Congressional Budget Office

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Answers to Questions for the Record Following a Hearing on the Budget and Economic Outlook for 2015 to 2025 Conducted by the House Committee on the Budget

On January 27, 2015, the House Committee on the Budget convened a hearing at which Douglas W. Elmendorf, Director of the Congressional Budget Office, testified about CBO's report The Budget and Economic Outlook: 2015 to 2025 (January 2015), *www.cbo.gov/publication/49892. Following that hearing, Chairman Price and other Members of the Committee submitted questions for the record. This document provides CBO's answers.*

Chairman Price

Question. CBO indicates in its report somewhat slowed per beneficiary spending in the short term. Yet, we know that demographics in our country have not changed: 10,000 baby-boomers are aging into the Medicare program every day. Does this temporarily slowed rate demonstrate that the current Medicare program is now sustainable? Has anything fundamentally changed the projections that the Medicare trust fund would be exhausted, as the Medicare Trustees project, in 2030?

Answer. CBO's projections of Medicare spending are subject to a considerable degree of uncertainty. A particular challenge currently is assessing the extent to which the recent slowdown in the growth of health care spending can be attributed to temporary factors such as the recession or, instead, to more enduring developments. Studies have generally concluded that some of the observed reduction in growth cannot be linked directly to the weak economy, although they differ considerably in their assessment of the relative importance of other factors. In August 2013, CBO released a paper that reviewed the observed slowdown in growth in Medicare spending between the 2000–2005 period and the 2007–2010 period.[1] That review suggests that demand for health care by Medicare beneficiaries was not measurably diminished by the financial turmoil and recession and that, instead, much of the slowdown in spending growth was caused by other factors affecting beneficiaries' demand for care and by changes in providers' behavior.

Accordingly, over the past several years, CBO has substantially reduced its 10-year and long-term projections of spending per person for Medicare. For example, over the past 5 years CBO has reduced its projection of Medicare outlays (net of premiums paid by beneficiaries

1. Michael Levine and Melinda Buntin, *Why Has Growth in Spending for Medicare Fee-for-Service Slowed?* Working Paper 2013-06 (Congressional Budget Office, August 2013), www.cbo.gov/publication/44513.

and other offsetting receipts) in 2020 by about $120 billion, or about 14 percent, reflecting that slowdown. (That amount excludes revisions made in response to legislative action and to the economic outlook.) CBO projects that slower rates of growth will persist for some years to come, although the rate of growth in spending per person is expected to rebound somewhat from its recent very low level.

Part of that reduction in projected Medicare outlays reflects a reduction in projected expenditures from Medicare's Hospital Insurance (Part A) trust fund. However, CBO also anticipates that the income flowing into that trust fund in future years will be less than what the agency had previously projected because of lower payroll tax revenue. As a result, between August 2010 and March 2015, CBO revised its projection of that trust fund's balance at the end of 2020 by only a small amount—from $195 billion to $232 billion.

In CBO's March 2015 projection, annual expenditures from the trust fund are projected to exceed noninterest income by amounts that will increase over time. Even including interest receipts, the trust fund is expected to run deficits in most of the next 10 years. By 2025, CBO projects, the annual deficit will reach $40 billion and the fund's balance will fall to $124 billion.[2] CBO has not recently projected the fund's balance beyond the 10-year period spanned by the baseline, but it is likely that such projections would show the fund continuing to incur deficits in subsequent years. CBO anticipates that, if current laws remained in place, the fund's balance would probably be exhausted early in the decade after 2025.

Question. CBO's Medicare spending projections assume physician payments are cut 21 percent in April 2015. How much higher would net Medicare outlays be if Congress does what it always does and stops the cut?

Answer. Spending for Medicare is constrained by a rate-setting system—called the sustainable growth rate—for the fees that physicians receive for their services. If the system is allowed to operate as currently structured, physicians' fees will be reduced by about 21 percent in April 2015 and will both increase and decrease by small amounts in subsequent years, CBO projects. If, instead, lawmakers overrode those scheduled reductions—as they have every year since 2003—spending on Medicare might be greater than the amounts projected in CBO's baseline. For example, using CBO's March 2015 baseline projections, holding payment rates through 2025 at current levels would raise outlays for Medicare (net of premiums paid by beneficiaries) by $6 billion in 2015 and by $136 billion (or nearly 2 percent) between 2016 and 2025.[3] The net effects of such a change in payment rates for physicians on spending for Medicare and on the deficit would depend on whether lawmakers offset the effects of the change, as they often have done in the past, with other changes to reduce deficits.

Question. What is CBO's projected penalty on individuals for the 2015 tax-filing season due to the enforcement of the individual mandate and the clawback of subsidy overpayments?

2. Congressional Budget Office, "Congressional Budget Office's March 2015 Medicare Baseline" (March 2015), www.cbo.gov/publication/44205.

3. Congressional Budget Office, "Budget Data and Projections" (supplemental material for *Updated Budget Projections: 2015 to 2025*, March 2015), www.cbo.gov/publication/45069.

Answer. Under the Affordable Care Act (ACA), most citizens of the United States and lawfully present noncitizens are required to obtain health insurance or pay a penalty. People who are subject to that requirement and do not obtain coverage owe the greater of two amounts: a flat dollar penalty per uninsured adult in a family, which was $95 in 2014 and will rise to $695 in 2016 and be indexed to inflation thereafter (the penalty for an uninsured child is half the amount for an uninsured adult, and an overall cap applies to family payments); or a percentage of a household's adjusted gross income in excess of the income threshold for mandatory tax-filing—a share that was 1.0 percent in 2014 and will rise to 2.5 percent in 2016 and subsequent years (also subject to a cap). CBO and the staff of the Joint Committee on Taxation (JCT) estimate that, in 2015, individuals will pay a total of $2 billion in penalties for not obtaining health insurance; those payments will primarily reflect penalties for not obtaining insurance in 2014.[4]

CBO and JCT also expect that, given the information on the tax returns they file this year, some people will owe more in taxes in 2015 than they would have otherwise because they received larger subsidies in 2014 than was appropriate. That clawback of subsidy overpayments is reflected in CBO and JCT's estimate of exchange subsidies in 2015, but it is not identified separately as part of the analysis.

Question. CBO updates its baseline throughout the year to reflect binding, final actions, including, for instance, Supreme Court rulings. How quickly does that happen? Against what baseline would actions related to the ruling be scored?

Answer. CBO usually publishes three sets of baseline projections each year (in the winter, spring, and summer), all of which are released publicly. In general, for the year following the publication of the spring baseline, CBO estimates the costs of legislation relative to that baseline. During that year, new legislation, actions by the Administration, Supreme Court rulings, or new information concerning individual programs can sometimes necessitate changes in the baseline projections. Because the effects of any subsequent legislation would ordinarily be measured relative to a baseline that took such changes into account, CBO incorporates them as quickly as possible. Some of those changes are complicated, however, and revisions to the baseline can take some time. For example, after the Supreme Court issued its decision about the health insurance coverage provisions of the Affordable Care Act on June 28, 2012, it took CBO and JCT about one month to update their estimates of the budgetary effects of those provisions. The amount of time required to produce an update depends mainly on the complexity of the issues involved; revisions to the baseline could take more or less than a month.

Question. The reality of the Medicaid program is one of limited access and incredible pressure on state budgets. Instead of fixing this critical safety net program, the President relies on enrolling millions more Americans into this broken program. What are CBO's updated projections on enrollment in the Medicaid expansion contained in the President's health care law?

4. That amount is shown in the row labeled "Penalty Payments by Uninsured People" in Table 1 of the following: Congressional Budget Office, "Effects of the Affordable Care Act on Health Insurance Coverage—Baseline Projections" (supplemental material for *Updated Budget Projections: 2015 to 2025*, March 2015), www.cbo.gov/publication/43900.

Answer. In calendar year 2014, according to CBO and JCT's estimates, 6 million people who were newly eligible for Medicaid under the ACA enrolled in the program. In addition, an estimated 2 million people who were eligible for Medicaid and the Children's Health Insurance Program (CHIP) under previous law—but who would not have participated in the absence of the ACA—chose to enroll as a result of the ACA. Therefore, according to those estimates, enrollment in Medicaid and CHIP in 2014 increased by a total of 8 million people, on average, during the year, compared with the number who would have been enrolled in the absence of the law. Over the coming years, the increase in the number of people enrolled in Medicaid or CHIP because of the ACA is expected to be even larger—about 10 million in 2015 and 12 million to 14 million in each year between 2016 and 2025, according to CBO's March 2015 baseline projections.[5]

Question. CBO and JCT have reduced their estimate of average enrollment in the exchanges over the course of 2015 by 1 million people, from 13 million to 12 million. For 2016, CBO and JCT revised their estimate of average enrollment through exchanges from 24 million to 21 million. Further still, for most years after 2016, CBO and JCT estimate that enrollment through exchanges will be 1 million lower than previously thought. What could this large change mean for the health of the risk pool?

Answer. The health of enrollees is one factor that affects the premiums charged for health insurance obtained through the exchanges. When the exchanges were first established in 2014, the problems related to the enrollment process probably deterred healthier people from enrolling slightly more than they deterred less healthy people. However, CBO and JCT expect that small differences in enrollment for 2015 and beyond will not affect the average health of the enrolled population noticeably. Thus, the agencies expect that their recent revisions to projections of enrollment in the exchanges have not been associated with any appreciable change in the expected average health of enrollees.

Congresswoman Blackburn

Question. The President has failed to act on the Keystone XL pipeline permit application for over six years. How many U.S. jobs did the State Department estimate that construction of the Keystone XL pipeline would create? How much money would it add to the U.S. economy over the next ten years? Is it fair to say then that a five billion dollar infrastructure project funded solely with private sector capital would have a positive effect on the federal budget?

Answer. The State Department has estimated that the Keystone XL pipeline would support about 42,000 jobs during construction and generate about 50 jobs once the pipeline became operable.[6] CBO has not evaluated that estimate nor has it separately analyzed the potential effects of the project on the U.S. economy.

In general, the federal government could increase employment and output—and also reduce federal budget deficits—during the next few years by hastening or relaxing the approval

5. Congressional Budget Office, "Effects of the Affordable Care Act on Health Insurance Coverage—Baseline Projections" (supplemental material for *Updated Budget Projections: 2015 to 2025*, March 2015), Table 2, www.cbo.gov/publication/43900.

6. Department of State, *Final Supplemental Environmental Impact Statement for the Keystone XL Project* (January 2014), http://keystonepipeline-xl.state.gov/finalseis/.

process for energy projects or by expanding opportunities to develop resources on public lands. However, the short-term effects of such changes would probably be small relative to the size of the overall economy for several reasons. First, state and local governments strongly influence the siting of energy facilities within their boundaries, and the federal government does not control the actions of those governments. Second, even if additional projects were approved in the next few years, many of them would not commence in earnest for several more years. Finally, energy production accounts for only a small percentage of overall output, so incremental gains in that sector would have only a modest effect on the economy as a whole.

In CBO's cost estimate for the Keystone XL Pipeline Approval Act, the agency reported that authorizing a private entity to construct, connect, operate, and maintain the proposed pipeline and related cross-border facilities described in the existing application would have no significant effect on the federal budget.[7] The potential effects on the U.S. economy of building the Keystone XL pipeline were not incorporated in that cost estimate, following the long-standing convention of not incorporating macroeconomic effects in cost estimates. Except for a few estimates for comprehensive immigration legislation, which would have substantially increased the U.S. labor force, cost estimates produced by CBO and JCT have reflected the assumption that macroeconomic variables such as gross domestic product (GDP) and employment remain fixed at the values they are projected to reach under current law.

Congressman Grothman

Question. During your testimony, you talked about the economic benefits of government spending. Please let me know what effect the following government spending bills could have on economic growth both in the short-term and the long-term? $60 billion in government spending to hire construction workers to dig ditches, funded by estate tax increases and a repatriation tax holiday to offset the new spending? $60 billion in government spending to build recreational bike paths, funded by estate tax increases and a repatriation tax holiday to offset the new spending? $60 billion in government spending to rebuild aging bridges, funded by estate tax increases and a repatriation tax holiday to offset the new spending?

Answer. The effects on the economy of specific types of government spending on infrastructure and specific types of tax increases are complex and difficult to assess. Over the long run, the effects on GDP of policies that combined additional infrastructure spending with changes in tax law and that had no net effect on the deficit in any given year would depend primarily upon two factors: the effects of the infrastructure spending on productivity, and the effects of the tax policies on incentives to work, save, and invest domestically. CBO has not analyzed the specific combinations of policies that you inquired about.

Question. Can you please provide additional information on how Fair Value Accounting would affect federal student loans? Can you provide details how the federal budget process would be affected and how taxpayers would be affected by switching to Fair Value Accounting?

7. Congressional Budget Office, cost estimate for the Keystone XL Pipeline Approval Act (January 12, 2015), www.cbo.gov/publication/49893.

Answer. The accounting method that CBO uses to provide its official estimates of the costs of federal credit programs is prescribed by the Federal Credit Reform Act of 1990 (FCRA). That legislation requires such costs to be measured by discounting expected future cash flows associated with a loan or loan guarantee to a present value at the time of disbursement. The discount rate used for FCRA estimates is tied to Treasury securities rather than to market rates. Thus, although the FCRA methodology accounts for expected losses from defaults, it does not account for the fact that losses from defaults tend to be highest when economic and financial conditions are poor, which is when resources are scarcer and hence more valuable.

Fair-value accounting differs in that it recognizes such market risk—the component of financial risk that remains even after investors have diversified their portfolios as much as possible and that arises from shifts in current and expected macroeconomic conditions—as a cost to the government. To incorporate the cost of such risk, present values in fair-value accounting are calculated using market-based discount rates. Thus, fair-value estimates generally imply larger costs to the government for issuing or guaranteeing a loan than do FCRA-based estimates.[8]

Last year, CBO found that if fair-value procedures had been used to estimate the cost of all credit programs in 2014, the total deficit would have been estimated to be about $50 billion greater than the deficit as measured using current procedures.[9] Much of the difference derived from the valuation of student loans: Under FCRA procedures, those loans generate very large budgetary savings per dollar lent compared with other federal credit assistance; under the fair-value approach, most of those savings disappear. CBO's most recent estimates of the cost of student loans on a fair-value basis were made last year using the agency's April 2014 baseline. At that time, CBO projected that student loans issued between 2015 and 2024 would cost $88 billion on a fair-value basis, as contrasted with the savings of $135 billion projected under FCRA accounting.[10]

Switching from a FCRA approach to a fair-value approach to recording costs in the federal budget without making any changes to credit programs themselves would not affect the terms under which credit was made available, the risks borne by the government, or the costs for users of loan and loan guarantee programs. The switch would only affect the way in which those costs and risks are recorded in the budget. However, the use of fair-value accounting could affect Congressional decisions about the volume of loans to be made or guaranteed, the fees charged to borrowers, or other terms associated with any new loans or loan guarantees—perhaps to reduce estimated budgetary costs. Without an adjustment to the caps on discretionary funding, appropriations for other programs might have to be reduced to make up for the higher budgetary costs of credit programs. Further, if a FCRA approach was replaced by a fair-value approach for a purpose other than recording costs in the federal budget—such as part of a requirement that fees on loans to small businesses be set so that those loans would have no cost on a fair-value basis—then costs for users of some programs would be increased.

8. Congressional Budget Office, *Fair-Value Accounting for Federal Credit Programs* (March 2012), www.cbo.gov/publication/43027.

9. Congressional Budget Office, cost estimate for H.R. 1872, the Budget and Accounting Transparency Act of 2014 (February 12, 2014), www.cbo.gov/publication/45109.

10. Congressional Budget Office, *Fair-Value Estimates of the Cost of Selected Federal Credit Programs for 2015 to 2024* (May 2014), www.cbo.gov/publication/45383.

Question. Using the average interest rates from 1980 to 2000 to service government debt, how would the interest owed on the national debt change from interest rates used today? How would it affect today's budget deficit?

Answer. Movements in interest rates affect the budget mostly by changing the amount the federal government pays in interest on debt held by the public. Although interest rates are currently at historic lows, CBO projects that they will rise over the next few years and return to levels closer to their long-run average, with adjustments for inflation. As a result, interest payments on federal debt held by the public will rise substantially, CBO expects.

If interest rates on all types of Treasury securities were 1 percentage point higher each year through 2025 than is projected in the baseline and all other economic variables including inflation were unchanged, the government's interest costs would be substantially larger, increasing by nearly $1.7 trillion over the 2016–2025 period.[11] By 2025, according to CBO's estimates, such higher interest rates would boost the federal budget deficit by $272 billion. That estimate—which is based on one of CBO's "rules of thumb"—provides a rough sense of how that difference, taken in isolation, would affect budget totals; it is not, however, a substitute for a full analysis of the implications of an alternative economic forecast.[12]

Moreover, although that rule of thumb is roughly scalable for moderate increases in interest rates, it would not provide an accurate assessment of the effect on the budget if interest rates equaled their averages from 1980 to 2000 because those averages were a great deal higher than both current rates and the rates that CBO projects for the coming decade. In particular, inflation was much higher in the early 1980s than in CBO's baseline projection, and real interest rates (which are adjusted to remove the effects of inflation) were also much higher because the rapid decline in inflation during the 1980s was unexpected. An analysis using an alternative economic forecast would be needed to account for differences in real interest rates as large as those between the averages from 1980 to 2000 and the current and projected rates. Moreover, such large differences in real rates would probably be associated with differences in inflation, private saving, inflows of capital from foreign investors, and other economic variables that would also affect the amount of tax revenues and spending for federal programs. CBO has not undertaken such an assessment.

Congresswoman Lee

Question. Americans not only need jobs, but they need jobs that pay a living wage. Jobs that provide enough income to feed their families, lift themselves out of poverty and into the middle class. What impact, if any, would raising the federal minimum wage to a living wage have on economic growth and the budget outlook? We also know that rising income inequality can have a negative impact on our overall economic growth. Does your outlook reveal anything about the effects of income inequality over the next 10 years?

11. Congressional Budget Office, *The Budget and Economic Outlook: 2015 to 2025* (January 2015), Appendix C, www.cbo.gov/publication/49892.

12. CBO's rules of thumb are generally symmetrical for increases and decreases in the economic variable in question. However, because interest rates on some types of Treasury securities are currently so close to zero, this rule of thumb is not fully applicable to decreases in interest rates.

Answer. Last year, CBO examined the effects of two options for increasing the federal minimum wage.[13] Although the agency has not updated its quantitative estimates of those effects, the qualitative findings would still apply to similar options. Specifically, increasing the minimum wage would have two principal effects on low-wage workers. Most of them would receive higher pay that would increase their family's income, and some of those families would see their income rise above the federal poverty thresholds. But some jobs for low-wage workers would probably be eliminated, the income of most workers who became jobless would fall substantially, and the share of low-wage workers who were employed would probably fall slightly. CBO did not assess the impact of those options on economic growth.

In addition to affecting employment and family income, increasing the federal minimum wage would affect the federal budget directly by increasing the wages that the federal government paid to a small number of hourly employees and indirectly by boosting the prices of some goods and services purchased by the government. Most of those costs would need to be covered by discretionary appropriations, which are capped through 2021 under current law. Federal spending and taxes would also be indirectly affected by the increases in real income for some people and the reduction in real income for others. As a group, workers with increased earnings would pay more in taxes and receive less in certain types of federal benefits than they would have otherwise. However, people who became jobless because of the minimum-wage increase, business owners, and consumers facing higher prices would see a reduction in real income and would collectively pay less in taxes and receive more in federal benefits than they would have otherwise. It is unclear whether the effect for the coming decade as a whole would be a small increase or a small decrease in budget deficits.

CBO's budget projections reflect trends in the distribution of income because that distribution is a key determinant of how much income will be taxed at particular rates and how many people will be eligible for certain benefit payments. For example, CBO expects that earnings will grow faster for higher-income people than for others during the next decade—as they have for the past several decades—which will tend to increase tax receipts. Specifically, receipts from income taxes will be greater because a larger share of income will be taxed at higher income tax rates; that effect will be partially offset by lower receipts from payroll taxes because a smaller share of earnings will be subject to the Social Security payroll tax. To take another example, because the Social Security Disability Insurance (DI) program uses average earnings per worker in the economy as part of the formula to determine benefits, those benefits have risen faster than the earnings of low-wage workers. That increase in benefits relative to the compensation associated with working tends to increase the number of people seeking DI benefits. However, CBO has not made a comprehensive assessment of the budgetary effects of projected changes in income inequality.

Question. While overall defense spending has decreased over the last several years due to sequestration and spending cuts, according to a recent CBO projection in November of 2014, the average real cost of the Department of Defenses' (DOD) base-budget plans from 2015 through 2019 would exceed average spending for DOD from 1980 to 2014 by $64 billion a year. Moreover, CBO estimates that the cost of those plans after 2015 would still significantly exceed the funding that would be provided to DOD under the Budget Control Act (BCA), which could pose a serious problem to our economy and the budget. How would overall

13. Congressional Budget Office, *The Effects of a Minimum-Wage Increase on Employment and Family Income* (February 2014), www.cbo.gov/publication/44995.

defense spending cuts reduce the federal deficit? What impact would defense spending cuts have on our overall economic growth, including revenues and overlays?

Answer. CBO's baseline economic and budget projections incorporate the assumption that funding for the defense activities that are subject to the caps put in place by the Budget Control Act of 2011 (as subsequently amended) will equal the amounts of those caps from 2016 through 2021. For later years, the baseline reflects the assumption that such funding will keep pace with inflation. Appropriations for overseas contingency operations (that is, overseas military operations, such as those in Afghanistan) are assumed to grow with inflation from the amount provided in 2015.

The projected funding for defense activities apart from overseas contingency operations is substantially below CBO's most recent projection, published in November 2014, of the costs of implementing the plans that the Department of Defense issued in April 2014.[14] (DoD's plans focus on defense activities excluding overseas contingency operations.) CBO has not completed its analysis of the President's most recent budget request, but it appears that DoD's current plans would also cost more than the amounts projected in CBO's baseline. Thus, the baseline implicitly incorporates the assumption that DoD's plans will be scaled back to comply with the funding caps and with CBO's extrapolation of those amounts in subsequent years.

In general, the impact of reductions in defense spending on the federal budget and the economy would depend on the specific reductions made and whether they were accompanied by other policy changes. If unaccompanied by other changes, such reductions would tend to reduce output in the short term by decreasing total demand for goods and services. In the long term, such reductions, by themselves, would lower government borrowing, which tends to bring down interest rates, boost private investment, and raise output.

Question. In 2014, our economy had the fastest pace of job growth since 1999, adding more than 11.2 million jobs over the past 58 consecutive months. However, there are still 8.7 million unemployed Americans, including 2.8 million long term unemployed. For communities of color, those statistics are even worse. Nearly 11 percent of African Americans, and more than 6 percent of Hispanics are unemployed, compared to their white counterparts who have an unemployment rate of just over 4 percent. While CBO has projected that the unemployment rate will continue to fall with historical lows into 2017, there are still too many people left behind and are discouraged from looking for work altogether. What impact, if any, has structural (or permanent) unemployment had, or will have, on our economic growth, particularly as we continue to recover from the Great recession?

Answer. In CBO's assessment, the recession and weak recovery have led to an ongoing reduction in the supply of labor, which will reduce economic growth over the next decade in comparison with what it otherwise would have been. Persistently weak demand for workers has led some people to leave the labor force permanently, and persistently high long-term unemployment has led some workers to experience stigma and the erosion of their skills. CBO estimates that the lasting effects of the recession and slow recovery will, in 2025, boost the unemployment rate by about 0.2 percentage points and depress the labor force

14. Congressional Budget Office, *Long-Term Implications of the 2015 Future Years Defense Program* (November 2014), www.cbo.gov/publication/49483.

participation rate by about 0.3 percentage points.[15] Those lasting effects also imply a reduction in real GDP of less than one-quarter of one percent in 2025.

Question. Health care spending has significantly slowed since 2010; due in part to the implementation of the Affordable Care Act, economic assumptions, and a change in CBO baseline projects for overall healthcare spending. Moreover, in 2013, total U.S. health spending grew by just 3.6 percent – the fifth consecutive year of historically low growth rates since the government began collecting this data in 1960. But CBO's report also highlighted the fact that over the next decade, healthcare spending, including Medicare and Medicaid, will grow faster than the economy. We also know that these programs, including Social Security, are earned benefits and provide critical income and healthcare to millions of retirees, workers with disabilities, spouses, and their children. Additionally, we also know that safety net programs such as the Supplemental Nutrition Assistance Program (SNAP) are vital to addressing poverty, and in millions of American's opinions, should not be targeted for cuts. These programs have proven anti-poverty effects, and particularly in the case of SNAP, also have a positive economic benefit, as the families who receive assistance spend the money immediately. Could you report on how investments in these programs, coupled with increased revenue, can have a positive impact on our long-term deficit?

Answer. The budgetary effects of combining additional spending on Social Security, Medicare, or means-tested programs with increases in revenues would depend on the specifics of the policy changes, which would determine both the changes in the amount of taxes that people owed and in the amount of benefits or services they received. If, on balance, revenue increases exceeded spending increases, then deficits would be reduced.

A combination of such policy changes could have macroeconomic effects that would "feed back" to the budget even if those changes had no net direct effects on deficits. Many ways of increasing revenue would reduce incentives to work and save and, thus, in the long run would reduce the supply of labor and capital in the economy and ultimately reduce tax collections (leaving aside the direct effects of the revenue increases). In addition, many sorts of increases in government benefits would reduce the supply of labor in the economy, which in

15. Congressional Budget Office, *The Budget and Economic Outlook: 2015 to 2025* (January 2015), p. 49, www.cbo.gov/publication/49892.

the long run would reduce tax collections—but that is not true for every possible increase in benefits.[16] Thus, it is possible that a combination of policies that raised both revenues and spending for benefits to an equal extent (leaving aside any indirect effects of those policies on the economy) could increase output and thereby reduce budget deficits—but such a combination would have to be carefully crafted in order to have such effects.

Of course, policies have other important effects besides their effects on budget deficits, such as on people's health or quality of life. Also, different combinations of policies would affect various groups of people to a different extent. Policymakers may decide that the effects of policies on budget deficits are less important than their effects on other aspects of the economy or society or their effects on particular groups.

16. For example, if the government provides a new benefit that gradually declines as recipients' earnings rise, those recipients would tend to reduce the amount they work for two reasons: First, because there is a decline in benefits associated with an increase in income, the total resources (compensation plus benefits minus taxes) available to recipients from an additional hour of work decreases and that makes work less valuable relative to other uses of people's time. Second, because benefits have been provided, the amount of total resources that recipients have for any given amount of work is greater and that allows those recipients to maintain the same standard of living while working fewer hours. Alternatively, under some circumstances, decreasing the rate at which benefits of an existing program phase out as income rises tends to encourage recipients to increase the amount they work.

CBO recently assessed the effects on the supply of labor stemming from decreasing rather than increasing benefits under one particular program, the Supplemental Nutrition Assistance Program, or SNAP (formerly known as the Food Stamp program). See Congressional Budget Office, *The Effects of Potential Cuts in SNAP Spending on Households With Different Amounts of Income* (March 2015), www.cbo.gov/publication/49978. The agency concluded that one illustrative approach to cutting SNAP benefits would increase the supply of labor; the two reasons mentioned earlier that a new benefit tends to reduce work would generate the opposite effects for that benefit cut. However, CBO also concluded that two other illustrative approaches to cutting benefits would decrease the supply of labor because of the particular ways in which they would phase out benefits. Although CBO did not analyze the effects of increasing SNAP benefits using analogous approaches, such changes would probably induce changes in labor supply in the opposite directions.