

Statement of  
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before the  
Committee on Energy and Commerce  
U. S. House of Representatives

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**NOTICE:**

This statement is not available for public release until it is delivered at 10:00 a.m. (EST), Wednesday, January 29, 1986.

Mr. Chairman, I am pleased to have the opportunity to testify on our experience in implementing the provisions of the Balanced Budget and Emergency Deficit Control Act of 1985 (P.L. 99-177)--or, more briefly, the Balanced Budget Act. My statement this morning will cover the highlights of the joint CBO/OMB sequestration report to the Comptroller General.

#### JOINT CBO/OMB SEQUESTRATION REPORT

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The Balanced Budget Act establishes an automatic spending reduction procedure if the federal deficit is estimated by OMB, CBO, and GAO to exceed certain specified amounts. The maximum deficit amounts decrease each year from \$171.9 billion for fiscal year 1986 to zero for 1991. Any necessary spending reductions are to be accomplished through the sequestration of budgetary resources. Except for trust and special funds, this involves permanently cancelling new budget authority and other spending authority to obligate and expend funds. For 1986, the outlay reduction is limited by the Act to a maximum of \$11.7 billion, regardless of the amount of the excess deficit. In later years, the amount of possible outlay reductions is not limited.

The first step in the sequestration process is a joint report by the Directors of CBO and OMB to the Comptroller General that estimates budget base levels and calculates the amounts of budgetary resources to be sequestered. Our report for 1986 was delivered on January 15, as required by the Act. It was also published in the Federal Register on that date.

The CBO/OMB report covers 418 pages, most of which are budget account listings. There is also a 20-page summary at the beginning of the report that we have had printed separately and have distributed to Members of this Committee. This summary provides a good description of our sequestration calculations, and I would like to go through a number of its tables quickly to highlight the major features.

**BASE LEVEL BUDGET ESTIMATES**

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Table I of our report summary shows the CBO and OMB base level estimates for 1986. Our deficit estimates are remarkably close--within \$800 million of each other. The average of the two deficit estimates is \$220.5 billion, which exceeds the \$171.9 billion maximum deficit amount by \$48.6 billion. This is far more than enough to invoke the full amount of the \$11.7 billion spending reduction established by the Balanced Budget Act.

**TABLE 1. BUDGET BASE LEVELS FOR 1986**  
(In billions of dollars)

Budget Aggregates	OMB Estimates	CBO Estimates	Average
Revenues	774.9	777.2	776.0
Outlays	994.9	998.0	996.5
Deficit	220.1	220.9	220.5

**SOURCES:** Congressional Budget Office and Office of Management and Budget.

The CBO base level deficit estimate is \$220.9 billion, which is \$26.2 billion higher than the \$194.6 billion deficit estimate we made last November for the conference committee on H.J. Res. 372. The November estimate was based on our August economic forecast, tax and spending laws in effect at that time, and 1985 appropriation levels. Our latest deficit estimate is based on a new economic forecast, tax and spending laws as of January 10, 1986, and 1986 appropriation levels.

Approximately \$10 billion of the higher CBO deficit estimate can be attributed to changes in our economic forecast for 1986. These changes result in somewhat lower revenues and a very slight change in net interest costs. The remaining \$16 billion increase can be attributed to Congressional legislative actions and to technical reestimates of spending. The largest change in outlay estimates is for agriculture programs, primarily CCC farm price support programs (+\$10.0 billion). The farm bill passed in December added \$2 billion to \$3 billion to estimated 1986 outlays, and lower farm commodity prices have led to a sharp upward revision in our spending estimates by \$7 billion to \$8 billion. The other major change in our outlay estimates is for national defense programs (+\$7.7 billion). The 1986 appropriation level is somewhat higher than for 1985, which adds roughly \$4 billion in outlays. The rest is a technical reestimate based on the faster spending rates for defense programs that have occurred since July.

#### ECONOMIC ASSUMPTIONS

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Table 2 of the report shows the latest CBO and OMB economic assumptions for fiscal year 1986. As would be expected from the closeness of our budget

TABLE 2. ECONOMIC ASSUMPTIONS (Fiscal Year 1986)

Economic Variable	OMB	CBO
<b>Gross National Product:</b>		
Current dollars (in billions of dollars)	4,209	4,192
Percent change, year over year	6.9	6.5
Constant (1982) dollars (in billions of dollars)	3,675	3,658
Percent change, year over year	3.5	3.0
GNP Implicit Price Deflator (percent change, year over year)	3.3	3.4
CPI-W (percent change, year over year)	3.3	3.3
Civilian Unemployment Rate (percent, fiscal year average)	6.9	6.9
Interest Rates (fiscal year average)		
91-day Treasury bills	7.3	6.9
10-year Treasury notes	9.2	9.2

SOURCES: Congressional Budget Office and Office of Management and Budget.

estimates, our economic assumptions for the major variables are quite similar.

The Balanced Budget Act requires CBO and OMB to include in our joint report real economic growth rates for each quarter of the relevant fiscal year, and the last two quarters of the preceding fiscal year. Our projections for fiscal year 1986 and the last two quarters of fiscal year 1985 are provided in Table 3 of the report. If either CBO or OMB project real economic growth to be less than zero for any two consecutive quarters, or if the Department of Commerce reports actual real growth to be less than

TABLE 3. REAL ECONOMIC GROWTH RATES BY QUARTER  
(In percents, annual rates)

	FY 1985 Actual <sup>a/</sup>		FY 1986 Estimates			
	Apr-Jun 1985	Jul-Sep 1985	Oct-Dec 1985	Jan-Mar 1986	Apr-Jun 1986	Jul-Sep 1986
OMB	1.1	3.0	4.2	4.0	4.0	4.0
CBO	1.1	3.0	3.2 <u>a/</u>	3.5	3.3	3.4

SOURCES: Congressional Budget Office and Office of Management and Budget.

a. As reported by the Department of Commerce (December 20, 1985).

1 percent for two consecutive quarters, many of the provisions of the Act could be suspended by the Congress, including a sequestration order if it has not already gone into effect. As you can see in Table 3, however, both CBO and OMB are projecting real growth in the 3 percent to 4 percent range, and actual growth for the last two quarters as reported by the Department of Commerce has been above 1 percent.

#### SEQUESTERABLE RESOURCES

Table 4 of the report summary provides further detail on the CBO and OMB base level outlay estimates for 1986. This table shows that a relatively small portion of 1986 outlays will be affected by the sequestration of budgetary resources. About \$110 billion of estimated 1986 outlays for defense programs, or 40 percent of total defense spending, are associated with budgetary resources subject to an across-the-board percentage

TABLE 4. BASE LEVEL OUTLAY ESTIMATES FOR 1986  
(In billions of dollars)

Category	OMB Estimates	CBO Estimates	Average
<b>Defense Programs a/</b>			
Subject to across-the-board reduction	106.2	112.4	109.3
Other b/	<u>164.7</u>	<u>162.1</u>	<u>163.4</u>
Subtotal, defense programs	270.9	274.6	272.8
<b>Nondefense Programs</b>			
Programs with automatic spending increases c/	48.9	48.4	48.6
Certain special rule programs d/ Subject to across-the-board reduction	87.0	87.1	87.1
Major exempt programs	104.3	106.1	105.2
Social security and railroad retirement tier 1	202.6	202.0	202.3
Net interest	137.9	136.9	137.4
Earned income tax credit	1.3	1.3	1.3
Low-income programs e/	60.9	61.1	61.0
Veterans compensation and pensions	14.3	14.3	14.3
State unemployment benefits	18.2	18.1	18.2
Offsetting receipts	-50.2	-50.5	-50.4
Other f/	<u>98.8</u>	<u>98.7</u>	<u>98.8</u>
Subtotal, nondefense programs	724.0	723.4	723.7
<b>Total</b>	<b>994.9</b>	<b>998.0</b>	<b>996.5</b>

SOURCES: Congressional Budget Office and Office of Management and Budget.

- a. Budget function 050 excluding FEMA programs.
- b. Outlays from obligated balances and the portion of military personnel accounts exempted by the President for 1986.
- c. Primarily federal employee retirement and disability programs.
- d. Guaranteed student loans, foster care and adoption assistance, medicare, veterans medical care, community health, migrant health, and Indian health.
- e. AFDC, child nutrition, medicaid, food stamps, SSI, and WIC.
- f. Outlays from prior-year appropriations, certain prior legal obligations, and small exempt programs.

reduction. The special 1986 exemption for military personnel accounts made by the President removed more than \$60 billion in outlays from the sequesterable portion.

About \$240 billion, or one-third of estimated outlays for nondefense programs, is associated with sequesterable budgetary resources. Nearly \$50 billion are for programs with automatic spending increases, primarily military and federal civilian employee retirement and disability programs. For these programs, the amount of spending reduction required by the Act is limited to the cost-of-living adjustments, which were generally 3.1 percent for 1986.

Another \$87 billion in nondefense outlays are associated with certain special rule programs, of which the largest is Medicare. The Act also limits the extent of spending reductions for these programs; for example, 1 percent for Medicare in 1986 and not more than 2 percent in future years. Only slightly more than \$100 billion in 1986 nondefense outlays--about 15 percent--are associated with budgetary resources subject to an across-the-board percentage reduction. Over \$380 billion--or more than one-half of total estimated outlays for nondefense programs--are entirely exempt from sequestration by the Act. As shown by Table 4, these exempt outlays are mostly Social Security benefits and net interest costs.

#### SEQUESTRATION CALCULATIONS

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Table 5 of the report summary provides the major elements of our sequestration calculations. Although the sequestration actually applies to



TABLE 5. SEQUESTRATION CALCULATIONS FOR 1986  
(Outlays in millions of dollars)

Category	OMB	CBO	Average
<b>Defense Programs:</b>			
Total required reductions	5,850	5,850	5,850
Estimated savings from automatic spending increases:			
Indexed retirement programs <u>a/</u>	496	497	497
Amount remaining to be obtained from uniform percentage reductions of budget resources	5,354	5,353	5,353
Estimated outlays associated with sequesterable budget resources	106,225	112,446	109,335
Uniform reduction percentage	5.0	4.8	4.9
<b>Nondefense Programs:</b>			
Total required reductions	5,850	5,850	5,850
Estimated savings from automatic spending increases:			
Indexed retirement programs	496	497	497
Other indexed programs	45	45	45
Estimated savings from the application of special rules:			
Guaranteed student loans	10	10	10
Foster care and adoption assistance	5	5	5
Medicare	300	300	300
Other health programs	82	83	82
Amount remaining to be obtained from uniform percentage reductions of budget resources	4,912	4,911	4,912
Estimated outlays associated with sequesterable budget resources <u>b/</u>	114,444	115,080	114,762
Uniform reduction percentage	4.3	4.3	4.3

SOURCES: Congressional Budget Office and Office of Management and Budget.

- a. These retirement programs are not included in the national defense function of the budget; most are included in the income security function.
- b. Includes estimated 1987 outlays for the Commodity Credit Corporation (CCC) that can be affected by a 1986 sequester (see discussion of special rule for the CCC). The OMB estimate is \$10,095 million, the CBO estimate is \$8,940 million, and the average is \$9,518 million.

new budget authority and other spending authority, the calculations use outlay estimates to determine the amount of sequestration.

The first step is to divide the amount of required deficit reduction--\$11.7 billion for 1986--into two halves. One-half--\$5,850 million--is assigned to defense programs (budget accounts in function 050) and the other half to nondefense programs.

Second, the total amount of outlay savings from eliminating automatic spending increases is calculated. One-half of the resulting savings for indexed retirement and disability programs are applied to the required reduction in defense programs and one-half to nondefense programs. This amounts to an estimated \$994 million for 1986, so that \$497 million is subtracted from the \$5,850 million required reduction for both defense and nondefense programs.

Various additional calculations are made for nondefense programs. These include the savings that can be obtained by eliminating automatic spending increases in three other specific programs--the National Wool Act, the special milk program, and vocational rehabilitation grants. Also included are savings that are to be obtained by applying special rules for guaranteed student loans, foster care and adoption assistance, Medicare, and certain health programs. These estimated savings amount to another \$442 million, which is also subtracted from the \$5,850 million required reduction in nondefense outlays.

This leaves \$5,353 million for defense programs and \$4,912 million for nondefense programs to be obtained by an across-the-board uniform percentage reduction in budgetary resources. The uniform percentages are calculated by dividing these dollar amounts by total estimated 1986 outlays associated with sequesterable budgetary resources. For defense programs, the sequesterable outlay base is \$109.3 billion. For nondefense programs, the base is \$114.8 billion, which includes \$9.5 billion of 1987 outlays for farm price support programs that can be affected by the 1986 sequestration. The resulting percentages are 4.9 percent for defense programs, and 4.3 percent for nondefense programs. These percentages are then applied to the new budget authority and other spending authority in the sequester base.

Had the President not exempted the bulk of the military personnel accounts from sequestration, the uniform percentage reduction for defense programs would have been 3.1 percent. Similarly, had the Balanced Budget Act not limited the maximum 1986 deficit reduction to \$11.7 billion, so that the full \$48.6 billion excess deficit would have to be removed, the uniform reduction percentages would have been 21.8 percent for defense programs (assuming the exemption of the military personnel accounts) and 20.3 percent for nondefense programs.

The required reductions in spending authority of various types are summarized in Tables 7, 8, and 9 in the report. The required reductions in more than 800 separate budget accounts, and in 4,000 defense programs, projects, and activities are itemized in the Federal Register. For defense

TABLE 7. DEFENSE PROGRAM SEQUESTRATIONS FOR 1986  
(In billions of dollars)

Function 050	Spending Authority <u>a/</u>	Estimated Outlays
Department of Defense-Military:		
Military personnel	0.2	0.2
Operation and maintenance	3.9	2.9
Procurement	6.6	0.9
Research, development, test, and evaluation	1.9	0.9
Military construction	0.5	0.1
Family housing and other	<u>0.2</u>	<u>0.1</u>
Subtotal, DoD	13.3	5.1
Atomic energy defense activities	0.4	0.2
Other defense-related activities <u>b/</u>	0.1	<u>c/</u>
Total	13.8	5.4

SOURCES: Congressional Budget Office and Office of Management and Budget.

- a. Includes new budget authority for 1986 and unobligated balances from budget authority provided in previous years.
- b. Includes the function 050 portion of Federal Emergency Management Agency budget accounts which are reduced at the same rate as nondefense programs.
- c. Less than \$50 million.

TABLE 8. NONDEFENSE PROGRAM SEQUESTRATIONS FOR 1986  
(In billions of dollars)

Function	Spending Authority <u>a/</u>	Direct Loan Obligations	Loan Guarantees	Estimated Outlays
International affairs	0.9	0.3	0.5	0.5
General science, space and technology	0.4	---	---	0.3
Energy	0.3	0.2	0.1	0.1
Natural resources and environment	0.6	<u>b/</u>	---	0.4
Agriculture	0.9	0.7	0.3	1.0 <u>c/</u>
Commerce and housing credit	0.2	0.2	5.7	0.2
Transportation	1.9	<u>b/</u>	<u>b/</u>	0.4
Community and regional development	0.2	0.1	<u>b/</u>	0.1
Education, training, employment, and social services	1.2	<u>b/</u>	---	0.4
Health	0.5	<u>b/</u>	---	0.3
Medicare	0.4	---	---	0.4
Income security	1.8	<u>b/</u>	---	1.3
Social security	0.1	---	---	0.1
Veterans benefits and services	0.2	<u>b/</u>	0.5	0.2
Administration of justice	0.3	---	---	0.3
General government	0.3	---	---	0.3
General purpose fiscal assistance	0.3	---	---	0.2
Total	10.5	1.6	7.3	6.3

SOURCES: Congressional Budget Office and Office of Management and Budget.

- a. Includes new budget authority, obligation limitations, and other spending authority for 1986.
- b. Less than \$50 million.
- c. Includes \$0.4 billion in estimated 1987 outlay savings for Commodity Credit Corporation (CCC) programs (see discussion of special rule for CCC).

TABLE 9. SEQUESTRATIONS FOR 1986 BY AGENCY  
(In billions of dollars)

Department or Other Unit	Spending Authority <u>a/</u>	Direct Loan Obligations	Loan Guarantees	Estimated Outlays
Legislative Branch	0.1	---	---	0.1
The Judiciary	<u>b/</u>	---	---	<u>b/</u>
Executive Office of the President	<u>b/</u>	---	---	<u>b/</u>
Funds appropriated to the President	0.6	0.3	<u>b/</u>	0.3
Agriculture	1.3	1.1	0.5	1.3 <u>c/</u>
Commerce	0.1	<u>b/</u>	<u>b/</u>	0.1
Defense-Military	13.3	---	---	5.1
Defense-Civil	0.6	---	---	0.5
Education	0.7	<u>b/</u>	---	0.2
Energy	0.6	---	---	0.3
Health and Human Services	1.3	<u>b/</u>	---	1.0
Housing and Urban Development	0.7	<u>b/</u>	5.5	<u>b/</u>
Interior	0.3	<u>b/</u>	<u>b/</u>	0.2
Justice	0.2	---	---	0.1
Labor	0.4	---	---	0.2
State	0.1	<u>b/</u>	---	0.1
Transportation	1.8	<u>b/</u>	<u>b/</u>	0.4
Treasury	0.4	---	---	0.4
Environmental Protection Agency	0.1	<u>b/</u>	---	<u>b/</u>
General Services Administration	0.1	---	---	<u>b/</u>
National Aeronautics and Space Administration	0.3	---	---	0.2
Office of Personnel Management	0.6	---	---	0.6
Small Business Administration	<u>b/</u>	0.1	0.2	<u>b/</u>
Veterans Administration	0.2	<u>b/</u>	0.5	0.2
Other independent agencies	<u>0.4</u>	<u>0.1</u>	<u>0.5</u>	<u>0.3</u>
Total	24.3	1.6	7.3	11.7

SOURCES: Congressional Budget Office and Office of Management and Budget.

- a. Includes new budget authority for 1986, unobligated balances from budget authority provided in previous years (Defense-Military and other function 050 programs and certain administrative costs), obligation limitations for and other spending authority for 1986.
- b. Less than \$50 million.
- c. Includes \$0.4 billion in estimated 1987 outlay savings for Commodity Credit Corporation (CCC) programs (see discussion of special rule for CCC).

programs in function 050, the required reduction in spending authority (new budget authority and unobligated balances) amounts to \$13.8 billion to achieve outlay savings of \$5.4 billion. This defense outlay reduction is lower than one-half of the \$11.7 billion required reduction because the savings from eliminating automatic spending increases for federal retirement programs--including military retirement--are counted in the income security function and are shown in the nondefense savings table.

For nondefense programs, the required reduction in spending authority is \$10.5 billion, \$1.6 billion in direct loan obligations, and \$7.3 million in new loan guarantee commitments. These reductions are estimated to produce \$6.3 billion in outlay savings, including \$0.4 billion in estimated 1987 outlay savings for Commodity Credit Corporation (CCC) programs. In most instances, additional outlay savings will be gained in 1987 and later fiscal years as the result of eliminating the 1986 cost-of-living adjustments and cancelling 1986 budget authority. We did not calculate these outlay savings for our report to the Comptroller General, but a rough CBO estimate for the 1987 savings is \$7 billion to \$8 billion.