

The Budget at Midyear: Some Preliminary Impressions

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On June 28 the administration released its midsession review of the budget, while at the same time revising significantly the budget proposals it had presented in January. Since next year is a presidential election year, many believe that the next few months represent President Clinton's last major attempt to influence domestic policy.

This note is a preliminary attempt to explain the administration's budget and some of the changes—both economic and political—that have occurred since January.

First, the administration and Congress have essentially agreed they will not attempt to let temporary social security surpluses over the next 15 years become an excuse for running a deficit in the non-social security part of the budget. The unified budget—the budget encompassing all of government including social security—is running, and will continue to run, significant surpluses over this same period of time, barring dramatic actions by a future Congress. Tax cuts, whatever their size, will take a back seat to the effort to increase government saving.

Second, it is virtually certain that government saving, at least in the short run, will be in excess of social security saving projected under current law. That is, not all of the projected non-social security surpluses are likely to be spent either. As in January, the administration still attempts to achieve that goal by declaring it will "spend" some of those non-social security surpluses in the form of general revenue transfers to the social security and Medicare trust funds. But this is really just a form of saving.

While the budgeting methods proposed by the administration may or may not be accepted, Congress is in a box nonetheless. Since it has proposed no structural reform of social security, the administration must oppose an attempt to spend all of the non-social security surplus, or else it would be accused of having done nothing to bring social security and Medicare into greater balance. After all, the administration has always stated unequivocally that spending budget surpluses could not be done until some reform of social security and Medicare is undertaken. And it has come to define "reforming social security" not by bringing taxes and benefits in line for the long-run, but by putting some general revenues into the trust fund so that the entitlement program has a larger balance to draw on, at least for awhile. Therefore, on net there must be some additional saving to be able to claim that this symbolic goal has been met.

Third, the gap between receipts and outlays represents the amount of money that is typically "put in play" (for better or worse), and the amount of money we are talking about is becoming significant. The [figure below](#) shows the gap between receipts and outlays as projected until 2009 as a percentage of gross domestic product (GDP)—pending any real social security and Medicare reform. By 2009 the administration reckons that figure to rise to about 3.4 percent of GDP or close to \$475 billion annually in a GDP of \$13.9 trillion.

Fourth, the gap increases over time not because of projected changes in receipts, but because of a dramatic decline in outlays. The decline stems mainly from drastic reductions as a percentage of GDP in the discretionary part of the federal budget—the part that includes spending for defense, education, the environment, and most of what has traditionally been thought of as government activity. The budget already assumes that new discretionary authority will be required in the near term to meet some emergencies and pet projects, but then assumes that the pressures on the discretionary part of the budget will fall so substantially in the future that the long-term decline as a percentage of the GDP can continue (indeed, if we go to the president's budget released in January, it predicts the decline will continue without end). In effect, the new discretionary initiatives in the president's budget are assumed to have only a temporary bubble effect on a downward sloping trend of discretionary demands.

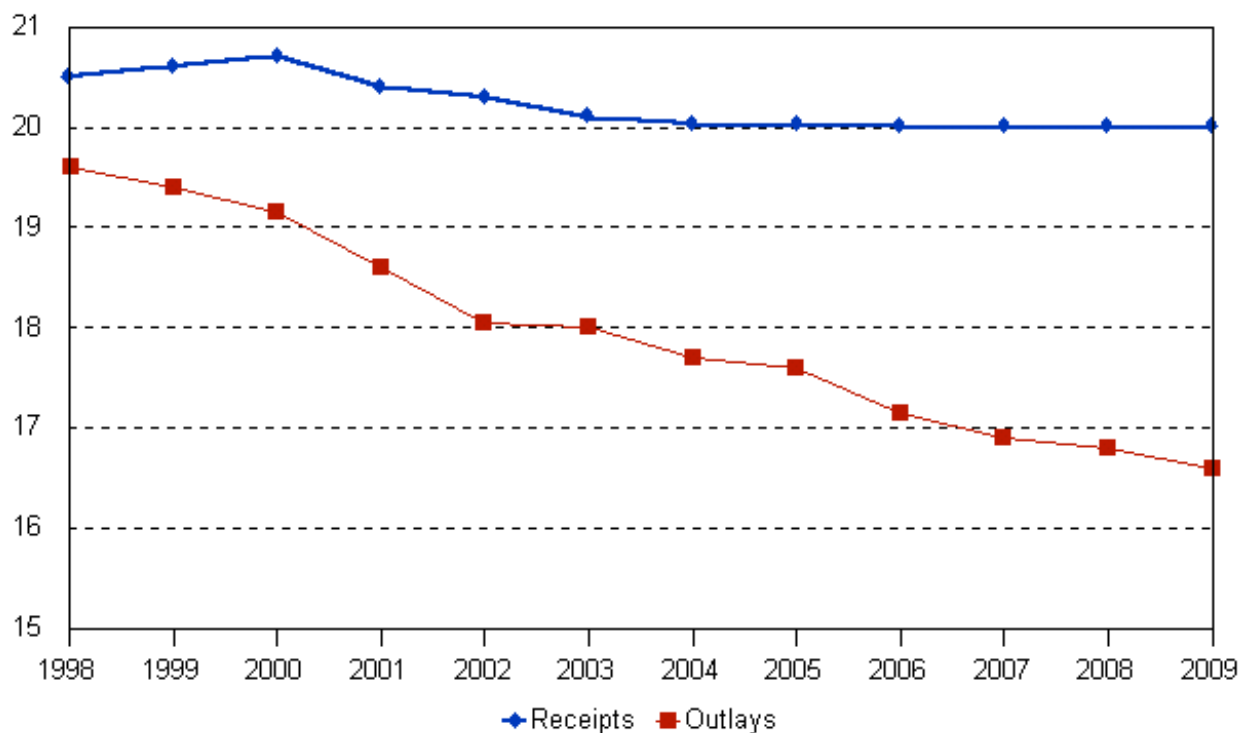
Fifth, Clinton has dramatically changed his focus from social security to Medicare. Under his current plan social

security would basically save its own surplus, which means no change to current law, until 2011. Only then would it start to receive some gradual transfers from general revenues. Medicare, on the other hand, would get even more transfers than social security. Moreover, Clinton wants to tack a new drug benefit on to Medicare that adds to the requirement for support out of general revenues.

Finally, the president has indicated both through the budget proposal and through his briefings that he may well go along with a tax bill this year. On net, the money he has put in play comes mainly from his Universal Savings Account proposal. For example, for 2004, tax relief proposals in the president's budget equal \$26.3 billion in USA subsidies, and \$7.3 billion in other subsidies. However, in that same year, Clinton would also raise substantial revenues through new tax provisions, including \$6.4 billion in tobacco taxes. On net, revenues as a percent of GDP would decline hardly at all—as can be seen from the chart—and some of the decline will occur anyway under current law.

Figures

**Receipts and Outlays, 1998-2009,
Pending Social Security and Medicare Reform
(Percentage of Gross Domestic Product)**



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