

Commitment to American Prosperity (CAP) Act

The CAP Act reduces total federal spending – discretionary and mandatory spending combined – to a target of approximately 20.6 percent of gross domestic product (GDP), the historical average of federal spending. Beginning in 2013, the CAP Act will establish federal spending limits that will be gradually reduced over 10 years to 20.6 percent.

Determining Spending Caps

The amount of spending allowed in any given year is a function of two things: a “lookback GDP” and a “nominal spending cap” expressed as a percentage of GDP. The lookback GDP is the average GDP of the first three of the preceding four years – i.e., the lookback GDP for 2013 would be the average GDP of 2009, 2010, and 2011 as determined by OMB (Office of Management and Budget). To determine the amount of permissible spending, the lookback GDP is multiplied by the nominal spending cap. In 2013, the CAP Act permits spending amounting to a nominal spending cap of 25 percent of lookback GDP. It is important to note that the nominal spending cap percentage will be higher than the actual percentage of GDP spent (the “effective cap”) because GDP in the current year will be higher than the lookback GDP barring an economic catastrophe. For example, 25 percent of the lookback GDP for 2009/10/11 results in an effective spending cap of 22.25 percent of GDP in 2013. The following table shows the steps above in practice for fiscal years 2013-2015:

	*Effective Cap	**Permissible Spending	Projected GDP	Nominal Cap	***Lookback GDP
2009	--	--	\$14,237	--	--
2010	--	--	\$14,513	--	--
2011	--	--	\$15,034	--	--
2012	--	--	\$15,693	--	--
2013	22.25%	\$3,649	\$16,400	25%	\$14,595
2014	21.70%	\$3,744	\$17,258	24.83%	\$15,080
2015	21.29%	\$3,873	\$18,195	24.66%	\$15,709

(\$ in billions)

*Yields Effective Cap = $\$3,649/16,400 = 22.25\%$

**Permissible Spending = $\$14,585 \times 25\% = \$3,649$

***Lookback GDP = $(14,237 + 14,513 + 15,034) / 3 = \$14,595$

Why Do We Use Lookback GDP and Skip a Year to Calculate It?

Lookback GDP is used for three reasons. First, using the average GDP from three prior years will help to smooth out any cyclical changes in the economic environment over a given time period. This means, for example, that one bad economic year would not cause an abrupt drop in permissible spending when coupled with two other years. Second, GDP numbers are not considered “final” until three months after the year has concluded, and even then they are subject to further revisions during the BEA’s (Bureau of Economic Analysis) annual July review, at which time the GDP numbers from the three most recent years are reviewed. In other words, the final GDP numbers for that year will be not ready for use in the budget calculations; plus, it would not be prudent to use projected GDP numbers for that year as they could be subject to significant political pressures. Third, it allows for an estimate for permissible spending one year before the start of a target fiscal year, giving policymakers ample time to make their deliberations and spending decisions.

Enforcing Spending Caps

OMB estimates the permissible spending limit for a target fiscal year at the beginning of the prior fiscal year, on April 30, August 20, and 15 days after the conclusion of that fiscal year. If the August 20 report indicates that spending will exceed the limit, the Senate and House Budget Committees may report a resolution that would bring spending in line with the cap. If federal spending is projected to exceed the CAP Act designated amount for that year, the OMB is required to sequester funds such that it brings federal spending back to the CAP Act mandated levels. The sequestration amounts are determined proportionally to growth in outlays for direct spending, discretionary security spending, and discretionary non-security spending, reducing within such accounts by a uniform percentage. The sequestration must occur within 45 days after the start of the fiscal year. This concept is based in part on the sequestration requirements of the current PAYGO law and its predecessor, the Gramm-Rudman-Hollings Balanced Budget and Emergency Deficit Control Act.

Exceeding Spending Caps

The CAP Act does not directly preclude Congress from spending in excess of the prescribed spending caps. However, it does establish a new budget point of order that a member of Congress may raise when such legislation is considered. Waiving this point-of-order would require a supermajority threshold of two-thirds in both the House and the Senate. As such, this point-of-order would present a powerful tool to curb excess spending. Currently, budget points of order are subject to either a three-fifths majority or simple majority (depending on the point of order) vote threshold in the Senate, and whatever rules are adopted for the bill by the House Rules Committee in the House. The bill also codifies in law, for the first time, a definition of “emergency spending” that must be met in order for emergency spending to be used to exceed the proscribed spending caps. Under CAP, for a spending bill to be legally deemed emergency spending it must be “for a situation that poses a threat to life, property, or national security, and is (i) sudden, quickly coming into being, and not building up over time; (ii) an urgent, pressing, and compelling need requiring immediate action; (iii) unforeseen, unpredictable, and unanticipated; and (iv) not permanent, and temporary in nature.” Spending need not be designated as “emergency spending” to exceed the cap as long as the point of order is waived by a two-thirds vote; however, emergency spending is the most likely scenario to spend above the cap.