

INFORMED BUDGETEER:**CBO'S FIRST UPDATE OF THE YEAR**

- The Congressional Budget Office (CBO) on May 18 published its completed analysis of President Bush's budget request for FY 2002. *An Analysis of the President's Budgetary Proposals for Fiscal Year 2002*, can be found on the CBO web site linked to our SBC site.
- The following table summarizes only the technical changes in conjunctions with their analysis of the President's budget:

Changes in CBO's Surplus Projections since January 2001 (By Fiscal Year, \$ in Billions)			
	2001	2002	2002-2011
January 2001 Baseline Surplus	281	313	5,610
Technical Changes			
Revenues	-20	-10	-15
Outlays			
Discretionary	-4	-4	-27
Mandatory			
Medicaid	*	*	-25
SSI	*	-1	-17
Credit reestimates	-11	0	0
SCHIP	1	1	7
FHA**	2	2	19
Other	<u>-1</u>	<u>1</u>	<u>9</u>
Subtotal, mandatory	-10	3	-7
Subtotal, outlays	-14	-1	-34
Total Effect on Surplus	-6	-9	19
May 2001 Baseline Surplus	275	304	5,629

SOURCE: CBO; *Between -\$500 million and \$500 million; **Mutual Mortgage Insurance, outlay increases reflect offsetting collections reclassified as discretionary.

- The CBO analysis of the President's budgetary request compared to the recently passed FY 2002 Budget Resolution follows:

Comparison of CBO's Reestimate of the President's Budget and the Congressional Budget Resolution (\$ in Billions)						
	Reestimate of Pres. Budget		Budget Resolution*		Budget Res. less reestimate	
	2002	2002-11	2002	2002-11	2002	2002-11
Revenues						
On-budget	1669	19482	1638	19911	-31	429
Off-budget	<u>532</u>	<u>6691</u>	<u>532</u>	<u>6691</u>	<u>0</u>	<u>0</u>
Total	2201	26173	2171	26603	-31	429
Outlays						
Discretionary						
Defense	320	3621	319	3592	-0	-28
Nondefense	<u>364</u>	<u>4189</u>	<u>363</u>	<u>4130</u>	<u>-1</u>	<u>-59</u>
Subtotal	684	7809	683	7722	-2	-87
Mandatory						
Social Security	451	5724	452	5721	0	-2
Medicare	226	3279	226	3474	-0	195
Other	<u>401</u>	<u>5100</u>	<u>405</u>	<u>5181</u>	<u>5</u>	<u>82</u>
Subtotal	1078	14102	1082	14376	5	274
Net Interest	<u>182</u>	<u>1083</u>	<u>187</u>	<u>1120</u>	<u>5</u>	<u>37</u>
Total Outlays	1944	22994	1952	23218	8	224
On-budget	1583	18784	1590	19015	8	231
Off-budget	361	4210	361	4204	1	-7
Surplus						
On-budget	86	698	48	897	-38	198
Off-budget	<u>171</u>	<u>2481</u>	<u>171</u>	<u>2488</u>	<u>-1</u>	<u>7</u>
Total	257	3179	219	3384	-39	205
Memorandum:						
Disc. BA**						
Defense	325	3688	325	3656	0	-32
Nondefense	<u>336</u>	<u>3815</u>	<u>336</u>	<u>3774</u>	<u>0</u>	<u>-42</u>
Total	661	7504	661	7430	0	-74

SOURCE: CBO; *These figures are consistent with scoring at the time of passage

of the Concurrent Resolution on the Budget for FY 2002 and do not include revisions that were done pursuant to Section 310 (c)2(A) of the Budget Act. **Budget Authority in the Administration's budget excludes \$22.7 billion in advance appropriations for 2002 that the President proposes to reclassify as mandatory spending.

- In preparing the analysis, CBO provided an update of their January baseline budget projections based strictly on technical changes. These technical changes include: year-to-date information on spending and receipts, revised rates of projected spending, and budget reclassifications.
- Overall, CBO has only slightly increased its projected budget surplus by \$19 billion over the 2002 to 2011 period from \$5.610 trillion to \$5.629 trillion as a result of these technical changes. In the near term, for the current fiscal year the projected budget surplus of January was reduced by \$20 billion in less revenues, but offset with \$14 billion in less spending, for a net \$6.0 billion reduction in the January projected surplus of \$281 billion.
- Later this summer, CBO is required by law to provide a mid-session update of these projections to reflect both policy changes, technical changes, and changed economic assumptions from the time of their January forecast

SENATE RECONCILIATION TAX BILL

- The reconciliation tax bill (Restoring Earnings to Lift Individuals and Empower Families - - RELIEF - - Act of 2001) passed the Senate on May 23, by a vote of 62-38. All Republican Senators and 12 Democratic Senators voted for the bill. As of print time, conferees were meeting but have not yet reached a final agreement.
- After expiration of the statutory 20 hours of debate allowed for a reconciliation bill, the Senate remained on the bill for an additional 25 hours, voting on a total of 54 amendments. There were 26 motions to waive the Budget Act made; none were agreed to.
- Overall, the bill reduces revenues by \$1.238 trillion and increases outlays by \$109 billion over eleven years, for a total cost of \$1.347 trillion. The Senate-reported bill included the bottom bracket reduction retroactive to January 1, 2001 and a reduction in all other marginal rates, effective January 1, 2002.
- The bill doubles the child tax credit from \$500 to \$1000 over ten years, and makes the child credit generously refundable.
- The bill contains marriage penalty relief, education tax relief and pension and IRA savings incentives. The legislation fully repeals estate tax by 2011.
- The Senate bill makes the tax code more progressive. Wealthy taxpayers will pay a larger share of the income tax than they do now.
- Through the Senate amendment process, the Senate passed bill now includes:
 - < an increase in the adoption credit to \$10,000.
 - < a \$250 nonrefundable tax credit for teachers' classroom expenses and a \$500 above-the-line deduction for teachers' professional development expenses.
 - < an increase in the dependent care credit.
 - < a deduction for charitable contributions of artistic works and books.
 - < a permanent extension of the research and development tax credit.
- These amendments were offset by reducing the Senate-reported marriage penalty relief and by changing the corporate estimated tax requirements.

VOTE-A -RAMA

- For those who were wondering how many votes the Senate recorded

on the tax bill this week, the *Bulletin* looked into it for you.

- The Senate has had a total of 54 roll call votes on H.R. 1836, over the course of 4 days with 27 of those votes recorded on Tuesday, May 22.
- That is just 3 votes shy of the record for the most roll call votes in the Senate on a reconciliation bill. That honor belongs to H.R. 2491 the Balanced Budget Act of 1995 (BBA), which had a total of 57 votes recorded in the Senate over 2 days (October 26-27, 1995). The BBA also holds the title of the most roll call votes in a single day in the Senate, on October 27, 1995 the Senate had 39 roll call votes between 9:30 a.m. and midnight.

S.1 : THE COST OF SCHOOLING CHILDREN

- The Senate took up the S.1 education reform bill, also known as the Better Education for Students and Teachers (BEST) bill, on May 3. The House passed its version on May 23 by a vote of 384-45.
- S.1 reauthorizes programs under the Elementary and Secondary Education Act (ESEA) through 2008, ostensibly following the principles for reform outlined by the President in his *No Child Left Behind* proposal.
- The bill reported by the Senate Health, Education, Labor And Pensions Committee (HELP) authorized \$27.7 billion on elementary and secondary programs for 2002. The comparative funding for these programs in 2001 was \$17.6 billion, and the President’s budget requests \$19.1 billion for the same. Over the 2002-2008 authorization period, authorized spending totals \$205.5 billion. Most of the difference over last year’s funding level is explained by a dramatic increase in authorized spending for Title I (education for the disadvantaged).
- As of May 23, numerous amendments had been adopted on the floor, including 13 that altered discretionary spending provisions in the underlying bill. The *Bulletin* calculates that these amendments, coupled with increased authorizations in the Jeffords substitute, raised total authorized discretionary spending in the bill by \$1.7 billion in 2002 and \$97.9 billion over the period 2002-8.
- In addition, the Senate adopted by voice vote an amendment that would fund IDEA grants to states at the 40% level by 2007. This amendment requires mandatory spending of \$181.1 billion over the next ten years. The Budget Resolution assumed a 20% discretionary increase for IDEA, but did not provide an allocation for any mandatory provision.
- The House companion bill (H.R. 1) as passed authorizes \$22.8 billion for 2002. The House bill reauthorizes programs only through 2006, but a roughly comparable spending figure for 2002-2008 would be \$198 billion.

GSEs UNDER THE MICROSCOPE AGAIN

- Last week was a busy one for CBO in looking at the three government-sponsored enterprises (GSEs) engaged in housing activity: Fannie Mae, Freddie Mac, and the Federal Home Loan Banks (FHLBs).
- CBO released two companion reports entitled *Federal Subsidies and the Housing GSEs* and the supporting *Interest Rate Differentials Between Jumbo and Conforming Mortgages, 1995-2000*. CBO Director Crippen also testified before a subcommittee of the House Financial Services Committee on CBO’s findings.

- It was about a year ago that Fed Chairman Greenspan, in responding to a letter from the House subcommittee Chairman Richard Baker (long a watchdog of the activities and risks posed by and the regulatory structure over the GSEs), suggested that it might be appropriate for CBO to update its 1996 study of the federal subsidies conferred on the GSEs and how they are allocated.
- CBO’s new analysis (prepared for Chairman Baker) – while responding to and improving on criticisms of the first study, using new methodology, and estimating new levels of subsidy – reaches a familiar conclusion. In 2000, Fannie Mae and Freddie Mac passed on 63% of the federal subsidy to mortgage borrowers, and **retained the balance – 37% – for its own shareholders and other stakeholders**. Back in the 1996 report, CBO likewise found that “as a means of funneling federal subsidies to home buyers...the GSEs are a spongy conduit—soaking up nearly \$1 for every \$2 delivered.”
- And while not included in its original study, CBO now reports that the FHLBs pass on even a smaller portion of their subsidy to “conforming” (< \$275,000) mortgage borrowers – 10%. Though their subsidy accounts for the smallest piece (22%) of the total subsidy provided to the three housing GSEs, the hefty remaining 90 percent of that subsidy is retained by the FHLBs for other stakeholders and spread over other assets held by members institutions, such as jumbo mortgages and other loans.
- Familiar also, to budgeteers with long memories, will be the scoffing response to CBO’s analysis --“Subsidy? What subsidy?” CBO’s analysis makes the crucial point that the federal government can extend a subsidy without providing an appropriation.
- In the case of these GSEs, the federal government confers a subsidy in two ways: (1) “the direct cost from the fees and taxes that otherwise would be collected by federal, state, and local governments”, and (2) “the opportunity cost of providing free credit enhancement to the GSEs [with the perception by investors of protection from credit risk], because competing financial institutions would be willing to pay to receive similar treatment.”
- In the latter case, the GSEs can issue debt at lower cost and receive better prices on mortgage-backed securities (MBSs) than competitors can. All told, federal subsidies accruing to the housing GSEs amounted to \$13.6 billion in 2000, but only \$7 billion of that amount reached the intended target – conforming mortgage borrowers – in the form of lower interest rates (see table below).

Sources of Federal Subsidies in 2000 to Housing GSEs (\$ in billions)		
GSE	Level in 2000	Percentage of total
Fannie Mae		
Debt	3.6	45%
MBS	1.9	
Tax & Regulatory exemptions	<u>0.6</u>	
Subtotal	6.1	
Freddie Mae		
Debt	2.4	34%
MBS	1.8	
Tax & Regulatory exemptions	<u>0.4</u>	
Subtotal	4.6	
FHLBs		
Debt	2.8	22%
Tax & Regulatory exemptions	<u>0.2</u>	
Subtotal	3.0	
TOTAL	13.6	

Distribution of Subsidies in 2000		
	Level in 2000	Percentage of total
Amount passed to borrowers:	<u>7.0</u>	51%
Fannie Mae	3.8	62%
Freddie Mac	2.9	63%
FHLBs	0.3	10%
Amount retained by:	<u>6.6</u>	49%
Fannie Mae	2.3	38%
Freddie Mac	1.6	37%
FHLBs stakeholders	2.7	90%
TOTAL	13.6	--

Source: SBC