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Some advice to President Clinton: Develop a long-run balanced budget law

[Colander, David](#), [Daane, Dewey](#). **Challenge**. Armonk: [May/Jun 1993](#). Vol. **36**, Iss. **3**; pg. **51**, 2 pgs

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Abstract (Document Summary)

The US public is ready to deal with the deficit issue. President Clinton's first order of business should be to design a credible plan to deal with the deficit. A long-run balanced budget law is proposed stating that all current deficits must be explicitly financed by future spending cuts or increased taxes.

Full Text (1174 words)

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When Louis XIV's finance minister was asked what to do about the deficit, he responded, "Nothing, it's too serious." Now that the election is over, we can only hope that President Clinton will not follow that approach. Perot's legions made one thing abundantly clear--the American people are ready to deal with the deficit issue. Our present dilemma is how to deal with it. The President's first order of business should be to design a credible plan to deal with the deficit.

The Clinton plan that seems to be emerging--to deal with the deficit eventually--is unacceptable. The public has seen the "eventual approach" in the past and, somehow, the "eventually" never comes. If we are to deal with the deficit, we need an institutional change which makes Congress deal with "eventually" now. That is what we're proposing. The new Congress should pass a long-run balanced budget law as its first order of business. That law would state simply: All current deficits must be explicitly financed by future spending cuts or increased taxes.

Despite its simplicity, this is no small change. The long-run balanced budget law will not allow Congress to pretend that there is such a thing as a costless tax cut or spending increase. The economic reality is that cutting taxes or increasing spending now creates a deficit now; that deficit must be financed immediately by borrowing and should eventually be financed through higher taxes or lower spending. But, under current budgeting procedures, Congress keeps putting "eventually" off (pretending it will never come), and continues to avoid dealing explicitly with the future implications of the deficit.

Congress would be restrained from persisting in this practice under the long-run balanced budget law; it would have to deal immediately with what will happen eventually. The law would require that, if the budget includes a deficit, Congress must pass legislation to lower-future spending or raise future taxes. The "eventually" must be dealt with now.

For example, if Congress began to run a current \$300 billion deficit, the law would require Congress to pass legislation now so that the addition to our total debt would be specifically offset in the future. They would find it necessary either to cut future spending or increase future taxes in order to match the deficit. Under the long-run balanced budget law, Congress could choose how to deal with the long-run implications; it could not avoid dealing explicitly with them.

In one scenario, the law would permit a short-run stimulus package in fiscal year 1993 (such as an investment tax credit), if that stimulus was simultaneously offset by a mandated reduction in spending or an increase in taxes in future years.

CHANGING THE POLITICAL DYNAMICS

While at first glance it might seem to be tilting at windmills (particularly in the light of Gramm-Rudman), it is quite different under closer examination. Gramm-Rudman did not change "eventually" into now. It left Congress the option of retreat--which they used. The long-run balanced budget law eliminates the escape hatch. Because it forces Congress to deal explicitly with the long-run implications of budget deficits, the law will fundamentally change the dynamics of the political debate. Politically, much of the thrill of policies--such as a middle-class tax cut or infrastructure spending--disappear when long-run modifiers are added to them. "A tax cut now, but higher future taxes" isn't going to sell on Main Street.

Since the long-run balanced budget law allows backloading of tax increases and frontloading of spending increases, it gives much more flexibility to politicians than does a balanced budget law such as Gramm-Rudman. But it is far stronger, and changes the political dynamics in a far more important way than did previous attempts. It forces politicians to deal explicitly with the future implications of their current decisions.

ITS FOCUS WITHIN ECONOMIC THEORY

Our proposed law is not novel; it is simply an attempt to build explicit recognition of the one immutable law of economics into the the political decision-making process, namely, the TANSTAAFL (There Ain't No Such Thing As A Free Lunch) law. Previous attempts at balanced budget laws have not been consistent with this law; they caused budget deficits to seem like the problem. But current budget deficits are not necessarily the problem if they do not lead to an overextended government financial system in the long-run. Deficits are a problem now precisely because they are leading to such an overextended system.

That's why it is so important to make specific plans for the long-run financing of deficits. As long as these plans are made, many of the problems posed by current deficits are eliminated. The TANSTAAFL law is a long-run, not a short-run, law.

THE IMPLICATIONS OF ECONOMIC GROWTH

The technical implications of the TANSTAAFL law depend on an economy's rate of growth. A growing economy can handle an ongoing deficit; moreover, since tax revenues increase with income, high growth rates can lead to expected future budget surpluses which can be used to offset current deficits. If one predicts a sufficiently high real growth rate, any deficit can be made to seem consistent with the TANSTAAFL law; but that's not an acceptable approach. Claims of high future growth rates do not reassure the markets and should not be used to circumnavigate the discipline of economics' immutable law.

It is important that all technical adjustments to the long-run balanced budget law be determined outside the political process in order to counter the tendency to rely on future growth to make up for our current failings. One reasonable approach would be to base all future estimates of growth on some average of past growth rates.

THE POLITICAL CHOICES

Clearly, the long-run budget law is not the total answer to our country's economic woes. It will not solve the problems of the budget deficit in and of itself, but it will create an institutional structure that forces us to face the real issues posed by the deficit. It will coerce government and the American people to see the difficult choices we must make more clearly.

We are not sure which political options would be chosen concerning taxes and spending if the long-run balanced budget law were enacted. We suspect that society's choices might well be different than their current ones. For example, Social Security is the one inviolate program of Congress now. The conventional wisdom is that under no circumstances does society want to touch this program. Once the people are faced with the enormously high future tax rates that our current fiscal decisions implicitly require, their view about Social Security might change. Society may well choose to trade off a higher retirement age in, say, 2010, for an improved health-care system now.

Economic theory doesn't proclaim which choices society should make, but it does say that society must make choices. The TANSTAAFL law cannot be avoided in the long run. If the United States tries to hide from that law much longer, in a hundred years, President Clinton will be joining Louis XIV as another historical example of what happens when a leader tries to do so.

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