

INFORMED BUDGETEER

A CUSTOMARY OFFSET

customary *adj.* in keeping with custom, or usage; usual; habitual.

offset *n.* anything that balances, counteracts, or compensates for something else; compensation.

- The generic term “Customs user fees” refers to nine different conveyance and passenger user fees and a merchandise processing fee collected by the Border and Transportation Security Directorate (formerly the U.S. Customs Service) of the Department of Homeland Security. The conveyance and passenger user fees were first established by the Consolidated Omnibus Budget Reconciliation Act (COBRA) of 1985; the merchandise processing fee was established by the Omnibus Budget Reconciliation Act (OBRA) of 1986. Together these fees bring in about \$1.3 billion per year to the federal government.
- Customs user fees are classified as offsetting receipts and appear in the budget as negative outlays rather than as revenues. Budgeteers define offsetting receipts and offsetting collections as fees, charges and assessments levied on individuals or organizations directly benefitting from, or subject to, regulation by a government program or activity. Offsetting receipts require further legislative action to be spent; offsetting collections do not. (Revenues, on the other hand, result from the federal government’s exercise of sovereign power. Most federal revenues are from taxes, which people are compelled to pay.)
- When first enacted in 1985, Customs user fees were to be permanent – they had no expiration date. It was OBRA 1986 (which added the merchandise processing fee) that made all of the fees temporary by setting a termination date of September 30, 1989. Since then, Customs user fees have been extended five times (see table below).

CUSTOMS USER FEE EXTENSIONS		
Public Law	Bill Title	Extended fees through...
100-203	Budget Reconciliation Act of 1987	Sept. 30, 1990
101-382	Customs and Trade Act of 1990	Sept. 30, 1991
101-508	Omnibus Budget Reconciliation Act of 1990	Sept. 30, 1995
103-66	Omnibus Budget Reconciliation Act of 1993	Sept. 30, 1998
103-182	North American Free Trade Agreement	Sept. 30, 2003

Source: U.S. Code Annotated

- Customs user fees were most recently extended in 1993 (first, for five years in OBRA '93, and then for 1998-2003 as part of the NAFTA legislation). They are due to expire on September 30, 2003, and the budget baseline reflects that expiration. Therefore, any legislation Congress may consider this year that would extend Customs user fees would be scored with a reduction in outlays (remember, offsetting receipts appear in the budget as negative outlays).
- The *Bulletin* has looked back to the 107th Congress (and in the 108th so far) and found several high-profile pieces of legislation that proposed extension of Customs user fees. For example, in the 107th Congress, the Bipartisan Patient Protection Act contained an extension of Customs user fees that passed both the House and Senate, but a conference agreement was never reached. Several other pieces of legislation proposed extensions of Customs user fees (see table at top right).
- In the 108th Congress, language extending Customs user fees has appeared in the Senate-passed (H.R. 2) reconciliation bill, six proposed substitute amendments to the Senate reconciliation bill, the Senate-passed prescription drug bill, the Senate-passed refundable child credit bill, and several other pieces of legislation.

LEGISLATION CONTAINING EXTENSION OF CUSTOMS USER FEES			
Congress	Bill Number	Bill Title	Status
107 th	H.R. 7	Community Solutions Act of 2001 (CARE Act)	Reported in the Senate
107 th	H.R. 2563	Bipartisan Patient Protection Act	Passed House, Senate, no conference agreement
107 th	H.R. 4737	Personal Responsibility, Work, and Family Promotion Act of 2002	Reported in the Senate
107 th	H.R. 5095	American Competitiveness and Corporate Accountability Act of 2002	Introduced in House
107 th	S. 2737	Trade Adjustment Assistance Improvement Act of 2002	Reported in the Senate
107 th	S. 3007	Servicemembers' Tax Assistance For Noteworthy Duty Act	Introduced in the Senate
108 th	H.R. 1	Prescription Drug and Medicare Improvement Act of 2003	Passed the Senate (in conference)
108 th	H.R. 2	Jobs and Growth Tax Relief Reconciliation Act of 2003	Passed the Senate a/
108 th	H.R. 1308	Relief for Working Families Tax Act of 2003	Passed the Senate (in conference)
108 th	H.R. 2392	Relief for Working Families Tax Act of 2003	Introduced in House
108 th	H.R. 2615	Rebuild America Act of 2003	Introduced in House
108 th	S. 10	Health Care Coverage Expansion and Quality Improvement Act of 2003	Introduced in the Senate
108 th	6 amendments	Jobs and Growth Tax Relief Reconciliation Act of 2003	Introduced in the Senate

a/ This measure was enacted without a customs user fee extension, which was dropped in conference.
 Source: CBO, Congressional Record

- Why can Customs user fees be used over and over again as an offset and in many pieces of legislation simultaneously? The short answer is – because it hasn’t been enacted yet, but let’s back up a few steps. Section 308(b) of the Congressional Budget Act of 1974 directs CBO to periodically report to the House and Senate Budget Committees on the budget effects of congressional action on bills and resolutions. The Budget Committee chairmen, in turn, report on the "current level" of congressional action affecting the budget through statements printed in the Congressional Record. In budget jargon, current level represents the estimated revenue and direct spending effects of all legislation that Congress *has cleared for the President*.
- The current level reports issued by the Budget Committee chairmen compare the effects of enacted legislation to the spending ceilings and revenue floors set in the budget resolution, and are the basis for determining points of order under Section 311 of the Budget Act. Even though an offset such as Customs user fees has been included in one measure, it remains available to be used in other measures until it passes both Houses and is cleared for the President’s signature.
- Two extensions of Customs user fees are pending in two different conference committees – a ten-year extension (through September 2013) was included in the Prescription Drug and Medicare Improvement Act of 2003 passed by the Senate, and a six-and-a-half year extension (through March 2010) was included in the Relief for Working Families Tax Act of 2003 (refundable child credit bill) passed by the Senate.
- News reports have said that Ways and Means Chairman Thomas may want to use the Customs user fee extension offset for yet another measure – the Extraterritorial Income (ETI) and Foreign Sales Corporation (FSC) legislation that has yet to be reported.
- Customs user fees most likely will be extended before September 30 – the question is, who will get to keep the gift that has kept on giving, and how will all the other bills find other offsets when they lose this one?

STATES' BUDGET CRUNCH: IS IT THE FEDERAL GOVERNMENT'S FAULT?

- According to the National Conference of State Legislatures (NCSL), 36 states currently face a combined \$22 billion shortfall for fiscal year 2003. Of these, NCSL estimates that 15 states face a budget gap exceeding 5% or more of general funds. For fiscal year 2004, the aggregate budget gap is expected to approach \$80 billion in 41 states, of which 37 states would have budget gaps of 5% or more. While there is little dispute over this daunting situation, there has been wide disagreement about its causes and whether the federal government should do anything about it.
- How to apportion blame for states' fiscal distress? Because no one had projected the baseline surpluses that states would currently be enjoying if they had not experienced changes to their baseline trends (i.e., spending increases, tax cuts, a recession, and a weakening tax structure), no one knows how to rank these changes in terms of causality. Instead, most commentators resort to anecdotal evidence that focuses on changes in selected trends for the "evidence" that supports their solution for states' problems. The *Bulletin* summarizes some of the trend evidence here.
- Trends. About a decade ago, the economy began to grow rapidly, accompanied by low unemployment, rising incomes, and ever increasing investment returns. Income effects of this expansion were especially notable for those earning upper incomes and capital gains, which, combined with progressive tax rates, caused state tax revenues to skyrocket. From 1991-2000, state and local tax revenue growth averaged 7.4% annually (in nominal terms). This revenue growth gave legislators in most states the freedom to cut taxes overall by about 8.2%. Despite the resulting smaller tax bases, state revenues continued to strengthen as long as the economy prospered. On the spending side, state outlays averaged 5.6% annual growth (excluding all federal aid grants) while the GDP was averaging 6.4% yearly growth.
- By March 2001, it was apparent that the 10-year expansion had come to an end. Growth in state revenues in FY 2001 fell off compared to growth rates in previous years. In 2002, revenue actually declined by nearly 5.6% compared to 2001 receipts. State revenues were declining more rapidly than spending could be adjusted. The Bureau of Economic Analysis found that in 2002, state and local spending still grew by 4.9%.
- Unfunded Mandates. Besides these revenue fall-offs, states justify calls for new federal assistance by describing "a new era" of unfunded federal mandates, most commonly citing new, increased spending pressures from special education, No Child Left Behind, election reform, and homeland security. The NCSL claims that these four areas alone cause \$20 billion to \$80 billion in unfunded federal mandates. However, the unfunded mandates claim is thrown around all too casually because those who claim it are sloppy in their "definition" of an unfunded mandate.
- The Unfunded Mandates Reform Act of 1995 (UMRA) was developed to force Congress to recognize and consider the costs imposed by proposed legislation that includes federal mandates on state and local governments and the private sector. According to this law, a mandate is an enforceable duty imposed on any state, local, or tribal government (including any compliance costs or a prohibition on collecting any revenues). Unfunded means that any federal funding for the mandate is less than it costs other levels of governments to comply with the mandate. CBO recently released its annual report detailing federal mandates imposed since UMRA was enacted. To date, only two notable unfunded mandates have been imposed on state and local governments – the 1996 Minimum Wage Increase and the 1998 Food Stamp Administration reimbursement reductions.
- So how can states label so many other areas as new unfunded mandates? For example, states have recently cited the Individuals with Disabilities Education Act (IDEA) as an unfunded mandate. This is not a new program. States have been complaining since the mid-1970s (when the program was created) about the federal government's failure to fully follow through on its share of funding as originally contemplated in the authorization bill. Recently, Congress has reacted to this longstanding criticism by devoting more federal spending to IDEA, which can only have helped (not hurt) states as they hit the fiscal wall.
- As for No Child Left Behind, the CBO cost estimate for that legislation made it explicitly clear that there is no federal mandate. Any requirements in the bill are conditions of accepting federal dollars, which states are free to forgo if they do not want to comply with the requirements.
- Regarding homeland security, it is true Congress has passed a few laws requiring action by states in the name of homeland security (e.g., vulnerability assessment of most communities' water systems, costing \$0.9 billion, port security requirements, and public universities screening students – only some of which remain to be federally funded), which certainly do not add up to the \$18 billion that NCSL claims the federal government "owes" to states for homeland security. States seem to think that all increased police and other security activities they have decided to undertake since 9/11 are a federal responsibility that has thus far gone unreimbursed.
- Only election reform is a significant new federal mandate, but states cannot claim it is unfunded yet. CBO estimates these reforms could cost states up to \$3.5 billion over the 2003-2007 period (average of \$0.7 billion per year). The federal government is ahead of the game in fully funding this mandate. The 2003 Omnibus appropriations bill provided \$1.5 billion for states – sufficient to cover the authorized costs for 2003.
- Tax Structure. There is one underappreciated structural problem that has been pinpointed by the National Governors Association as the major cause (along with exploding health care costs) of states' current difficulty. States' tax bases and tax systems have been eroding with the shrinking incidence of sales taxes, as the economy has shifted to producing more services than goods and as some remaining goods escape sales taxes. But the revenue windfall from wealthy taxpayers in the 1990s had disguised the emerging problem.
- What To Do? Despite mixed signals of economic recovery on the national level, both federal and state revenues have yet to show signs of any recovery. To help keep their budgets afloat, legislators in many states have depleted "rainy day" funds by more than two thirds since 2001, and now have little choice but to reduce spending further or find ways to increase revenue. Because every state except Vermont has a constitutional balanced budget requirement, states have been forced to make changes to their 2003 budgets to respond to growing budget gaps. Meanwhile, some 2004 budgets are still being crafted to include tax increases.
- In the meantime, Congress decided to provide \$20 billion in assistance to states in the Jobs and Growth bill enacted in May. This assistance, however, is not likely to put an end to demands for further federal assistance later this year. Congress ought to evaluate such demands with an understanding of the real reasons states are facing budget pressures.