those programs—direct spending and tax legislation—already in existence. Going forward with new challenges, we believe that a new process that prompts the Congress to exercise more foresight in dealing with long-term issues is needed. The budget process appropriate for the early 21st century will have to exist as part of a broader framework for thinking about near- and long-term fiscal goals.

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Mr. Chairman, this concludes my statement. I would be happy to answer any questions that you or the Members of the Committee may have.

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## **Contacts and Acknowledgments**

For future contacts regarding this testimony, please call me at (202) 512-9142 or Christine Bonham at (202) 512-9576. Melinda Bowman also made key contributions to this testimony.