

INFORMED BUDGETEER

APRIL POSTS STRONG REVENUE GAINS

- There has been considerable interest in daily tax return data recently, as people have tried to gauge the strength of year-end tax payments for 1997. With all but one day’s worth of data in hand, it appears that April revenues have been very strong indeed.
- April always generates a large share of the year’s overall tax revenues since it includes year-end payments of individual tax liabilities. For example, April comprised 14.5% of FY 1997’s revenues.
- Non-withheld, year-end payments are heavily influenced by one-time capital gains realizations. The inherent variability of such income makes April revenues very difficult to forecast. This April, non-withheld payments are coming in roughly \$20 billion ahead of last year. This is similar to April 1997’s \$25 billion non-withheld increase.
- April withheld income tax receipts have also been healthy. They are running roughly 8% higher than the same period last year. For year-to-date FY1998, revenues are running 10.9% above YTD FY1997.

APRIL MONTH- TO-DATE RECEIPTS: 1997 VS. 1998			
(\$ in billions)			
	Overall Revenues	Individual Non-Withheld	Individual Withheld
April 1-29, 1998	247,483	138,124	93,224
April 1-29, 1997	217,402	118,997	86,029
Percent Change	13.8	16.1	8.4

STUDENT LOANS: WHO GETS THE SUBSIDY?

- Have you ever thought you knew what a word meant and then had to stop and think about it because you’re not quite sure after all, given how the word is used in the press? The press has been reporting on congressional efforts to reset interest rates for student loans because, under current law, rates will drop on July 1 to a level at which everyone agrees will be too low for banks, and students will no longer be able to get loans from banks.
- Study the following sentence from an article in the April 30th *Washington Post* on the supplemental appropriations bill: “Negotiators completed work on everything except a Republican provision that would provide more than \$2 billion of subsidies to banks as incentives to continue providing student loans.”
- From this statement, whom would you think is benefitting from the subsidy? Sure sounds like the banks. But what’s a subsidy again? Look it up: “a grant by a government to a private person or company to assist an enterprise deemed advantageous to the public” (*Merriam Webster’s Collegiate Dictionary*).
- So who is getting a subsidy in the student loan program--private persons or companies? Consider what would happen if there was no federal student loan program of any kind. How would students pay for college if they didn’t have enough saved? Perhaps a student would be able to get a loan from a bank, but the interest rate would be higher than credit card interest rates (say 20%, because no collateral or credit history). And repayment would start not when the student graduates and has a job, but immediately, when the student is starting school and has no income. Or else a parent would have to co-sign the loan and/or put home equity, if any, behind the loan.
- Enter the federal government. Under the above scenario, most students simply would not get loans because the cost would be too prohibitive, and banks (for whom student loans comprise only 1% of total assets) would make other kinds of loans. But the federal

government, deciding that college education is an “enterprise...advantageous to the public”, guarantees 98% of the loan made by banks (or else makes the loan itself in the direct lending program), promises that students will pay a rate no greater than 8.25%, and suspends interest repayments while many students are in school.

- Although the federal government makes actual payments to banks to make these benefits possible, to whom do the actual benefits flow? Who faces lower interest costs so that they can actually afford to take out a loan and go to college, thereby fulfilling the public interest? Students, of course. Students receive the subsidy.
- The trick is to pay banks just enough so that they are indifferent between continuing to make student loans at the terms and conditions beneficial to students or making, say, additional car loans. In the past, it appears that the government has set interest rates in the student loan program that offered banks more profits than necessary to participate.
- The current debate is how to cut banks’ remaining excess profits without threatening student access to loans (because at some point, banks would drop out and seek alternative investments with a higher return). The Administration asserts it knows the truth and would cut current bank rates by 80 basis points, while banks complain about the House and Senate higher ed bills that would reduce bank returns by 30 basis points.
- In either scenario, all the subsidies flow to students, with a legitimate debate about what are adequate returns to banks to attract sufficient participation in the program. But it is a debate that the legislative process is ill-equipped to resolve accurately. No side possesses the truth on this question. It is only a market-based approach that replaces the current programs, as the Administration, Senator Kennedy, and others have suggested, that will reveal the right amount of incentives to offer so that students can continue to receive a subsidy for college.

1998 INTEREST RATE OPTIONS				
(Rates in %)				
Proposals	Students	Lenders	Taxpayer Cost ^A (billns)	
			5/yr	10/yr
<u>Current Rates</u>				
Repayment	7.92	7.92	+2.9	+6.1
In school	7.32	7.32	-2.0	-5.9
<u>July 1, Rates</u>				
Repayment	6.96	6.96	NA	NA
In school	6.96	6.96		
<u>Administration</u>				
Repayment	7.12	7.12	+1.1	+2.0
In school	6.52	6.52	-1.5	-3.2
<u>House & Senate</u>				
Repayment	7.12	7.62	+3.9	+8.4
In school	6.52	7.02	+1.2	+2.6

^AItalics indicates with Probabilistic Scoring (OL). SOURCE: For interest rate projection: CBO’s “Economic and Budget Outlook: FY1999-2008.” For taxpayer cost: CBO estimates.

SUPPLEMENTAL BECOMES LAW

- President Clinton has signed into law a \$3.4 billion emergency defense and disaster relief supplemental appropriations bill (H.R. 3579) following congressional action to pass the conference agreement late Thursday.
- The bill includes the emergency defense and disaster aid requested by the President, but the conferees did not fund the \$17.9 billion requested for the International Monetary Fund (IMF) and approved by the Senate.
- Major issues that were expected to be raised during the conference -- a student loan interest rate “fix,” ISTEAs extension, and inclusion of the Agricultural Research, Extension and

Education Reform conference report -- were **not** included in the final bill. The conferees did not consider adding funding to pay U.S. dues to the United Nations as urged by the Administration.

- The final bill includes:
 - \$2.9 billion in emergency defense spending, including \$0.5 billion for Bosnia, and \$1.3 billion for military operations in Southwestern Asia;
 - \$2.6 billion in emergency appropriations to aid victims of natural disasters, which is offset;
 - \$142 million in non-emergency program supplementals, which are offset; and
 - \$550 million for the veterans compensation COLA.
- The emergency disaster funding and other supplementals are offset with a \$2.3 billion rescission of Section 8 housing funding and \$295 million in airport improvement grant contract authority. These rescissions offset the BA in the bill, but not outlays. The Section 8 funding is likely to need to be restored in FY 1999.

LIV SUPREME COURT ORAL ARGUMENTS SUMMARY

- On April 27th, the Supreme Court heard oral arguments in the latest chapter of the Line Item Veto saga. The argument lasted 60 minutes: with 30 minutes for the Government and 15 minutes each for the two plaintiffs (the Potato cooperative and the New York entities).
- Budgeteers will recall from previous issues that the two constitutional issues in the case involve: (1) whether or not LIV violates the Presentment Clause in Article I of the Constitution (that all laws must pass in the same form by both chambers of Congress and then be signed in whole or returned with a veto message from the President - nothing more, nothing less) and (2) whether or not LIV violates the doctrine of Separation of Powers by granting the President "lawmaking" authority - or in other words, is the LIV a proper delegation?
- A number of the Justices seemed concerned about both constitutional issues. Also in question is whether or not these two parties have standing to challenge the LIV. It is noteworthy that the previous litigation involving the LIV which was brought by members of Congress and the Treasury Employees Union was dismissed last year by the Supreme Court because of lack of standing.
- The government argued first in support of the LIV. The Court immediately began asking questions on the merits (whether or not the law is constitutional) and did not ask at all about standing (whether these are the proper plaintiffs with a legitimate injury). Most of the Justices participated in the questioning.
- Particularly with respect to the cancellation of limited tax benefits, a number of Justices again were concerned that the LIV permits the President to randomly pick and choose among citizens/taxpayers. It appears that the Court is going to give the tax provisions a very close look. They did not seem inclined to view the ability to raise revenue as the flip side of spending - it is something more unique unto itself.
- Justice Ginsberg suggested that what this law does is call upon the President to make the hard choices (what to spend? to whom to grant a tax benefit?) that the Congress finds itself unable to do. If so, this is performing a lawmaking function rather than executing a duly delegated authority with respect to an enacted law.
- The view of many court watchers that morning was that the LIV is not long for this world. The questioning seemed to indicate a Court very wary of the power which the Congress has attempted to bestow upon the President.

- Particularly with respect to the delegation question, one Justice summed it up well by asking the Government: I see that the LIV tells the President what he may NOT cancel, but where does it tell him what he must cancel? With respect to delegation, the Court is looking for "intelligible principles" - i.e. fairly specific criteria for the President to use in taking the questioned action. The Court did not seem at all convinced that "not harming the national interest" and the other criteria set out in the law, satisfy this test.
- The Potato Cooperative's attorney was questioned on the both the merits and the standing issue. Two or three Justices seemed concerned that perhaps the injury was too remote to warrant finding that these plaintiffs had standing. The Cooperative's response was that it was clear the Congress enacted this particular tax provision with the purchasers (the cooperatives) not the sellers (owners of processing facilities) in mind.
- The argument concluded with the presentation by the attorney for the various New York entities. Again, the Justices' questions focused upon the standing issue. The fact that the State of New York was not a party to this litigation did not escape the attention of the Court.
- Justice Ginsberg asked about the issue raised by the Government regarding the use of the word "individual" instead of "person" in the portion of the statute dealing with the expedited judicial procedures. The attorney for the City of New York responded that they arguably have an "individual" among their plaintiffs because they also sued on behalf of the hospital employees' unions.
- He further argued that he could not believe that Congress would allow real people to make use of the expedited judicial procedures (i.e. a direct appeal to the Supreme Court) and not permit injured corporate entities or municipalities the same opportunity. No one other than Ginsberg took up this line of questioning.
- We can expect to see a decision some time before the Court recesses in June.

THE LOCK BOX QUESTION AGAIN

- Budgeteers will be interested that the question that seemed to "stump" everyone - including members of the Court - was, how the "lockbox" works. Although the Government argued that the "lockbox" is significant in showing that LIV does not allow the President to "repeal" laws, none of the lawyers could explain to the Court how it works. Both the Government and the attorney for the Potato Cooperative have submitted materials to the Court to correct the record with respect to the "lockbox" issue.
- The "lockbox" is fairly simple. In order to ensure that savings resulting from Presidential cancellations under the LIV go towards deficit reduction, the lockbox (section 1024 of the Budget Act) provides that any cancellations of discretionary budget authority will lead to a reduction in the statutory discretionary caps and any cancellations of either direct spending or limited tax benefits will not be available to be spent under Pay-Go. Both of these "scorekeeping" rules have the effect of creating Budget Act points of order and the possibility of a sequester if any attempt is made to "spend" the canceled amounts.