

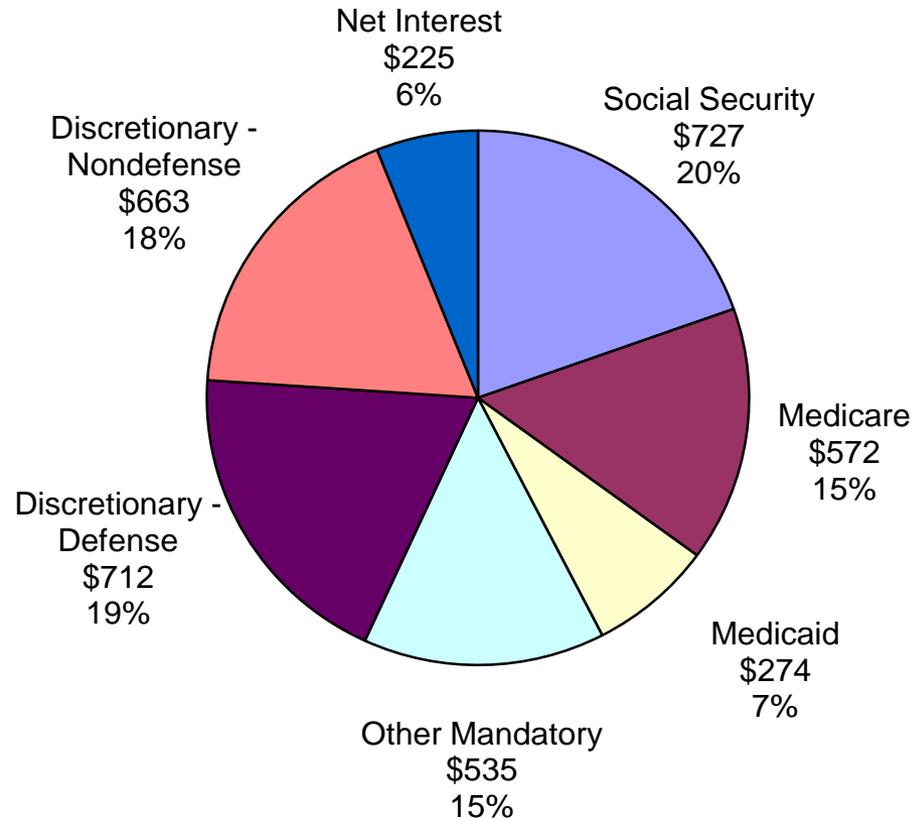


# Business Cycle Balanced Budget Amendment

Justin Amash

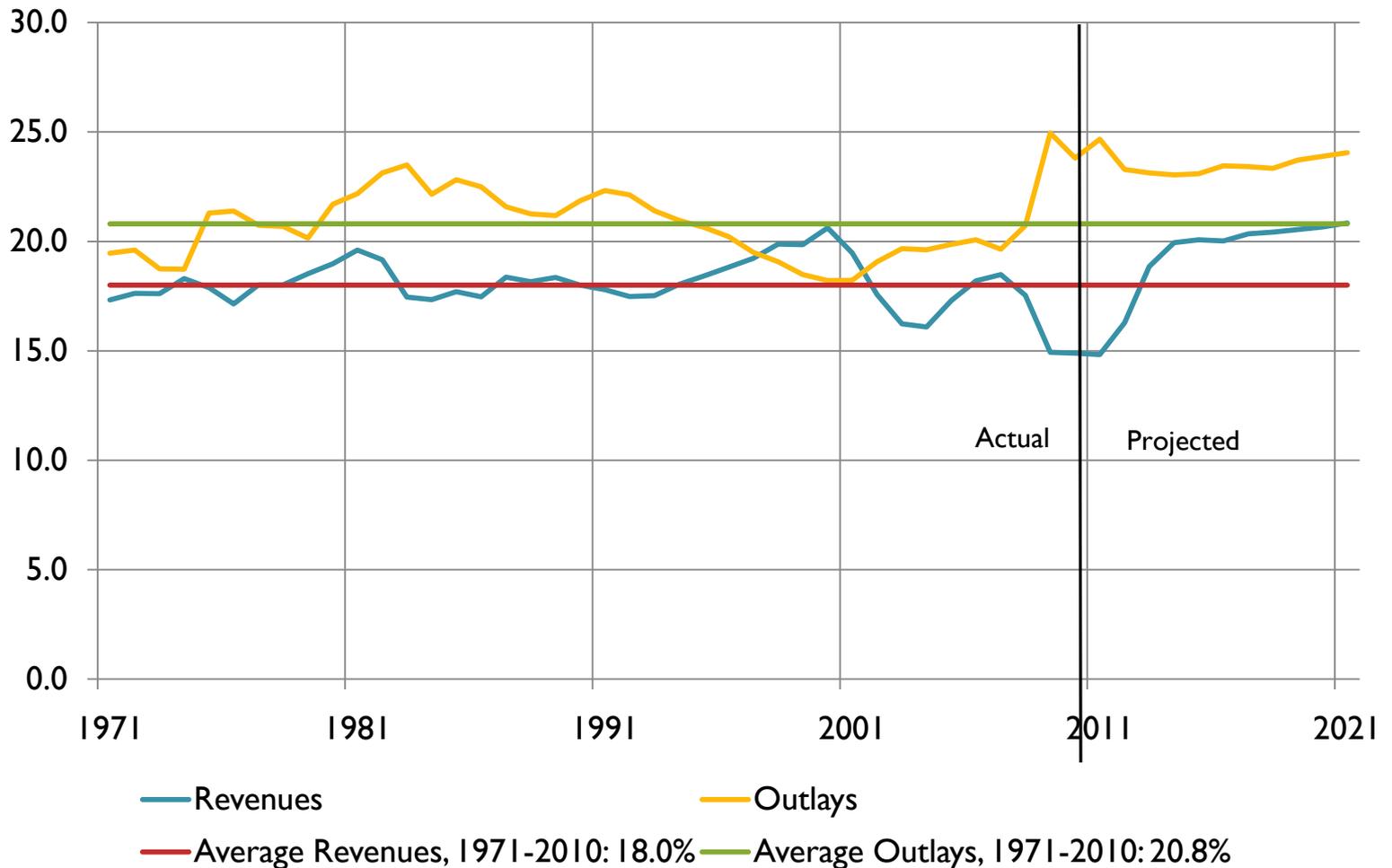
May 2011

# U.S. Spending, FY I I, \$billion



Source: CBO

# U.S. Spending & Revenue 1970-2021, % GDP

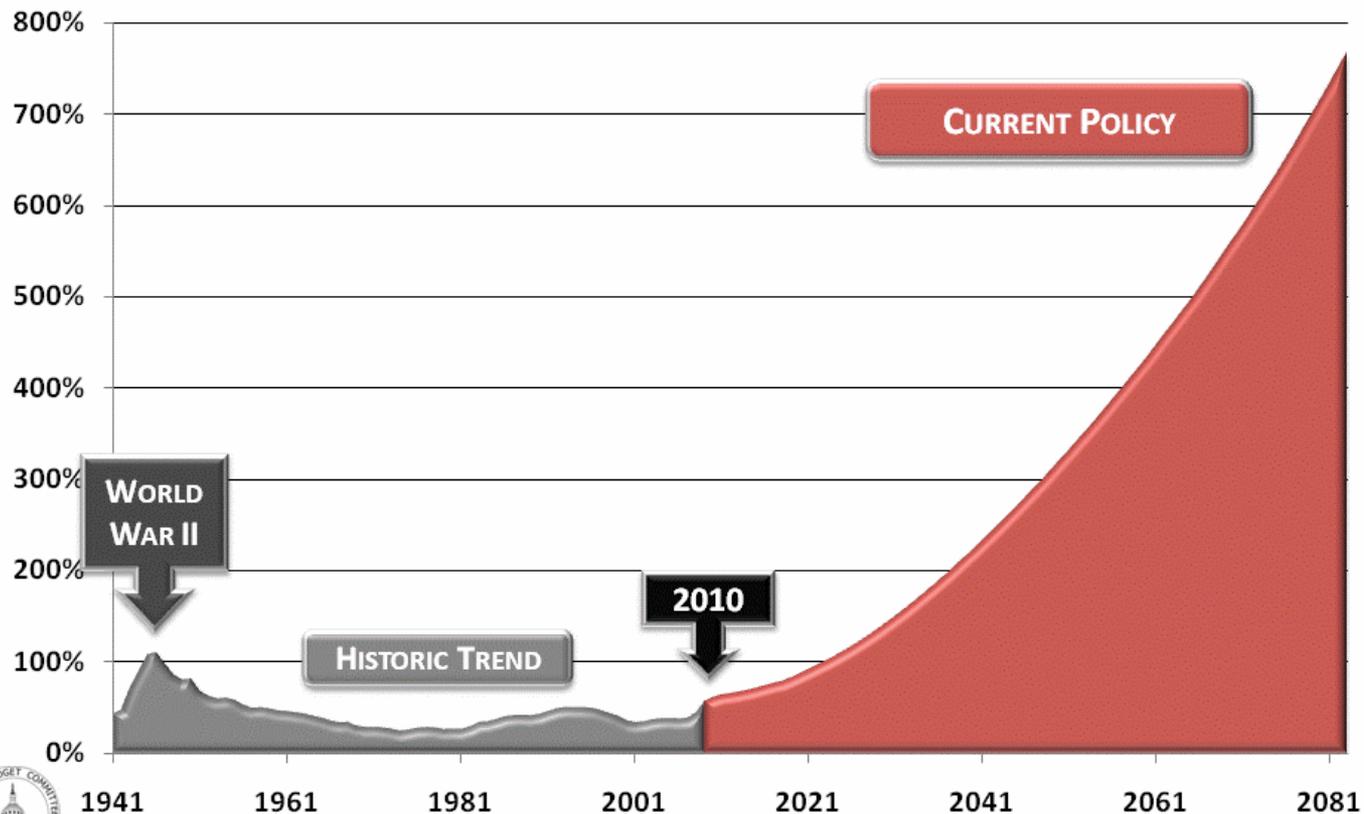


Source: CBO/OMB

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# The Long-Term Prognosis

FIGURE 4  
**THE PATH AHEAD: TIDAL WAVE OF DEBT**  
(DEBT HELD BY PUBLIC AS PERCENTAGE OF GDP)



Source: House Budget Committee

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# Principles for a Fiscal Rule

- **Simple:** easily understandable
- **Comprehensive:** include all spending and revenue
- **Responsible:** provide for current needs without burdening future generations
- **Predictable:** give policymakers and citizens time to modify plans and behavior
- **Binding:** limit policymaker discretion
- **Durable:** likely to persist over time (not be repealed)

# The Solution

- The Business Cycle Balanced Budget Amendment:
  - A responsible fiscal rule that is value neutral towards the size and scope of government
  - Ties **spending** to recent **revenue** levels (adjusted average of three prior years)
  - Allows emergency spending with 3/4 support in Congress and description of emergency
  - Phases in gradually over a decade

# Constructing the BCBBA

- i.e., FY2012 spending would equal the average of the sum of FY2009, FY2010, and FY2011 revenue
  - Adjusted for inflation & population growth
  - $FY2012 \text{ spending} = 1/3 * [(FY2009 \text{ Revenue}) * (2009-12 \text{ inf./pop. changes}) + (FY2010 \text{ Revenue}) * (2010-12 \text{ inf./pop. changes}) + (FY2011 \text{ Revenue}) * (2011-12 \text{ inf./pop. changes})]$

# Constructing the BCBBA (cont.)

Year	Inflation Rate (i)	Population Growth (pop)	Multiplier (1 + i) * (1 + pop)	Revenue	Spending Limit
2004				<b>1,880.1</b>	
2005	0.033	0.009	1.0423	<b>2,153.6</b>	
2006	0.033	0.009	1.0423	<b>2,406.9</b>	
2007	0.029	0.010	1.0393		<b>2,322.4</b>

$$\begin{aligned}
 \mathbf{\$2,322.4 B} = & 1/3 * (\mathbf{\$1,880.1 B} * 1.0423 * 1.0423 * 1.0393 + \\
 & \mathbf{\$2,153.6 B} * 1.0423 * 1.0393 + \mathbf{\$2,406.9 B} * 1.0393)
 \end{aligned}$$

# Effects of the BCBBA

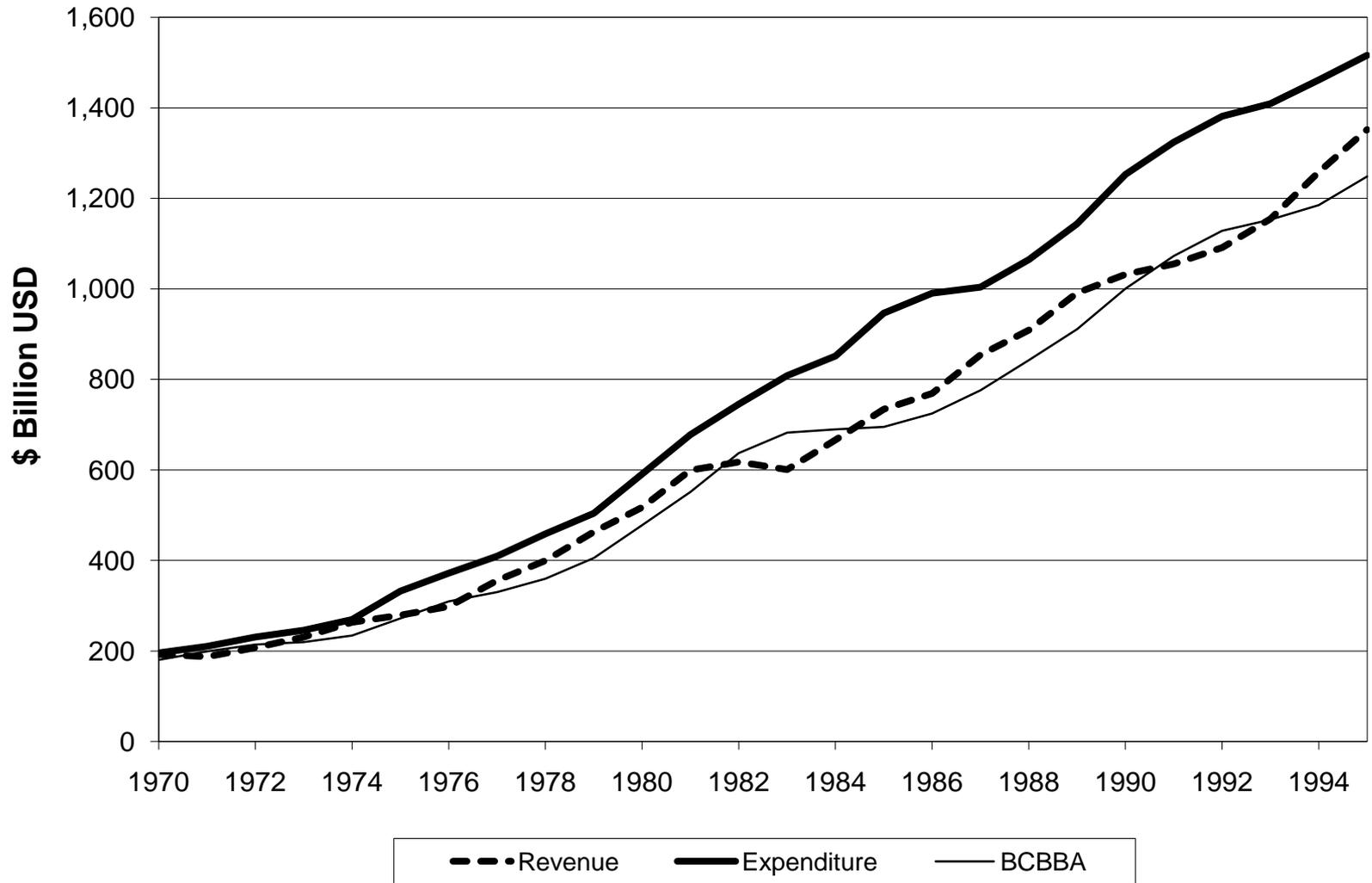
- **Countercyclical:** spending peaks during recessions, likely steady or simply slower growth rate during recovery
- **Focus on Spending:** revenue changes in a year cannot impact that year's spending
- **Surpluses over the Business Cycle**
- **Encourages Prioritization**

# U.S. Business Cycles Since 1945

Peak	Trough	Contraction (peak to trough)	Expansion (previous trough to this peak)
February 1945	October 1945	8 months	80 months
November 1948	October 1949	11 months	37 months
July 1953	May 1954	10 months	45 months
August 1957	April 1958	8 months	39 months
April 1960	February 1961	10 months	24 months
December 1969	November 1970	11 months	106 months
November 1973	March 1975	16 months	36 months
January 1980	July 1980	6 months	58 months
July 1981	November 1982	16 months	12 months
July 1990	March 1991	8 months	92 months
March 2001	November 2001	8 months	120 months
December 2007	June 2009	18 months	73 months
<b>Average, 1945-2009</b>		<b>11 months</b>	<b>59 months</b>

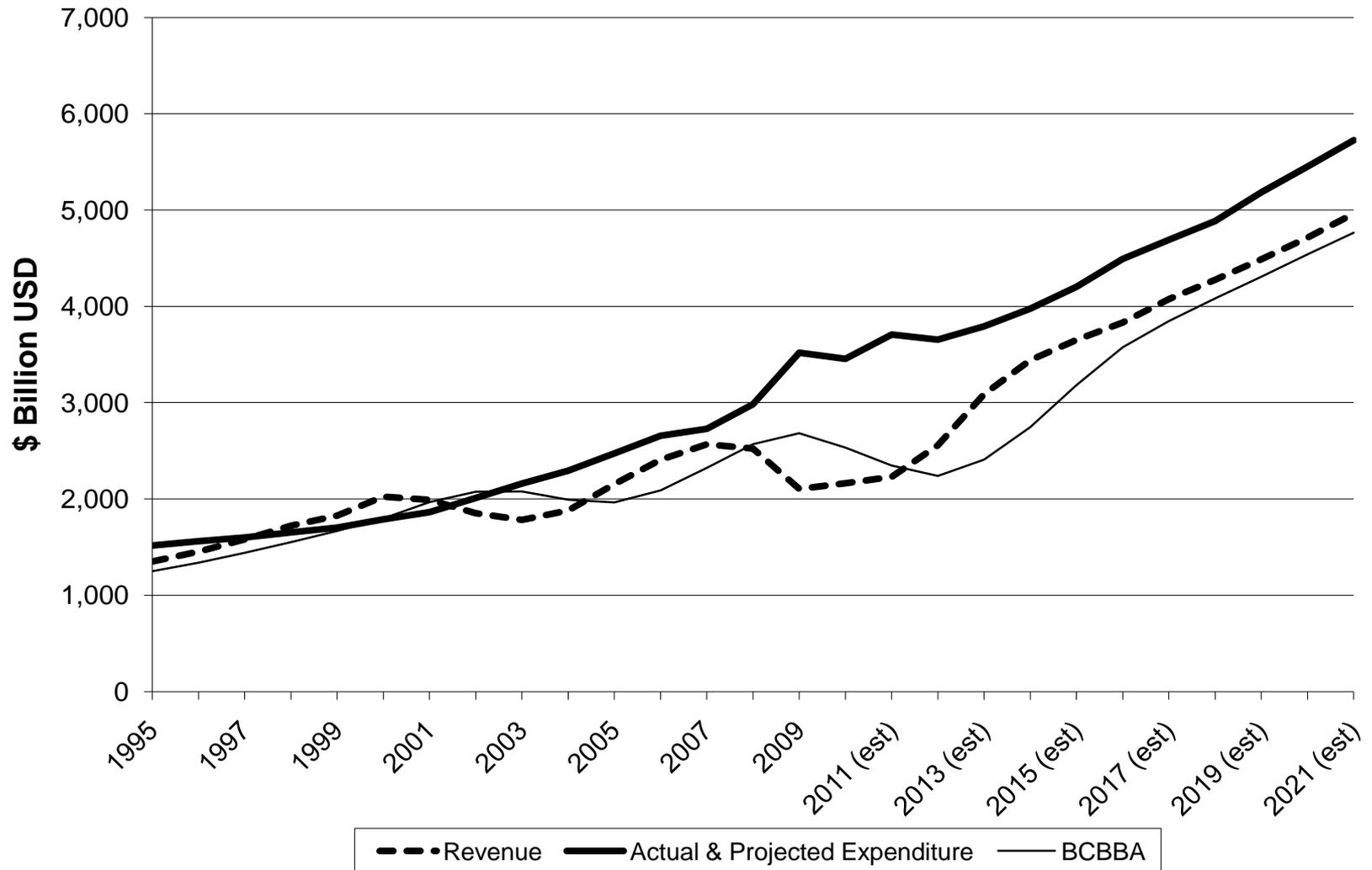
Source: NBER

# Federal Budget Scenarios, 1970-1995



Source: OMB, staff calculations

# Federal Budget Scenarios, 1995-2021



Source: OMB, staff calculations

# Responding to Emergencies

- Other proposals: rules set aside during military conflict
  - No fiscal restraint: how often has the U.S. not had troops in harm's way abroad?
  - May encourage small scale operations for fiscal reasons
- Better alternative: consensus-driven supermajority

# Broad-based Emergency Provision

- National emergencies can take many forms
  - War
  - Natural disaster (i.e., floods, hurricanes, earthquakes, tsunamis, asteroid impacts?)
  - Manmade disaster (i.e., terrorist attacks, nuclear accidents)
  - Economic crises

# Consensus on Emergencies

- Emergency spending should reflect consensus
  - That an emergency exists,
  - What the nature of the emergency is,
  - That specific outlays are necessary to respond appropriately, and
  - That such funding does not include appropriations for non-emergency items

# High Supermajority Required

- Normal process: no check to overspending
- Need balance between
  - Fiscal responsibility
  - Responding to emergency situations
- Why three-fourths?
  - Congress has always approved response to national emergencies by much higher proportions whenever the remedy was broadly supported
  - Not high enough to allow small groups to extract concessions by strategic blocking

# Crisis Votes in American History

		House*	Senate
Declaration of War: World War I	1917	86.9%	92.1%
Pre-WWII Appropriations	1940	91.2%	83.3%
WWII Declaration of War: Germany	1941	91.4%	92.6%
WWII Declaration of War: Italy	1941	92.8%	94.7%
WWII Declaration of War: Japan	1941	90.2%	86.3%
Cuban Missile Crisis Resolution Authorizing Force	1962	88.3%	86.0%
Gulf of Tonkin Resolution	1965	97.2%	88.0%
Operation Desert Shield Appropriations	1990	88.2%	Unanimous Consent
Authorization for Use of Military Force against Iraq	1991	<b>57.5%</b>	Unanimous Consent
Y2K Preparation	1999	92.9%	81.0%
Defense and Emergency Appropriations, FY 2002	2001	94.0%	94.0%
9/11 Response Supplemental Appropriations	2001	97.9%	Unanimous Consent
9/11 Authorization of Military Force	2001	Unanimous Consent	98.0%
Supplemental Appropriations, FY 2002	2002	91.5%	92.0%
Authorization for Use of Military Force in Iraq	2002	<b>68.5%</b>	77.0%
Defense Appropriations, FY 2003	2002	94.9%	93.0%
Defense Appropriations, FY 2004	2003	93.8%	95.0%
Supplemental Appropriations, FY 2003	2003	Voice Vote	Unanimous Consent
Supplemental Appropriations, FY 2004	2003	<b>68.7%</b>	Voice Vote
Defense Appropriations, FY 2005	2004	94.5%	96.0%
Defense and Emergency Appropriations, FY 2006	2005	<b>71.0%</b>	93.0%
Hurricane Katrina Response	2005	Voice Vote	Unanimous Consent
Hurricane Katrina Supplemental Appropriations	2005	94.7%	97.0%
Supplemental Appropriations, FY 2007	2006	85.0%	100.0%
Supplemental Appropriations, FY 2006	2006	81.3%	98.0%
Defense Appropriations, FY 2007	2006	91.2%	100.0%
Defense Appropriations, FY 2008	2007	92.6%	Voice Vote
Supplemental Appropriations, FY 2008	2007	95.6%	92.0%
Bush 2008 Stimulus Bill	2008	88.4%	81.0%
Emergency Economic Stabilization Act of 2008 (TARP)	2008	<b>60.6%</b>	<b>74.0%</b>
Defense Appropriations, FY 2010	2009	91.0%	88.0%
Supplemental Appropriations Act, 2009	2009	<b>52.1%</b>	91.9%
American Recovery and Reinvestment Act of 2009 (Obama's Stimulus)	2009	<b>56.8%</b>	<b>60.6%</b>

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\*Committee of the Whole, not those voting "yea" or "nay"

# A Gradual Transition

- Ten-year transition
- Closes the gap by at least one-tenth each year of the ratification year difference between outlays and the limit
- Formula-based to lock in progress
- Does not prevent faster adjustment

# Mechanics of the Transition

- Balance reached through declining fractions
- Spending =  $G_{t-1} * (10-Y)/(11-Y)$ , where
  - $G_{t-1}$  = gap b/n actual spending and BCBBA rule in prior year
  - Y = year subsequent to ratification
- For example, in the first year after ratification, the prior year's gap would be multiplied by  $(10-1)/(11-1) = 9/10$  to obtain that year's transitional spending level

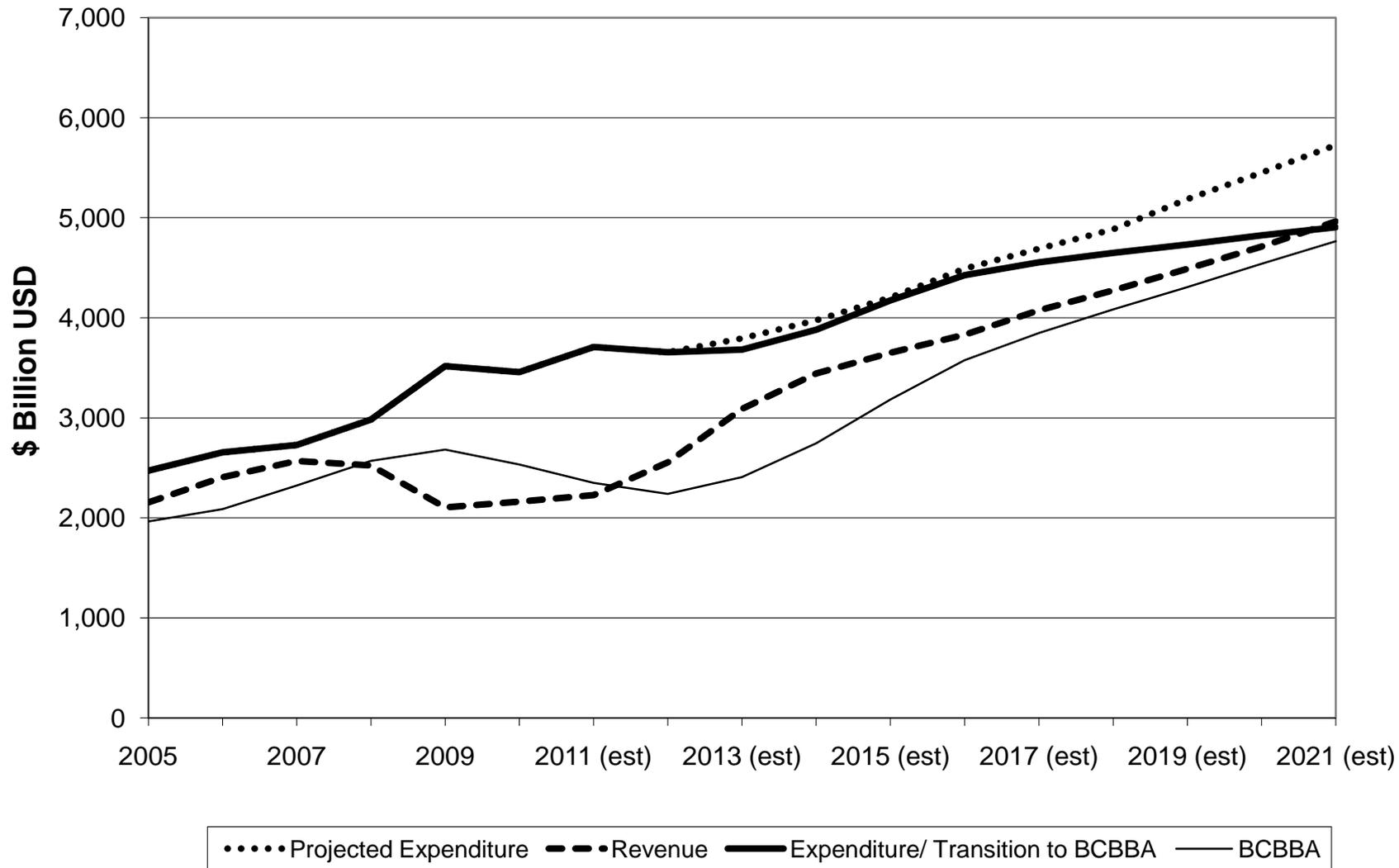
## Mechanics of the Transition (cont.)

- Simple result: smooth transition from gap at ratification to balance
- Year 1: **9/10**
- Year 2:  $(9/10)*8/9 = 8/10$
- Year 3:  $(9/10*8/9)*7/8 = 7/10$
- Year 4:  $(9/10*8/9*7/8)*6/7 = 6/10$
- And so on

# Mechanics of the Transition (cont.)

Year	Gap relative to prior year	Amount above rule, starting at \$1.2 trillion	Gap Reduced	Fiscal Balance
0 (ratification)	n/a    x	\$1,200 B	n/a	-\$1,000 B
1	9/10    =	\$1,080 B	\$120 B	-\$880 B
2	8/9	\$960 B	\$120 B	-\$760 B
3	7/8	\$840 B	\$120 B	-\$640 B
4	6/7	\$720 B	\$120 B	-\$520 B
5	5/6	\$600 B	\$120 B	-\$400 B
6	4/5	\$480 B	\$120 B	-\$280 B
7	3/4	\$360 B	\$120 B	-\$160 B
8	2/3	\$240 B	\$120 B	-\$40 B
9	1/2	\$120 B	\$120 B	\$80 B
10	0	\$0	\$120 B	\$200 B

# Transition to the BCBBA



# Items Not Included

- **Supermajority to raise taxes**
  - Delay = disincentive
  - Politically non-starter
- **GDP-based spending limit**
  - Would lock in size of federal government at levels desired neither by liberals nor conservatives
  - Politically non-starter
- **Supermajority to increase debt limit**
  - Not needed: when in force, surpluses over the business cycle keep debt from rising

# Options for Implementing Legislation

- Define: population growth, inflation, emergency
- Enforcement: spending sequester, tax increase trigger, some combination, or other?
- Budget process: revamp of 1974 Congressional Budget Act, including process, points of order, reconciliation, budget projection horizons, etc.
- Prohibition on and remedy for debt issued except in compliance with the amendment
- Restrictions on judicial review
- Structure of a reserve fund when debt is eliminated

# Conclusion

- Spending tied to average of three prior years of revenue, adjusted for population growth and inflation
- Emergency exemption: 3/4 of both Houses of Congress
- Gradual, 10-year transition
- Provides framework for addressing fiscal challenges without limiting Congress' options to comply
- Support the Business Cycle Balanced Budget Amendment