Q. How accurate are long-run budget projections?

A. Some elements of spending—health care costs and interest on the federal debt—are difficult to predict. But even in the best scenarios, the debt will continue to grow.

The Congressional Budget Office (CBO) has been making periodic long-run budget projections since the 1990s. Since then, policies have changed—as have the economic and demographic assumptions underlying the analysis. But the lesson from these projections has remained the same: the United States is on an unsustainable fiscal path. That is to say, if policies are not reformed, the public debt will grow until no prudent investor will buy US Treasury securities.

CAUSES OF RISING PUBLIC DEBT

The most important underlying cause of our rising public debt is population aging. The result is pressure on Social Security, the largest program in the budget, and on Medicare and Medicaid, the largest health insurance programs. Aging is relatively easy to forecast because life expectancy has typically increased steadily and current age demographics are well known. More difficult to forecast are birth rates and growth of the taxpaying population, but birth rates have remained low for a long time with no surprises.

Per person health costs have risen faster than incomes, after adjusting for the population aging that has driven the projected rise in total spending. But this “excess cost growth” is difficult to forecast. After constituting most total health cost growth for decades, excess cost growth slowed abruptly in the 2000s. And no one knows whether the slowdown will last or will be a one-time phenomenon.

Structural changes in the delivery of health care may hold down cost growth in the long run. On the other hand, excess cost growth might resume at historically familiar rates. In recent long-run projections, CBO has assumed that excess cost growth will indeed resume, but at a rate lower than the historical average.

MAJOR DISRUPTIONS TO THE GROWTH RATE OF PUBLIC DEBT

With Social Security and major health programs expected to grow faster than the economy and tax revenues, the deficit and public debt are expected to grow faster and interest on the debt to become a growing part of the budget. Over the twenty or so years that CBO has been making long-term budget projections, this basic story has held true. But three major surprises have caused the debt-GDP ratio to rise more slowly than predicted in some periods and faster in others.

The most important surprise slowing the growth of the debt-GDP ratio has been interest rates falling dramatically during and after the Great Recession. Despite a rise in the debt-GDP ratio from 39 percent in
How accurate are long-run budget projections?

2008 to 74 percent in 2014, interest payments on the debt actually fell! As of early 2020, 10-year Treasury rates were at record lows. If they persist, such low rates will limit growth of interest payment in coming years. The second surprise involved a surge in revenues related to the dot-com boom of the 1990s. It caused the debt-GDP ratio to fall from the mid-1990s to 2001, when the ratio was supposed to rise according to all long-term projections. The third surprise was the Great Recession that caused the debt-GDP ratio to rise far faster than could be explained by the increase in Social Security and health programs.

Despite the two big surprises that made the long-term outlook appear better than expected and the one surprise that made it look worse, the fundamentals of long-term projections have held true. Social Security and health programs have been on a strong upward trend propelled by aging and health costs, and there is little reason to expect this trend to evaporate. Because Social Security and health programs are therefore expected to become a greater and greater share of total spending, it is less and less likely that their effect on the deficit will be overwhelmed by surprises.

*Updated May 2020*

**Further Reading**


Q. What have budget trends been over the short and long term?

A. In the long run, federal budget deficits are driven by demography and rising health care costs pushing spending above scheduled revenues. Short-term deficits were traditionally driven by external events such as war and recession. In recent years, however, persistent deficits have also been driven by conscious policy choices. When events conspire to drive revenues above the trend, tax cuts usually bring them down with alacrity.

The budget deficit has been on a roller coaster in recent years because of the Great Recession and the subsequent recovery. (The federal budget deficit measures the amount by which total government outlays exceed total revenues in a given year.) In 2007, before the recession, the deficit had fallen to 1.1 percent of gross domestic product (GDP) despite the wars in Afghanistan and Iraq and significant tax cuts earlier in the decade. Then the recession hit and the deficit soared to 9.8 percent of GDP by 2009, as tax revenues fell, automatic safety net programs kicked in, and hundreds of additional billions were spent to stimulate the economy. But the economic recovery and subsequent economic expansion quickly lowered the deficit again. By 2015 it was 2.4 percent of GDP.

Since then, the deficit has grown faster than the economy, reaching 4.6 percent of GDP in 2019. That increase was driven by a combination of tax cuts (e.g., the tax cuts enacted at the end of 2017) and spending increases (e.g., the lifting of discretionary spending caps in early 2018). The Congressional Budget Office now projects deficits of $1 trillion or more each year in the next decade, reaching 5.4 percent of GDP in 2030.

SHORT TERM

As the deficit rises above $1 trillion in 2020, the debt-to-GDP ratio is expected to reach 81 percent by the end of 2020 and 98 percent in 2030. This will be the highest debt-to-GDP ratio since shortly after World War II.

All categories of spending will rise. Recent policy changes have not affected mandatory spending significantly and it will continue its upward trend, rising 14 percent between 2017 and 2020. Discretionary spending will rise 12 percent, largely because of the legislated increase in spending caps. The interest bill on the debt will rise 84 percent because of the large increase in the debt and a forecasted increase in interest rates.
Some Background

What have budget trends been over the short and long term?

Tax revenue will fall as a percentage of GDP. The recent tax cut will lower tax revenue from 17.3 percent of GDP in 2017 to 16.7 percent in 2020. Under constant law, one would normally expect tax revenues to grow faster than GDP because real growth pushes people into higher tax brackets.

LONG TERM

Over the longer run, programs targeting the aged will hasten spending growth as baby boomers continue to enter these programs and as expected lifespan once again increases. The main impact will be on spending for Social Security, Medicare, and Medicaid. Those three programs already account for over 50 percent of total spending and are expected to continue to grow faster than the economy and tax revenues for the foreseeable future. Medicare and Medicaid face the added challenge that even if the population were not aging, costs per recipient would be rising faster than incomes per capita after one adjusts for the effects of aging. This so-called excess cost growth slowed surprisingly after 2009. However, the Congressional Budget Office expects the growth of Medicare and Medicaid costs to reaccelerate, although not to the high levels experienced in recent decades.

The ratio of revenues to GDP was remarkably consistent over much of the past 50 years, almost always varying between 17 and 19 percent of GDP. Whenever the ratio rose above 19 percent, a significant tax cut followed. A surtax imposed during the Vietnam War pushed the ratio to 19 percent in 1969, but it was quickly removed. Rapid inflation again pushed the tax burden above 19 percent in 1981, provoking the large Reagan tax cuts. The Bush tax cuts of the early 2000s followed an enormous surge in revenues during the dot-com boom of the late 1990s that also pushed the tax burden above 19 percent.

The Great Recession was devastating to revenues and briefly brought them below 15 percent of GDP. Revenues recovered with the economy but in an unusual move, the government passed a major tax cut in 2017 when revenues were already near their historical lower bound of 17 percent. As a result, revenues are expected to drift slightly below 17 percent for the next few years. Excepting the Great Recession years, revenues only fell below 17 percent in four years between 1959 and 2017.

The growth of Social Security, Medicare, and Medicaid, combined with the reluctance to raise taxes, has been squeezing other entitlements and discretionary spending. Discretionary spending has been hit hardest, with defense falling from 9.1 percent of GDP at the height of the Vietnam War in 1968 to 3.2 percent in 2020. Nondefense spending has fallen somewhat more erratically to 3.2 percent of GDP in 2020 after reaching a 50-year high of 5.0 percent in 1978. The Congress was clearly reacting to these long-run declines when it significantly raised defense and nondefense discretionary spending in early 2018. It did not, however, pay for the increases with tax increases or cuts in other spending.

The growth in Social Security and health spending combined with a near constant tax burden leads to the conclusion that the United States is on an unsustainable fiscal path. If these well-entrenched fiscal policies continue, the deficit will persist on an upward trend and the debt will continually grow relative to GDP. Low interest rates have helped offset some fiscal pressures from accumulating debt. If interest rates rise, however, interest on the debt will become a major budget problem. Eventually, there may be no choice but to undertake painful spending and tax policy changes.

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Some Background

What have budget trends been over the short and long term?

Data Sources

Office of Management and Budget. Historical Tables.


Q. How much spending is uncontrollable?

A. Technically, lawmakers can control all spending except the interest due on government debts. However, entitlement spending is sometimes said to be uncontrollable for political rather than legal reasons. It can always be controlled legally by reforming programs, but when an entitlement is extremely popular, reform may require more political courage than is readily available. Similar concerns apply to many tax expenditures—tax breaks that function much as spending programs.

The federal budget divides government spending into three categories: discretionary spending, mandatory or direct spending, and net interest.

Discretionary spending, set in annual appropriations acts, includes most defense programs as well as spending for education, transportation, environmental protection, law enforcement and border security, international assistance, and a host of other programs.

Mandatory spending, controlled by laws other than appropriations acts, includes spending on entitlement programs. This includes the big three—Social Security, Medicare, and Medicaid—and many smaller programs such as supplemental nutrition assistance, federal civilian and military retirement benefits, and unemployment insurance. Spending is also mandatory for items the government cannot avoid, such as plaintiff awards from lawsuits.

Government spending on mandatory programs and net interest on the public debt are often described as “uncontrollable.” Entitlements can be controlled legally by reforming them, but this can be highly unpopular politically. Interest costs can be controlled indirectly by curbing spending growth or raising revenues, but that is also difficult.

Uncontrollable spending has been growing much more rapidly than total spending and thus accounts for an ever-larger share of the total. However, most growth has been concentrated in entitlements that serve the elderly and in health insurance. The population has been aging rapidly, and that affects both Social Security and health programs. The latter have grown twice as rapidly because even after adjusting for aging, health costs per beneficiary have been growing faster than incomes per capita. Health cost growth has slowed recently, but the Congressional Budget Office expects it to reaccelerate in the long run. Social Security and Medicare, the largest health program, are among the most politically popular programs.

Whereas discretionary programs are funded by specific appropriations that generally last only one year, entitlement spending for Social Security and Medicare is ongoing and is not scrutinized as carefully or as
often as discretionary spending. The laws establishing entitlements specify who is eligible and describe the benefits. The government then pays for as many eligible individuals as claim them. Thus, total entitlement spending cannot be predicted with precision from year to year—and is, in this narrow sense, “uncontrollable.”

**FIGURE 1**

**Composition of Federal Spending**

<table>
<thead>
<tr>
<th>Fiscal years 1969 and 2019</th>
<th>1969</th>
<th>2019</th>
</tr>
</thead>
<tbody>
<tr>
<td>Discretionary (total)</td>
<td>64%</td>
<td>30%</td>
</tr>
<tr>
<td>Defense</td>
<td>45%</td>
<td>15%</td>
</tr>
<tr>
<td>Nondefense</td>
<td>19%</td>
<td>15%</td>
</tr>
<tr>
<td>Mandatory (total)</td>
<td>29%</td>
<td>62%</td>
</tr>
<tr>
<td>Social Security</td>
<td>15%</td>
<td>23%</td>
</tr>
<tr>
<td>Major health care programs</td>
<td>4%</td>
<td>25%</td>
</tr>
<tr>
<td>Other</td>
<td>10%</td>
<td>13%</td>
</tr>
<tr>
<td>Net Interest (total)</td>
<td>7%</td>
<td>0%</td>
</tr>
</tbody>
</table>


*Notes: "Major healthcare programs" includes Medicare, Medicaid, Children’s Health Insurance Program, and subsidies for health insurance purchases through the marketplaces established under the Affordable Care Act.*

As a matter of law, though, entitlement spending can be controlled by changing eligibility criteria or the generosity of benefits. This would require Congress to actively change the law, but as implied above, that is sometimes politically perilous. In contrast, a discretionary program, unless renewed, will automatically expire when its funding does. Discretionary spending is therefore often assumed to be easier to control than entitlement spending. But the difference should not be exaggerated: cuts in appropriations from year to year can also be highly unpopular and politically difficult. Also, it should be noted that similar concerns apply to tax expenditures—tax breaks that function much like spending programs run through the tax code.

As shown in figure 1, mandatory spending has grown as a percentage of overall spending in the last 50 years. In fiscal 1969, mandatory spending plus net interest constituted 36 percent of total spending. By fiscal 2019 the share had doubled to 70 percent. Over the same period, Social Security’s share of total spending rose from 15 percent to 23 percent. Medicare and Medicaid were created in 1965 and were responsible for a small portion of total spending throughout the rest of the 1960s. But by 2019 they and other health care
programs made up 25 percent of outlays. In contrast, defense discretionary spending fell over the same period from 45 percent of total spending in 1969 to 15 percent in 2019. The percentage of total spending devoted to nondefense discretionary programs also fell from 19 percent in 1969 to 15 percent in 2019, but this has fluctuated significantly over the period.

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Data Sources

Q. What are tax extenders?

A. Several dozen tax breaks are authorized for only a limited number of years. When these temporary provisions are scheduled to expire, they become collectively known as the “tax extenders” because lawmakers likely will consider extending most or all of them. Recently these extensions have often been retroactive, taking place well after the provisions officially expired. The temporary-but-not-temporary character of these provisions complicates tax policy and budgeting.

THE TAX EXTENDERS

Congress often enacts temporary tax provisions, almost all of which are tax cuts. Some are made temporary to force review when they’re scheduled to expire, or “sunset.” Some are temporary because Congress intended them to address temporary needs, such as recession, mortgage market collapse, or regional weather disasters. And some are temporary because proponents want them to be permanent but cannot muster the budgetary resources to offset the cost for more than a year or two at a time.

These temporary tax provisions are often known as the “expiring provisions,” because they are scheduled to expire or, in some years, already have. An important recent example were several dozen temporary tax cuts that expired at the end of 2017 and a few that expired at the end of 2018. Most reward business and consumer investments in energy efficiency and production, as well as use of alternative fuels. Other business provisions reduce taxes for auto racetracks and racehorses. The largest individual extender excludes mortgage forgiveness from income. These provisions were collectively known as the “tax extenders” because of the expectation that lawmakers will consider extending most or all of them. Lawmakers did, but not until December 2019, almost two years after many had expired.

THE 2015 DEAL ON TAX EXTENDERS

At the end of 2015, lawmakers made permanent many provisions that had previously been temporary. Those included the research and experimentation credit (which had been temporarily renewed 16 times since 1981), the “subpart F exceptions” that allow financial firms to defer tax on some international income (renewed seven times since 1998), the personal deduction for state and local sales taxes (renewed four times since 2004), and more than a dozen other expired provisions. The law also made permanent expansions of the Earned Income Tax Credit, the Child Tax Credit, and the American Opportunity Tax Credit that were scheduled to expire at the end of 2017. Originally enacted as part of the economic stimulus in 2009 and
Some Background

What are tax extenders?

extended in the fiscal cliff deal at the close of 2012, these provisions help working families with kids, encourage work, reduce marriage penalties, and help with education expenses.

The law thus made permanent many of the largest and most politically important expiring provisions. Dozens of temporary provisions remain, but tax extender deliberations have lower stakes now than several years ago.

PROVISIONS EXPIRING IN THE FUTURE

More tax provisions are scheduled to expire in coming years. The 2020 cohort of expirations includes almost three dozen provisions, including prominent tax breaks such as the Work Opportunity Tax Credit and the New Markets Tax Credit. But the most important expirations are scheduled for 2025, when key provisions of the 2017 tax bill expire. These include lower individual tax rates, the expanded Child Tax Credit, limits on the Alternative Minimum Tax, and the deduction for qualified pass-through business income.

POLICY IMPLICATIONS

Some tax provisions are temporary for good reasons. If Congress enacts tax cuts to soften the blow from disasters and recessions, it makes sense to limit their duration. Sunsetting tax breaks after several years can also inspire more congressional oversight than permanent features of the tax code may receive.

In practice, though, Congress often extends tax breaks a year or two at a time merely to meet the letter of the law governing congressional budget procedures. Budget rules often (but not always) require lawmakers to find offsetting revenue increases or spending cuts to pay for extending a tax break. Finding such offsets is easier for a temporary extension than for a permanent one.

It should be no surprise, then, that the number of expiring provisions snowballed, with more than 30 still set to expire at the end of 2020. The large number makes Congress less likely to consider their merits as individual provisions.

BUDGET IMPLICATIONS

The Congressional Budget Office must assume that these temporary-but-not-temporary laws will expire as scheduled when it compiles the budget baseline that serves as a starting point for congressional budget deliberations. Such assumptions make the baseline unrealistic, since temporary tax laws are typically extended. Moreover, because most extenders involve tax cuts, the assumption that these provisions will expire leads the Congressional Budget Office to project higher than likely revenues. There is one exception to the rule: temporary taxes whose revenue is deposited in trust funds are assumed to continue.

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Some Background

What are tax extenders?


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Q. What options would increase federal revenues?

A. Policymakers can directly increase revenues by increasing tax rates, reducing tax breaks, expanding the tax base, improving enforcement, and levying new taxes. They can indirectly increase revenues through policies that increase economic activity, income, and wealth.

Policymakers can raise revenues by modifying existing tax policy, enacting new taxes, and boosting economic activity.

MODIFYING EXISTING TAX POLICY

1. Congress could increase the tax rates that apply to personal income, corporate income, payrolls, estates, and specific products like gasoline and cigarettes. Higher rates almost always yield higher revenues, even if people and businesses do less of the taxed activity. Capital gains, which are currently taxed at a top rate of 23.8 percent, are one exception; some estimates suggest revenues may peak at rates around 30 percent but then decline at higher rates.

2. Congress could scale back or eliminate the myriad tax breaks in the existing code. Prominent personal examples include the exclusion of employer-provided health insurance, retirement saving incentives, and the exclusion of capital gains on sales of principal residences. Prominent business examples include expensing of new investments, low tax rates on overseas income, and the 20 percent deduction for qualified business income.

3. Congress could apply existing taxes more broadly. For example, it could reduce the standard deduction in the individual income tax, increase the cap on earnings subject to the Social Security payroll tax, or reduce the estate tax exemption.

4. The federal government could strengthen enforcement. The IRS estimates that the “tax gap”—the difference between taxes owed and those actually paid—averaged about $458 billion annually in 2008–10 and that enforcement efforts and penalties recovered about $52 billion. Better enforcement could further reduce the remaining $406 billion gap.

ENACTING NEW TAXES

Policymakers could also boost revenues by introducing new taxes. The largest potential revenue sources
Some Background

What options would increase federal revenues?

would be a value-added tax (already levied in every other developed nation), a carbon tax (which would target the pollutants causing climate change), or a wealth tax. Other recent proposals include taxes on financial transactions and unhealthy foods and drinks.

BOOSTING ECONOMIC ACTIVITY

All else equal, a bigger economy generates more tax revenue. Policies that boost economic activity, incomes, and wealth can thus lift revenues as well. Examples include policies that increase the number of people in the labor force, the number of hours they work, and their skills. Policymakers can also modify the tax code to increase workers’ physical and intellectual capital.

Immigration reform is one way to boost economic activity. Bringing new workers into the country would expand the labor force and attract new capital; allowing unauthorized workers to enter the legal workforce would boost their productivity and taxable wages.

Other policies that might boost economic activity include investing in infrastructure, education, and innovation; reforming the rules of social programs that discourage some people from working; and restructuring the tax code to encourage domestic investment. Actual economic gains depend on policy specifics; poorly designed investments and reforms could boomerang, reducing economic activity.

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Further Reading


What does it mean for a government program to be off-budget?

A. The two Social Security trust funds and the postal service are “off-budget”—their spending and receipts are walled off from the rest of the budget. Putting Social Security and the post office off-budget shields them from some pressures, but policymakers often focus on the unified budget that includes them. A few other agencies are excluded because of their independence (e.g., the Federal Reserve) or private character (e.g., government-sponsored, privately owned entities and funds managed for private citizens).

OFF-BUDGET VERSUS ON-BUDGET ACCOUNTING

The budget brings together the spending and receipts of virtually all federal activities, from paying doctors who treat Medicare patients to financing the Environmental Protection Agency to collecting income taxes to selling oil leases on federal land. In two cases, however, Congress has separated programs from the rest of the budget. The Postal Service Fund and the disability and retirement trust funds in Social Security are formally designated “off-budget,” even though their spending and revenues are included in the unified budget.

Lawmakers created this special accounting to try to wall off these programs. For the postal service, the intent was to free the agency to pursue more efficient practices than the conventional budget process allows. But that has not helped the postal service avoid financial difficulties.

With Social Security, the intent was to protect any surpluses from being diverted into other programs. The two Social Security trust funds have accumulated large surpluses since 1983. Those will eventually be drawn down to pay benefits. Advocates therefore argued that those surpluses should be separated from budgeting for the rest of government. Congress hoped that this separation would induce greater fiscal discipline in the rest of the government.

RESULTS

This accounting has had mixed results. Congressional budget rules prevent spending reductions or revenue increases in Social Security from being explicitly used to pay for spending increases or tax cuts elsewhere. In that sense, off-budget accounting has protected the program. But high-level budget discussions focus on the unified budget deficit and thus ignore the off-budget versus on-budget distinction. As a result, Social
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What does it mean for a government program to be off-budget?

Security surpluses have effectively helped finance deficits elsewhere in the government. Just how much is unclear, but in the almost three decades that Social Security has been off-budget, the rest of government has run a surplus in only two years (1999 and 2000).

In any case, these arguments have less relevance today. Annual Social Security expenditures have exceeded noninterest income since 2010. The combined trust funds still run surpluses through 2019 because of interest payments from the Treasury, but these payments are simply transfers from one government office to another and therefore do not affect the unified deficit. Trust fund balances may begin to decline in 2020.

THE FEDERAL RESERVE SYSTEM

The Federal Reserve System (the Fed) is part of the federal government but is explicitly excluded from the budget to shield monetary policymakers from political pressure. Other developed nations do the same. The Fed thus sets its own spending and finances itself from earnings on lending to banks and its financial assets. The Fed remits its profits to the Treasury each year, which the budget records as receipts, but the agency otherwise operates outside the budget.

OTHER ACTIVITIES OUTSIDE THE BUDGET

Some federal activities are outside the budget because the government plays a limited role in what is otherwise a private activity. The government manages various funds whose assets belong to Indian tribes, federal employees, copyright holders, and other private individuals. Spending from and receipts to those funds are generally not included in the budget.

Government-sponsored enterprises, such as the Federal Home Loan Banks, also fall outside the budget because they are privately owned and their debt does not bear the full faith and credit of the US government. However, most observers assume their close ties to the government would lead to a bailout if they got into financial trouble.

That assumption proved accurate for Fannie Mae and Freddie Mac, the giant mortgage finance enterprises. During the 2008 financial crisis, they received substantial financial assistance and were put into federal conservatorship. This has led to a dispute regarding their status. The Office of Management and Budget believes Fannie Mae and Freddie Mac are still sufficiently private to fall outside the budget. The Congressional Budget Office believes federal control is now so strong that the two entities are effectively federal agencies and their spending and receipts should be in the budget.

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Further Reading


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How did the TCJA affect the federal budget outlook?

Q. How did the TCJA affect the federal budget outlook?

A. The Tax Cuts and Jobs Act cut taxes substantially from 2018 through 2025. The resulting deficits will add $1 to $2 trillion to the federal debt, according to official estimates. The debt increase will be larger if some of TCJA’s temporary tax cuts are extended.

At the start of 2017, congressional Republicans often spoke about revenue-neutral tax reform. The revenue losses from tax cuts would be offset by rolling back tax breaks or introducing other taxes, most notably a destination-based cash flow tax—sometimes called the border-adjusted tax. The destination-based cash flow tax attracted intense opposition from business groups, especially retailers, and was eventually dropped. Lawmakers then pivoted to a combination tax cut and reform. The Tax Cuts and Jobs Act (TCJA) was the result.

ESTIMATING TCJA’S BUDGET IMPACT

The Joint Committee on Taxation and the Congressional Budget Office have published several estimates of TCJA’s expected budget impact. These estimates all show TCJA substantially reducing revenues and increasing deficits over its first decade. The specific amount varies—from about $1 trillion to $2 trillion—for three reasons.

First, the agencies estimated budget impacts using both conventional methods (which do not account for potential changes to the overall economy) and dynamic methods (which do). Second, the agencies originally estimated the budget impacts against a budget baseline established in 2017, when the act was debated and enacted. They later published updated figures using a 2018 baseline, which included new economic and budget information. Third, official scores typically do not include any new debt service costs resulting from tax cuts or spending increases. Projections for the entire budget, however, do include debt service.

CONVENTIONAL ESTIMATES

During legislative debate, the most-cited estimate was that the TCJA would increase deficits by about $1.5 trillion over 10 years. This figure comes from the Joint Committee on Taxation (JCT) and Congressional Budget Office’s (CBO’s) conventional score. JCT projected that the law would reduce revenues by $1.65 trillion from 2018 to 2027. That deficit increase would be partly offset, CBO and JCT projected, by $194 billion in reduced spending, primarily on health insurance.

In a subsequent update, CBO estimated the conventional budget effect at almost $1.9 trillion over the same period. That increase reflected an updated view of certain features of the law as well as new economic
Some Background

How did the TCJA affect the federal budget outlook?

projections.

DYNAMIC ESTIMATES

JCT’s original dynamic score found that the TCJA would boost economic activity (not growth) by an average of about 0.7 percent over the budget window. That growth would reduce the deficit impact by about $385 billion—a $451 billion boost to revenues, partly offset by $66 billion more in spending for higher interest rates. Including macroeconomic effects, TCJA would thus increase the deficit by slightly less than $1.1 trillion over a decade. CBO’s 2018 update increased that figure to about $1.4 trillion.

DEBT SERVICE COSTS

To finance TCJA’s tax cuts, the government will issue additional Treasury securities and pay additional debt service. Including that spending, the deficit effects of TCJA are larger. CBO’s 2018 update, for example, puts the conventional deficit increase from TCJA at almost $2.3 trillion over its first decade. The corresponding dynamic score is a $1.9 trillion increase.

EXPIRING PROVISIONS

To satisfy budget process requirements, lawmakers decided to sunset some provisions of the TCJA. Most cuts to individual income taxes, for example, expire at the end of 2025. Business expensing for new investment is also temporary. As conventionally scored, the act thus increased deficits from 2018 through 2026 and decreased them thereafter. If lawmakers decide to extend all the expiring provisions, however, that would add about $480 billion to deficits through 2027 and a growing amount thereafter.

LATER DECADES

The TCJA was enacted under a process known as reconciliation. Among other things, reconciliation requires that a bill not increase the deficit beyond the 10-year budget window. At the time, JCT and CBO concluded that the act satisfied that requirement on a conventional scoring basis. Indeed, they found that the law reduced deficits starting in 2027. If TCJA’s expiring provisions are eventually made permanent, however, deficits will be persistently higher.

HISTORICAL CONTEXT

Any way you slice it, the TCJA was a major tax reduction. Tax revenues will average just 16.7 percent of GDP from 2020 to 2024, according to CBO’s latest projections. That’s well below the 17.4 percent of GDP average from 1970 to 2019.

Revenues would rise to 18.0 percent of GDP by 2030 if all TCJA’s temporary provisions expire as scheduled. Revenues would be 17.5 percent of GDP if those provisions are extended.

Those revenues are far below expected spending, which CBO sees rising from 21 percent of GDP in 2020 to 23.4 percent in 2030. Absent dramatic spending cuts or revenue increases, the public debt will continue to grow faster than the economy.
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How did the TCJA affect the federal budget outlook?

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Data Sources


Further Reading


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