COMMITTEE FOR A RESPONSIBLE FEDERAL BUDGET

Memo to: Board and Members
From: Carol Cox Wait and Susan Tanaka
Date: June 16, 1998

Subject: The FY 1999 Budget Debate:
A Year of Living Dangerously

Surplus, What Surplus? Sorry there is no surplus.

The President's budget and the House and Senate budget resolutions are not in surplus. According to the 1990 Budget Enforcement Act, Social Security receipts and disbursements are off-budget and are not to be "…counted as budget authority, outlays, receipts, or deficit or surplus.." All of the surpluses about which we have heard so much are attributable to Social Security. Because the House and Senate budget resolutions comply with the law, they show significant deficits every year (see table 1 below for comparison).

Table 1. Projected Deficits* in FY 1999 Budget Proposals

	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002	FY 2003
President**	-94.9	-112.3	-130.0	-124.9	-90.2	-108.2
House	-50.7	-83.0	-104.6	-105.6	-65.5	-88.1
Senate	-95.7	-108.2	-124.4	-120.7	-75.0	-92.3

* On-budget deficits. Do not include Social Security and postal transactions.
**The President's Budget as re-estimated by CBO. We use the CBO re-estimate to avoid differences due solely to differences in underlying economic or technical assumptions.

Deficits in the House budget resolution are lower than in either the Senate resolution or the President's budget solely because the House acted later and factored into their budget more recent CBO revenue estimates. Even with those revenue re-estimates, however, the House resolution shows deficits in every year.

Once the differences due to the new revenue estimates are eliminated, we are struck by the similarity in the bottom line outcomes in the President's budget, and the House and Senate versions. Despite the apparent similarity in aggregates, however, there are significant differences between Congress and the President—and between the House and Senate. The biggest differences are:

- The President proposes to use the money from tobacco legislation and other offsets to finance $118 billion in new programs and $24 billion in tax cuts.

220½ E Street, N.E.*Washington, DC 20002*Tel. (202) 547-4484*Fax (202) 547-4476*CRFB @ aol.com

- Congressional versions of the budget assume deficit-neutral tax cuts financed by unspecified offsets. It now appears likely that Congress will use tobacco legislation revenues to help pay for these tax cuts and other priorities.

  > The Senate resolution cuts taxes $30 billion over five years, although the Majority Leader has promised to increase the cut to $60-70 billion by final passage. Senate spending levels generally reflect the 1997 BBA levels. The Senate resolution does not assume tobacco revenues, but provides that if legislation is enacted, revenues would be dedicated to the Medicare hospital insurance trust fund.

  > The House cuts taxes $101 billion, although the Speaker has promised that the final version will be more moderate. The tax cut is financed by unspecified spending cuts—$45 billion from discretionary programs and $56 billion from entitlements. The House resolution is silent on tobacco revenues.

Feeding Frenzy

Because the last unified budget surplus was recorded in 1969, surplus politics are new to us. We thought governments adopted tax cuts and spending increases when economies were in recession and needed stimulus. Thus, we were taken aback and dismayed last year when Congress and the President spent $200 billion almost over night. Remember, they discovered the extra money (due to CBO revenue re-estimates) shortly before closing the deal on the balanced budget agreement and proceeded to use all of that money to increase spending and cut taxes as part of the final deal.

Growing Unified Surplus Estimates. This year, the numbers are much larger and are growing. Since January, unified budget surplus estimates based on latest CBO analyses have risen $130 billion for fiscal years 1999 to 2008. OMB's midsession report implies $250 billion in additional surpluses.

The House leadership is reportedly furious with CBO's upward re-estimates of unified surpluses. If they had known last year what we know now about the budget picture, they could have cut taxes much more in the 1997 Balanced Budget Agreement. Of course, that might have delayed unified budget balance, but they only promised to reach balance in 2002. The leadership also questions CBO's continued use of moderate economic assumptions. They would prefer "green light" projections that could justify larger tax cuts. If, however, CBO's projections were to reflect "post-policy" assumptions (as OMB's do), they would be much more prone to subjective judgments about future economic performance and provide a much more uncertain basis for policy decisions.

As it is, there seems to be no end to the appetite of this Administration and this Congress to earmark every dime for some favored spending program or tax cut. As revenue estimates continue to rise, the Administration has identified more "priority needs" to use the money, including openness to a bigger tax cut. The House and Senate continue to talk of ever larger tax cuts. How likely is it that they will acknowledge slower growth and declining revenue estimates if they should develop and pare back spending plans and tax increases? They didn't during the 1990 budget debate when the economy began to sour. All of this optimism wouldn't be so troubling if lawmakers were willing to backup their budget promises with enforcement language that (at least) would make them revisit their spending and tax policies should reality turn out less rosy than projected. But so far, neither end of Pennsylvania Avenue has been willing to show that level of commitment to their numbers.

Veterans' Health Benefits for Tobacco Related Illnesses. A court held that veterans are entitled to collect health benefits for tobacco-related illnesses. The Administration added the estimated cost of those benefits ($17 billion over five years) to the baseline. The President's budget recommended repealing the entitlement and using it on other priorities. The House and Senate budget resolutions support the Administration on the repeal, but assume that money is available to offset part of the cost of the highway bill—and for other purposes.

This is like saying: I lost a lawsuit. The plaintiffs got a judgment for $10 million against me. I don't have $10 million to pay them, but I win on appeal, so I go out and spend the $10 million I never had in the first place. Too bad I didn't lose a $100 million lawsuit!

Tobacco Legislation. Passing a law to cut back on teen smoking sounded like a good idea, if it could be done. Passing a law to determine how much tobacco companies would pay for their sins, how much of that would go to the Federal government and how much to States, and over what period of time, even seemed like a salutary goal. No matter how one feels about tobacco, however, the debate on the floor of the Senate has proved very disturbing. Clearly, this is not about tobacco. It is about money. The numbers have risen from $360 billion to above *$500 billion* (over 35 years), and that is not enough to satisfy some Senators.

Don't Stop Thinking About Tomorrow

Although Ways and Means Committee Chairman Bill Archer warns of surpluses "surging out of control," we are not alarmed. Despite good news in the short term budget projections, the longer-term poses very serious challenges indeed.

- *CBO, GAO, and even, eventually, OMB long-term simulations show that unified surpluses are temporary.* Between 2010 and 2030, economic growth slow as baby boomers retire. Under current policies, shortly after 2020, Social Security will begin running deficits, unified budget deficits will reappear, and the national debt will rise. (See table 2.)

Table 2. Long-Term Budget Projections
Percent of GDP

	CBO			GAO		
	1997	2030	2050	1997	2030	2050
Receipts*	21	20	20	21	20	20
Expenditures*						
Social Security	4	6	6	5	7	8
Medicare	3	6	7	3	6	8
Medicaid	1	2	3	1	2	4
Other	11	8	8	9	9	8
Net Interest	3	1	4	3	2	9
Total	22	24	27	21	26	37
Deficit (-) or Surplus*	0	-3	-7	0	-5	-6
Debt held by the public	47	32	94	47	42	192

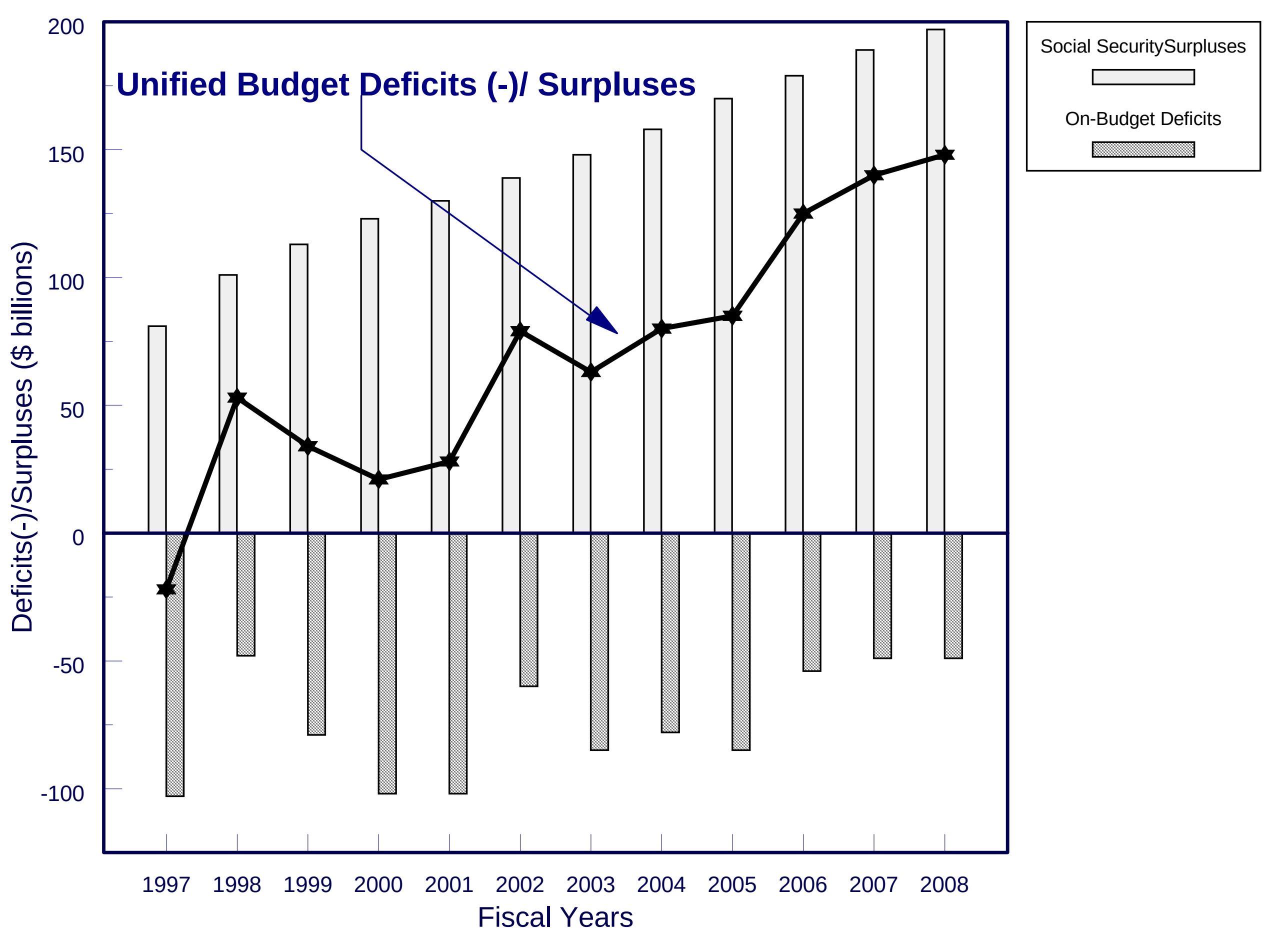
Sources: CBO, Long-Term Budgetary Pressures and Policy Options (May 1998). GAO, unpublished tables (February 1998).
* Measured on a National Income and Product Account (NIPA) basis.

- *Small changes in the economy could reduce unified budget surpluses and even bring back unified budget deficits.* CBO indicates that a 1 percent change in this year's GDP growth rate would increase or decrease revenues alone by $18 billion in 1998. If spending is 2 percent higher and revenues 2 percent lower than currently estimated, unified surpluses could fall $60 billion a year. Changes in the opposite directions would produce $60 billion more in unified surpluses.

- GAO's simulations show that if short term surpluses are saved, the deficit in 2030 would be 60 percent lower than if surpluses are not saved. Long-term projections of current policies show an unsustainable mismatch between promised benefits and tax revenues. To close the gap, policy makers will have to reduce benefit costs or raise taxes. Running short-term surpluses and paying down the publicly-held debt would help because the amount the government has to spend on interest would be lower.

The President and the Congressional leadership continue to emphasize their desire to"save" surpluses for Social Security. **We reiterate: they are using Social Security surpluses to finance their spending and tax cutting proposals.** Unified budget surpluses need to be significantly higher before they can claim that they are offsetting the full cost of their spending increases or tax cuts and saving all of Social Security's surpluses. (See figure I.)

Figure 1. Budget Deficits and Surpluses



*CRFB estimate based on CBO May 1998 Monthly Budget Review

Let's Hear it for Gridlock

As part of our ***Exercise in Hard Choices*** we have asked audiences across the country what they would do with any short term budget surpluses. Ninety percent would save the surpluses and buy down debt held by the public. Public opinion polls show that more people would use surpluses to shore up Social Security or to pay down the public debt (the same thing, really) than for tax cuts or new programs. The question is, why don't elected officials do what their constituents want them to do?

There is a school of thought that says voters are so complacent, politicians have to appeal to their core constituencies to help ensure that they will vote this fall. This promises to be a rather expensive, tax-financed get-out-the-vote (that is, incumbent protection) campaign.

The longer the budget debate has proceeded, the more convinced we have become that the country well might be better off if Congress were to pass a continuing resolution and go home. Given the track record so far (e.g., the transportation bill and the "emergency" supplemental appropriations bill), we fear that anything they and the President can agree to enact this year will be counterproductive and plain old bad policy.

Building a Better Future: An Exercise in Hard Choices

We have completed five of the ten ***Building a Better Future: Exercise in Hard Choices*** programs we will host this year. Nationally, these meetings are co-sponsored by American Express Financial Advisors. Locally, newspapers, television stations, universities, businesses, and local organizations have helped us put on these programs. Some thirty other organizations representing views across the political spectrum, are working with us on these programs.

This year's Exercise has been revised to focus on long-term fiscal policy issues, including Social Security and Medicare reform, tax policies, and the rest of the budget. So far, over 800 people have given a full day of their time to participate.

Between now and next Spring, we will hold meetings in Boston, Dallas, Ft. Lauderdale, Seattle, and New York City. We will issue a final report on our finding next spring. If you interested in interim results, please contact our office at (202) 547-4484 or crfb@aol.com.