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The Budget for Fiscal Year 2003

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SUMMARY

On January 29, 2003, Congress cleared the seventh in a series of continuing resolutions (CRs) on appropriations for fiscal year (FY) 2003. P.L. 108-4 funds the activities covered by the not-yet-adopted 11 regular appropriations through February 7, 2003. Two of the 13 regular appropriations bills (Defense and Military Construction) became law in the second half of October. An omnibus appropriations bill (H.J.Res. 2) to combine the remaining appropriations is in conference. None of the 13 regular appropriations had become law when FY2003 began, necessitating the CRs. (CRs generally provide funding at FY2002 levels for those activities without a regular appropriations.)

The Administration's FY2004 budget (submitted February 2003), reflecting the dramatic change in the budget outlook over the last 18 months, put the FY2003 deficit of $304 billion, up from the $80 billion in the Administration's original proposals. The Congressional Budget Office's (CBO) January 2003 budget report had an FY2003 deficit of $199 billion.

The President released his original budget proposals for FY2003 on February 4, 2002, shortly after the release of the CBO annual budget report at the end of January. The budget balance without the effect of the President's proposals (the baseline), showed a small surplus ($41 billion) from the Administration and a small deficit ($14 billion) from CBO.

The President's FY2003 budget proposed tax cuts and spending increases to stimulate the economy, rapid increases in defense and homeland security spending, and little growth in other areas of discretionary spending.

In early March 2002, CBO released updated reestimates of the President's policy proposals using CBO's economic and technical assumptions. The CBO estimates of the Administration's policy proposals produced a deficit of $121 billion for FY2003.

The Bush Administration's early 2002 economic stimulus proposal was superseded by stimulus legislation adopted by Congress on March 7, 2002 (The Job Creation and Worker Assistance Act of 2002; H.R. 3090-/P.L. 107-147), that would increase the deficit (from baseline levels) by a then estimated $43 billion in FY2003.

The House Budget Committee adopted its version of the FY2003 budget resolution, H.Con.Res. 353, on March 13, 2002. The House passed the resolution on March 20. The resolution contained a deficit of $46 billion for the year. Like the President's budget, much of the focus in the resolution was on funding for the war on terrorism and for homeland security.

The Senate Budget Committee reported its version of the FY2003 budget resolution (S.Con.Res. 100) on March 22. Its provisions for defense and homeland security were similar to (but not the same as) those in the House resolution and the President's budget. The Senate never considered the budget resolution.

The deficit in FY2002 and the one expected in FY2003 would be the first since FY1997. The weak economy, changes in underlying technical components of the budget estimates, the government's budgetary response to the terrorist attacks in the fall of 2002, and the tax cut adopted in June 2001 contributed to the expected elimination of the previously forecast surpluses.

Most Recent Developments

The President's February 2003 and CBO's January 2003 budget reports (for FY2004) reflected the deterioration in the budget outlook for FY2003 over the last year. Including its proposed policies (which will have some effect on FY2003), the Administration's budget raised the estimated FY2003 deficit to $304 billion (or $264 billion without the policy changes). CBO's baseline estimates that the FY2003 deficit will be $199 billion under current policies (no tax cuts, no spending increases, no costs associated with a war with Iraq).

Congress adopted the seventh continuing resolution (CR) on appropriations (P.L. 108-4) providing funding (mostly at FY2002 levels) for federal activities not otherwise funded through February 7, 2003. A resolution providing funding for the 11 remaining appropriations (H.J.Res. 2) is currently in conference. (One or two more CRs may be needed to ensure funding before the remaining appropriations are adopted.) The delays in adopting the 13 regular appropriations bills before and since the start of fiscal year FY2003 made the series of CRs necessary. Congress began considering the appropriations bills for the new fiscal year in the summer of 2002. As the new fiscal year approached, none of the regular appropriations bills had cleared Congress. Since the beginning of the new fiscal year, Congress has adopted two of the 13 regular appropriations bills, Defense (P.L. 107-248; October 23) and Military Construction (P.L. 107-249; October 23). Congress is in early consideration of omnibus appropriations measure that would roll the remaining 11 appropriations into one large bill.

Background and Analysis

Presidents generally submit their budget proposals for the upcoming fiscal year early in each calendar year. The Bush Administration presented its FY2003 budget documents on February 4, 2002. The budget documents contained extensive and detailed budget related information, including estimates of the budget without the proposed policy changes (current service baseline estimates), historical budget data, detailed outlay and receipt data, selected analysis of specific budget related topics, and the Administration's economic forecast. These detailed budget documents are an annual basic reference source for federal budget information in addition to their use as a transmitter of the Administration's policy proposals.

The Administration's annual budget submission is followed by congressional action on the budget. This usually includes the annual budget resolution, appropriations, and, possibly, a reconciliation bill or bills. During the months of deliberation on budget related legislation, the Administration often modifies its proposals, not only because of interactions with Congress, but because of changing circumstances in the economy and the world.

Budget Totals

The annual budget cycle provides the President and Congress with the opportunity to set policy for the upcoming fiscal year and to partially determine policy in subsequent years.

The decisions made for this year can and often do have repercussions for years into the future. Last year's tax cut (the Economic Growth and Tax Relief Reconciliation Act of 2001 – EGTRRA; P.L. 107-16; June 7, 2001) will change federal revenues in each year through 2010, when most of its provisions are scheduled to sunset. Although they are provided each year in appropriations bills, changes in the level of discretionary spending this year influences future levels of discretionary spending.

Table 1. Budget Proposals and Estimates for FY2003 (and FY2002)

(in billions of dollars)

	Receipts	Outlays	Deficit(-)/ Surplus
Actual for FY2001	*1,991*	*1,864*	*127*
*CBO Budget Outlook for **FY2002** 1/31/02*	*1,983*	*2,003*	*-21*
*President's Budget for **FY2002** 2/4/02*	*1,946*	*2,052*	*-106*
*President's Budget for **FY2002** baseline 2/4/02*	*2,011*	*2,020*	*-9*
*CBO revised baseline for **FY2002** 3/6/02*	*2,006*	*2,001*	*5*
*CBO estimate of President's Budget for **FY2002** 3/6/02*	*1,942*	*2,033*	*-90*
*House budget resolution for **FY2002** 313/02*	*1,968*	*2,033*	*-66*
*OMB MSR **FY2002** 7/15/02*	*1,867*	*2,032*	*-165*
*OMB MSR baseline**FY2002** 7/15/02*	*1,868*	*2,018*	*-150*
*CBO Update for **FY2002** 8/27/02*	*1,860*	*2,017*	*-157*
Actual for FY2002	*1,853*	*2,011*	*-158*
CBO Budget Outlook for **FY2003** 1/31/02	2,070	2,085	-14
President's Budget for **FY2003** 2/4/02	2,048	2,128	-80
President's Budget for **FY2003** *baseline* 2/4/02	2,121	2,070	51
CBO revised baseline for **FY2003**[a] 3/6/02	2,086	2,080	6
CBO estimate of President's Budget for **FY2003** 3/6/02	2,013	2,134	-121
House budget resolution for **FY2003** 3/20/02	2,077	2,122	-46
Senate Budget Committee for **FY2003** 3/22/02	2,046	2,139	-92
OMB MSR **FY2003** 7/15/02	2,029	2,138	-109
OMB MSR baseline **FY2003** 7/15/02	2,035	2,097	-62
CBO Update 8/27/02	1,962	2,107	-145
CBO Budget Outlook 1/31/03	1,922	2,121	-199
President's Budget for FY2004 2/3/03	1,836	2,140	-304

MSR – Mid-session review

a. These numbers exclude the effects of the economic stimulus law (P.L. 107-147) enacted on March 9, 2001.

Table 1 contains budget estimates and proposals for FY2002 and FY2003 from the CBO, the Administration (OMB), and, as they become available, budget proposals and estimates from Congress. Differences in totals occur because of differing underlying economic, technical, and budget-estimating assumptions and techniques as well as differences in policy proposals. Most *policy* differences between the Administration and various congressional proposals for the upcoming fiscal year are often relatively small in dollars compared to the budget as a whole. These often small changes, reflecting differing policy choices, may have large implications for the shape and content of the budget over extended time periods. As the budget works its way through Congress, budget totals will almost certainly change from the amounts originally proposed.

Budget Proposals and Estimates

Budget proposals and estimates depend on underlying assumptions about the economy, technical components and relationships within the budget estimating models, and assumptions about proposed and assumed current and future government policy. For FY2004 and for the remainder of FY2003, both the expected underlying economic conditions and the policy directions appear somewhat more unsettled than usual. The lack of resolution in discretionary funding for FY2003, the sluggish economy, and the possible war with Iraq contributed to the current uncertainty.

CBO's initial budget report for FY2003, the *Budget and Economic Outlook: Fiscal Years 2003-2012* (January 2002), contained baseline estimates and projections for FY2002 through FY2012.[1] CBO estimated that without any changes from current policy, the FY2003 budget would have $2,070 billion in revenues, $2,085 billion in outlays, with a (rounded) deficit of $14 billion. Over the 10-year forecast period (FY2003 - FY2012) CBO's projections produce a cumulative surplus of $2,263 billion. Of that amount, $1,078 billion is generated in the last two years of the projection period when the 2001 tax cuts would fully sunset as required by current law.[2] The 5-year (FY2003 - FY2007) cumulative surplus, reflecting the deficits and relatively small surpluses expected over this period, is $437 billion.

President Bush's FY2003 budget proposed receipts of $2,048 billion, outlays of $2,128 billion, with a resulting deficit of $80 billion. The Administration's proposals produced a 10-year total cumulative surplus of $1.0 trillion. Its 5-year cumulative surplus was $157 billion. (The President's budget provided most data for the 5-year period, FY2003 through FY2007; the budget provided very little data for either the individual years beyond FY2007 or cumulatively for the 10-year period, FY2003 through FY2012.)

The Administration's current services baseline estimates (the Administration's estimate of what the budget numbers would be without policy changes) show FY2003 receipts of $2,121 billion, outlays of $2,080 billion, with a resulting surplus of $41 billion.[3] The differences between these baseline numbers and the proposed amounts measure the dollar effect on the budget, in FY2003, of the Administration's proposals. The proposals would increase outlays by $58 billion, reduce receipts by $73 billion, and move the current services

[1] Baseline estimates provide a foundation from which to measure proposed policy changes. They extrapolate current policies into the future based on expectations of the future economy and other factors that affect the budget formulated under fairly explicit rules. They are not meant to predict future budget outcomes.

[2] CBO estimated that extending the expiring provisions immediately would reduce cumulative revenues over the 10year period by $735 billion. The implication is that the cumulative surplus over the 10-years would be reduced by at least that much and probably more if higher interest costs are included.

[3] The Administration also produced a variant of the standard baseline. The alternative assumed that the increased (mostly) emergency spending in FY2002 flowing from the September 11, 2001 terrorist attacks was a one-time event and would not be repeated. Making this assumption increases the baseline surplus to $51 billion in FY2003. The Administration measured its policy against this altered baseline. This report uses the standard baseline.

baseline from a $41 billion surplus to an $80 billion deficit. Over the FY2003 through FY2007 period, the time period covered by the Administration's baseline estimates, they show a cumulative surplus of $668 billion, meaning that the Administration's proposals reduce the cumulative baseline surplus by $511 billion over the 5 years.

CBO's estimate of the Administration's proposals (*An Analysis of the President's Budgetary Proposals for Fiscal Year 2003*, March 2002), using CBO's economic and technical assumptions, raises the estimated deficit for FY2003 (from the Administration's proposed $80 billion) to $121 billion. CBO's reestimates reduce revenues by $35 billion and increase outlays by $6 billion from the Administration's numbers, producing the $41 billion difference in the deficit estimate.

The CBO report also included updated CBO's baseline estimates that made relatively small changes in the estimates for FY2003. The updated numbers show a surplus of $6 billion for FY2003, instead of the $14 billion deficit estimated in January. Most of the change occurred because of higher expected revenues ($15 billion) and slightly smaller expected outlays ($5 billion).[4] Expectations of better short-term economic conditions produced most of the improvement in the budget outlook.[5] Over the 10-year CBO forecast period, the changes increased the cumulative surplus from $2,263 billion to $2,380 billion, a 5% increase over the January cumulative surplus estimate.

The House passed budget resolution (H.Con.Res. 353; March 20, 2002) followed, in general, the policy lead of the President's budget. Using the same underlying budget assumptions as the Administration, the resolution had revenues of $2,077 billion, outlays of $2,123 billion, with a deficit of $46 billion. The resolution, like the President's budget, contained estimates and projections for 5 years, through FY2007. The resolution expected the government to return to a small surplus in FY2004. Over the 5-year period, the resolution produced a cumulative surplus of $231 billion.

The Senate Budget Committee reported its version of the FY2003 budget resolution (S.Con.Res. 100; S.Rept. 107-141) on March 22. Using CBO's underlying assumptions (rather than the Administration's), the Senate Budget Committee resolution provided similar amounts of funding in FY2003 for defense and homeland security as the House-passed resolution but differed in other areas. Total revenues were $2,046 billion, total outlays were $2,139 billion, and the resolution had a deficit of $92 billion (most of the difference between the House and Senate Budget Committees' total for FY2003 was from differences in the underlying assumptions used rather than major policy differences in FY2003).

The Mid-Session Review (MSR) from the Administration forecast a fairly rapid recovery for both the economy and federal revenues. Under the assumptions and policy choices in the MSR, the deficit would decline from FY2002 to FY2003 (from $165 billion

[4] CBO estimates that incorporating the effects of the economic stimulus package signed into law (P.L. 107-147) on March 9, 2002, (and not included in CBO's revised baseline) produces a $40 billion deficit in FY2003.

[5] The $20 billion improvement in the budget balance represents only 1% of total receipts or outlays for the year. Relatively small changes in the underlying factors supporting the budget estimates can easily change receipts or outlays by larger amounts than this without any change in policy.

to $109 billion) and return to surplus in FY2005. Under baseline assumptions, the budget would return to surplus in FY2004. CBO's August *Update* had access to newer and revised budget and economic data than did OMB. CBO's baseline estimates put the FY2003 deficit at $145 billion, somewhat smaller than its FY2002 deficit estimate of $157 billion. It expects the budget to return to surplus in FY2006, assuming no change from existing policies.

The continuing economic weakness, along with various budget pressures, raised the expected deficits for FY2003 and subsequent years above the levels expected in the previous budget reports from August 2002. The results showed themselves in the early-2003 budget reports from both OMB and CBO. The FY2004 budget report from CBO (January 31, 2003) and the President's FY2004 budget proposal (February 3, 2003) drew a much darker short-term picture of the budget. CBO's baseline expects a $199 billion deficit in FY2003, with a return to surplus (as long as policy remains unchanged) in FY2007. The Administration's budget, incorporating the President's policy proposals, has a $304 billion deficit in FY2003, with no return to surplus before FY2009.

Part of the annual budget debate's intensity results from the awareness that the decisions made for this year affect, in some cases substantially, the funding levels or policy choices available to Congress in future years.

Uncertainty in Budget Projections

All budget estimates and projections are inherently uncertain. Their dependence on assumptions that are themselves subject to substantial uncertainty and variation makes budget estimates and projections susceptible to fairly rapid and dramatic changes. Nonetheless, budget estimates can help differentiate the budgetary effects of alternative proposals and the approximate magnitudes of various policy proposals even if the estimates do not match the actual outcomes.

The uncertainty of budget estimates was apparent over the last year. The estimates for the just ended fiscal year, 2002, produced early in 2001, projected baseline surpluses of between $283 billion (OMB) and $313 billion (CBO). The Administration's FY2002 proposals (February 2001), included a combination of tax cuts and spending increases that produced a surplus of an estimated $231 billion. By the time the summer 2002 budget estimates were released (the OMB MSR and the CBO Update), they showed baseline *deficits* of $150 billion to $157 billion in FY2002. The actual deficit for that year was $158 billion. The large baseline surpluses expected early in 2001 evaporated in a weak economy, the June 2001 tax cut, the spending increases in response to the terrorist attacks of September 2001, and substantial changes in the technical components and relationships underlying the budget estimates.

The unavoidable inaccuracy of budget projections is also obvious over longer periods of time. As CBO stated in its January 2002 budget report,

> Uncertainty compounds as the projection horizon lengthens. Even small annual differences in the many key factors that influence the budget projections – factors such as inflation, increases in productivity, economic growth, the distribution of income, and

growth rates from Medicare and Medicaid spending – can add to substantial differences in the budget outcome 10 years from now.[6]

Budget projections are dependent on underlying assumptions about the direction of the economy, future government policy, and the technical assumptions of the budget models, and how these interact. Any deviation from expected underlying assumptions, such as faster or slower economic growth, higher or lower inflation, changes in assumed spending and tax policy or alterations in the fundamental underlying relationships between the budget and economic variables (and the underlying technical assumptions) can have substantial effects on the budget projections.

Budget Action

Congress passed an economic stimulus bill in early March 2002. The legislation, the Job Creation and Worker Assistance Act of 2002 (P.L. 107-147; March 9, 2002) increased FY2003's expected deficit by an estimated $43 billion (plus another $3 billion in higher interest costs). The legislation, passed as an economic stimulus package, extended unemployment benefits, reduced selected business taxes, extended selected expiring tax provisions, and made miscellaneous technical corrections to the tax code.

The House Budget Committee approved its version of the annual concurrent resolution on the budget for FY2003 (H.Con.Res. 353) on March 13, 2002. The resolution used a slightly modified version of OMB's economic and technical assumptions rather than CBO's. Like the President's budget this year, the resolution extended its projections 5 years into the future rather than the 10 years that had been used in the last few years.

The resolution had a $46 billion deficit for FY2003 that closely matched the estimated cost of the economic stimulus bill adopted days earlier. It included almost $28 billion in unspecified tax cuts over 5 years (with upper limits for the size of the cuts for each year), a $46 billion year-over-year increase in budget authority for defense, close to a doubling of funding for homeland security between FY2002 and FY2003, and very small increases (overall) for remaining discretionary spending. The resolution was adopted in committee on a party-line vote. The House adopted the resolution on March 20.

The Senate Budget Committee adopted its version of the budget resolution (S.Con.Res. 100) on March 22. The Committee's resolution differed substantially in policy choices, in areas other than defense and homeland security, from the one adopted by the House. Although many of the differences were relatively small in FY2003, they became more pronounced over the years covered by the two resolutions. The Senate Budget Committee's resolution provided estimates through FY2012. The whole Senate never considered the Committee's resolution.

To avoid delaying its consideration of appropriations, the House adopted a deeming resolution (H.Res. 428) on May 22, 2002 (see CRS Report RL31443, *The "Deeming Resolution": A Budget Enforcement Tool*, by Robert Keith). This set spending levels to be

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[6] CBO, *The Budget and Economic Outlook: Fiscal Years 2003-2012*, Jan. 2002, pp. 5-6.

followed by the Appropriations Committee. The Senate did not adopt a budget resolution for the year (or a deeming resolution as in the House). In spite of the lack of guidance from a completed budget resolution, the House adopted five and the Senate passed three of the 13 regular appropriations bills for FY2003 as the new fiscal year approached, but none of the regular appropriations bills had cleared Congress before the start of the new fiscal year.

To avoid a funding crisis, Congress passed a continuing resolution (CR) on appropriations (H.J.Res. 111; September 26, 2002) that became law (P.L. 107-229) on September 30. The CR provided funding mostly at FY2002 spending levels for federal activities not otherwise funded, through October 4, 2002. A second CR (H.J.Res. 112), extending funding through October 11, cleared Congress on October 3, and was signed by the President (P.L. 107-235) on October 4. Congress adopted a third CR (P.L. 107-240; H.J.Res. 122) on October 10, providing funding through October 9. Funding was extended through November 22, 2002, by the fourth CR (H.J.Res. 123) that Congress cleared for the President on October 16. The bill was signed into law (P.L. 107-244) on October 18, 2002 Congress adopted a fifth CR, (H.J.Res. 124), providing funding, through January 11, 2003, those government activities covered by the 11 regular appropriations bills still pending. The President signed the bill on November 23, 2002 (P.L. 107-294). A sixth CR (P.L. 108-2; H.J.Res. 1) became law on January 10, 2003, continuing funding at FY2002 levels through January 31, 2003. Congress adopted a seventh continuing resolution in late January (P.L. 108-4; H.J.Res. 13), extending funding through February 7, 2003.

Legislation (H.J.Res. 2) to provide funding for the remaining appropriations for the rest of FY2003 went to conference on January 29, 2003.

During October 2002, Congress passed two of the 13 regular appropriations bills. Congress adopted the appropriations for Military Construction (H.R. 5011) on October 10, 2002, and for Defense (H.R. 5010) on October 16, 2002. Both became law on October 23, 2002, with the President's signature (Defense, P.L. 107-248 and Military Construction, P.L. 107-249).

Outlays

The President's budget proposed total outlays of $2.138 trillion for FY2003, $76 billion over the Administration's revised FY2002 level.[7] The year-to-year change was composed of proposed policy changes (approximately $26 billion in the President's proposal) and relatively automatic growth in outlays in mandatory programs resulting from inflation adjustments and demand growth. CBO's estimates of the President's budget put the year-to-year increase in outlays at $101 billion. Of that amount, CBO estimated that $22 billion came from proposed policy changes with the rest coming from inflation adjustment and demand growth. Outlays in the Administration's baseline estimates (excluding the effects of policy change) increased by $50 billion from FY2002 to FY2003.

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[7] The Administration proposed a $32 billion increase in FY2002 outlays above baseline levels, most of which was for its proposed "bipartisan economic security plan." The FY2002 estimate also did not include any outlays that might flow from the adoption of the Administration's $27 billion (in budget authority) supplemental spending request sent to Congress on March 21, 2002.

The Administration's proposals would raise FY2003 outlays by $58 billion over the FY2003 baseline estimate, measuring the effect of its policy proposals on outlays for the year. The proposals included an increase in defense spending of $21 billion, farm support legislation ($7 billion) and the "bipartisan economic security plan" ($8 billion). The remaining proposed policy changes were scattered throughout other categories of spending.

Table 2. Outlays for FY2001-2007

(in billions of dollars)

	FY2001	FY2002	FY2003	FY2004	FY2005	FY2006	FY2007
CBO Outlook 1/31/02	*$1,864* [a]	$2,003	$2,085	$2,152	$2,238	$2,319	$2,402
President's Budget 2/4/02		2,052	2,128	2,189	2,277	2,369	2,468
OMB Baseline 2/4/02		2,020	2,080	2,142	2,218	2,289	2,366
CBO Revised Baseline[b] 3/6/02		2,001	2,080	2,148	2,231	2,312	2,394
CBO Estimate of Pres.'s Budget 3/6/02		2,033	2,134	2,201	2,291	2,394	2,493
House Budget Resolution 3/13/02		2,033	2,123	2,192	2,289	2,383	2,479
SBC Budget Resolution 3/22/02		—	2,139	2,207	2,313	2,403	2,496
OMB MSR 7/15/02		2,032	2,138	2,217	2,298	2,390	2,483
OMB MSR baseline 7/15/02		2,018	2,097	2,163	2,232	2,301	2,376
CBO Update 8/27/02		2,017	2,107	2,195	2,283	2,366	2,461
CBO Budget Outlook 1/31/03		*2,011* [a]	2,121	2,199	2,298	2,387	2,479
President's FY2004 Budget 2/3/03		—	2,140	2,229	2,343	2,464	2,576

SBC = Senate Budget Committee

a. Actual outlays for FY2001 and FY2002.

b. These numbers exclude the effects of the economic stimulus law (P.L. 107-147) enacted on March 9, 2001.

Over the 5 years covered in detail in the President's FY2003 budget (FY2003-FY2007), total outlays would rise from $2,052 billion in FY2002 to $2,128 billion in FY2003 to $2,468 billion in FY2007. The average annual rate of growth in outlays over the FY2003 through FY2007 period was 3.8% a year, almost the exact same rate of growth as over the previous 5-year period (FY1997-FY2002). Over the future 5 years, the Administration proposed cumulative outlays of $11,431 billion. (Over 10 years, FY2003-FY2012, shown in a few tables, the Administration proposes cumulative outlays of $25,478 billion.)

CBO's estimates of the Administration's proposals (March 2002) raised estimated FY2003 total outlays by $6 billion. CBO's 5-year cumulative estimate of the President's policy proposals differs by only $81 billion, of which $44 billion results from higher net interest payments.[8] Over the longer 10-year period, CBO's estimates increased cumulative outlays above the President's budget by slightly more than a 1% increase or $296 billion. Most of the annual differences between the OMB and CBO estimates of the President's outlay proposals were also relatively small compared to total outlays in those years.

The outlays proposed in the House passed budget resolution (H.Con.Res. 353; March 13, 2002) were similar to the ones contained in the President's budget. The House Budget Committee, in producing the resolution, used the Administration's underlying assumptions and followed many of the policy proposals, ensuring a close similarity between the two

[8] CBO's larger deficits and smaller surpluses in its estimates of the President's budget policies slow the reduction in federal debt held by the public compared to the level in the Administration's budget. The larger debt held by the public in the CBO estimate raises the amount of net interest that the government must pay.

proposals. The Committee report (H.Rept. 107-376) compares the budget resolution to the President's proposals (see pages 74-75 in the report). Total outlays in the budget resolution are $5 billion smaller than the President's proposed total outlays for FY2003, but larger in each subsequent year. Over the 5 years covered by the two proposals, cumulative outlays in the House budget resolution were $35 billion larger than the President's proposed cumulative outlays, with both increases and decreases to components of the budget – compared to the President's proposals – scattered throughout the budget.

The Senate Budget Committee's budget resolution used CBO's underlying assumptions, in contrast to the House's use of OMB assumptions. This difference by itself would generate somewhat different numbers in the two budget resolutions even if they contained the same policy assumptions (which they did not). The Senate Budget Committee's budget resolution generally followed the policies of the House and Administration outlay levels for defense and homeland security in FY2003 and FY2004, and in general, the spending levels for mandatory programs with some differences. Spending for non-defense, non-homeland security discretionary spending in the Senate Budget Committee budget resolution were generally larger and had a different distribution from the allocations found in the House budget resolution or in the President's budget. Many of the differences were relatively small in FY2003 but would grow over time. The Senate did not considered the Committee's resolution.

The House passed and the Senate Budget Committee reported budget resolutions, as well as the President's budget, would all provide a large boost in defense outlays from FY2002 to FY2003 of approximately 9%, using each proposal's own numbers. Over the FY2003 and FY2007 period (the last year shown in the House and presidential budget proposals) the President's budget and the House budget resolution show defense outlays growing by almost 4% annually. The Senate Budget Committee passed budget resolution has defense outlays growing by 2%annually during these years.

Non-defense discretionary spending also got a larger boost between FY2002 and FY2003 than in subsequent years in the three proposals. The President's budget showed these outlays growing by 4.5%, the House budget resolution by 5.0%, and the Senate Budget Committee budget resolution by 8.2% between FY2002 and FY2003. The average rate of growth for non-defense discretionary spending in subsequent years in all three proposals was less than 2%, a rate that will not maintain spending for these programs against inflation or population growth. (By comparison, the CBO March baseline estimates of non-defense discretionary spending shows them growing by 2.7% annually in subsequent years, a rate designed to adjust spending for inflation but not population growth.)

The Administration's August 2002 MSR raised estimated total outlay by $10 billion over the original proposal in February 2002. Two-thirds of the increase resulted from adopted or proposed policy changes and the remaining third was attributed to economic and technical estimating changes. Over the 5-year period (FY2003-FY2007), cumulative outlays are 0.8% higher than in the February budget proposals. Compared to the original February proposals, discretionary spending shrinks (by 1.2%) while mandatory spending increases (by 1.6%) and net interest increases (by 3.4%) over the 5 years.

CBO's *Update* (August 27, 2002) also contained changed outlay estimates for FY2003 (and subsequent years) compared to its earlier estimates. CBO's estimated outlays had risen by $28 billion since its March 2002 estimates,. Legislative changes increased estimated outlays by $40 billion, technical changes raised estimated outlays by $11 billion, while changes in the economic outlook *reduced* estimated outlays by $23 billion. The changes raised estimated outlays from $2,080 billion in March 2002 to $2,107 billion in August 2002.

Receipts

The President's FY2003 budget (February 2002) proposed $73 billion in tax cuts for FY2003 (and a $65 billion tax cut in what remained of FY2002) producing a $102 billion increase in receipts from FY2002 to FY2003. Without the proposals, receipts would have increased by $110 billion between the two years. CBO's March 2002 estimates of the President's proposals put the year-to-year increase at $71 billion. The Administration's budget proposed $2,048 billion in receipts for FY2003; CBO estimated that the President's proposals under CBO's economic and technical assumptions would produce receipts of $2,013 billion in FY2003.

The President's budget also proposed making much of the tax cut adopted last year, the EGTRRA, permanent, along with extending a number of tax provisions scheduled to expire during the next five to 10 years. Under current law, most provisions of last year's tax cut would expire at the end of calendar year 2010. Making the tax cuts permanent would have little effect in FY2003, but would reduce receipts substantially in FY2011 and 2012 from baseline estimates.

The Administration estimated that its EGTRRA proposals would reduce revenues by $7 billion between FY2003 and FY2007 and by $343 billion between FY2003 and FY2012. CBO and the Joint Committee on Taxation estimated that extending the provisions expiring in 2010 would reduce revenue by $9 billion between FY2003 and FY2007 and by $374 billion between FY2003 and FY2012 (most of the revenue reduction, $356 billion, occurs in the last two years).[9] The Administration also proposed extending the research and experimentation (R&E) tax credit, which would reduce revenues by an estimated $14 billion to $15 billion over the FY2003 to FY2007 period and by $51 billion to $54 billion over the FY2003 to FY2012 period. CBO and the Joint Committee on Taxation estimated that extending all the other expiring tax provisions expiring through FY2012 (including the R&E tax credit) would reduce revenues by an estimated $78 billion between FY2003 and FY2007 and by $205 billion between FY2003 and FY2012.[10]

The House-passed budget resolution would have increased receipts by $110 billion between FY2002 and FY2003, with both years showing higher revenues than the President's budget. The House resolution reflected the revenue effects of the adoption of the Job Creation and Worker Assistance Act of 2002 (JCWAA; P.L. 107-147), which reduced

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[9] Making permanent the provisions of the 2001 tax cut expiring before 2010 produce estimated revenue reductions of $36 billion between FY2002 and FY2007 and $194 billion between FY2003 and FY2012.

[10] The reduced revenues in thee various estimates increase deficits or reduce surpluses raising the federal debt above the level under current law. This increases the government's net interest payments over the period.

receipts by $43 billion in FY2002 and $39 billion in FY2003 (as estimated by the Joint Committee on Taxation). The resolution accommodated $28 billion in unspecified additional tax reductions through FY2007. It also accepted, although with relatively little effect because of the assumed offsets in the years covered by the resolution, the Administration's proposals to remove EGTRRA's sunset provisions.

Table 3. Receipts for FY2001-2007

(in billions of dollars)

	FY2001	FY2002	FY2003	FY2004	FY2005	FY2006	FY2007
CBO Outlook 1/31/02	*$1,991* [a]	$1,983	$2,070	$2,206	$2,342	$2,447	$2,568
President's Budget for FY2003 2/4/02		1,946	2,048	2,175	2,338	2,455	2,571
OMB Baseline 2/4/02		2,011	2,121	2,234	2,366	2,461	2,581
CBO Revised Baseline [b] 3/6/02		2,006	2,086	2,209	2,342	2,448	2,569
CBO Estimate of Pres.'s Budget 3/6/02		1,942	2,013	2,150	2,314	2,442	2,560
House Budget Resolution 3/13/02		1,968	2,077	2,200	2,356	2,472	2,593
SBC Budget Resolution 3/22/02		—	2,046	2,180	2,338	2,464	2,586
OMB MSR 7/15/02		1,867	2,029	2,169	2,351	2,451	2,567
OMB MSR baseline 7/15/02		1,863	2,035	2,180	2,369	2,475	2,595
CBO Update 8/27/02		1,860	1,962	2,083	2,244	2,381	2,513
CBO Budget Outlook 1/31/03		*1,853* [a]	1,922	2,054	2,225	2,370	2,505
President's FY2004 Budget 2/3/03			1,836	1,922	2,135	2,263	2,398

SBC = Senate Budget Committee.

a. Actual receipts for FY2001 and FY2002.

b. These numbers exclude the effects of the economic stimulus law (P.L. 107-147) enacted on March 9, 2001

The Senate Budget Committee's reported budget resolution showed receipts increasing by $83 billion between FY2002 to FY2003. Like the House resolution, the Senate Budget Committee resolution reflects the revenue effects of the adoption of the JCWAA. The Senate Budget Committee resolution assumed no changes to the existing sunset provisions of EGTRRA. The resolution further assumed that any proposed revenue reductions be offset to avoid a net reduction in receipts.

The Administration's July 2002 MSR reflected the deterioration in revenue estimates resulting from changes in the underlying policy, economic, and technical assumptions since the February 2002 estimates. Receipts dropped below the earlier estimates in each year except for FY2005. For FY2003, the Administration estimated that changes in the underlying economic and technical assumptions reduced receipts by $51 billion below the February 2002 estimates. Enacted legislation and changed proposals raised receipts by $31 billion (compared to February proposals – the Administration's proposed economic stimulus proposal contained larger tax cuts than the legislation that became law, raising estimated revenues). The changes dropped receipts for FY2003 by almost $20 billion from earlier in the year. (Revised FY2002 estimated receipts in the MSR, reflecting the substantial fall in receipts, dropped FY2002 receipts by almost $91 billion from the February estimate). The MSR included estimates that the cumulative five-year (FY2003-FY2007) receipts would fall $21 billion below the February level.

CBO's August 2002 *Update* had newer budget data and revised economic data than did the Administration's MSR. From this, CBO produced its revised estimates. CBO's August 2002 baseline revenue estimates for FY2003 were $124 billion lower than CBO's March baseline revenue estimates (dropping from $2,086 billion to $1,962 billion). Over the 5-year period, FY2003 through FY2007, cumulative revenues had fallen by $470 billion between the March and August CBO baseline revenue estimates. CBO attributes about half of the FY2003 revenue decline to change in the estimates technical assumptions. One-third of the change in revenues CBO attributed to legislative changes, with the remaining portion of the revenue change attributed to differences in the economic assumptions used in the March and August reports. Over the 5-year period, CBO estimated that the technical changes produced 65% of the change, differences in economic assumptions generated 25% of the change, and the remainder came from legislative changes.

Surpluses Or Deficits

Surpluses or deficits are the residuals left after Congress and the President determine the general level of spending and receipts. Reducing the deficit and eventually reaching a balanced budget or generating and keeping a surplus (the government had its first surplus in 30 years in FY1998) had been a major focus of the budget debate for over a decade. The original baseline projections from both OMB and CBO (in early 2002 for FY2003 through FY2007 or FY2012) showed modest deficits in the early years and small, but growing, surpluses in the years through FY2007 or FY2012.

In general, surpluses reduce federal debt held by the public (the government is able to retire some of the debt it created when it had deficits). An expected surplus can also be used to finance spending increases or tax reductions, either of which will reduce (or eliminate) the previously forecast surplus. The Treasury in its normal debt management operations generally uses the surplus to reduce federal debt held by the public. The Treasury took an active role in retiring debt held by the public over the 4 years of surplus (FY1998-FY2001) by purchasing securities on the market and retiring some callable federal bonds. (The Treasury also could retain the cash generated by a surplus and build up government cash balances, but this would make little sense for the government or the economy and seems unlikely.)

The President's proposals and the House passed budget resolution for FY2003 would use the then forecast baseline surpluses to increase spending and cut taxes. The small remaining surpluses in future years in these proposals have been used to reduce the debt held by the public. The budget resolution passed by the Senate Budget Committee would have used the surplus for some spending increases and the rest for reducing the debt held by the public. None of the proposals reserved the entire Social Security surplus for debt reduction (a goal striven for in the budget proposals last year).

The budget outlook-changing events of 2001 (the terrorist attacks, the weakened economy, and policy changes), as reflected in revised budget forecasts in 2002, ended the 2001 forecasts of substantial and growing surpluses throughout the forecast period. The early 2002 budget estimates and forecasts expected a small ($14 billion – CBO) baseline deficit or a small ($41 billion – OMB) surplus in FY2003. The President's proposals turned the baseline surplus into an $80 billion deficit. CBO later (March 2002) estimated that the President's proposals would have produced a $121 billion deficit in FY2003. The MSR raised the Administration's estimate of the deficit to $109 billion in FY2003 (with a baseline deficit of $62 billion for the year). CBO's *Update* estimates that FY2003 will have a baseline deficit of $145 billion. The continued economic sluggishness through much of FY2003 increased the size of the deficit in both CBO's January 2003 budget report (for FY2004) and the Administration's FY2004 budget (February 2003). CBO's new report put the FY2003 deficit at $199 billion (without any further policy changes or unexpected events). The Administration's FY2004 budget boosted the expected FY2003 deficit to $304 billion.

Table 4. Deficits(-)/Surpluses for FY2001-FY2007

(in billions of dollars)

	FY2001	FY2002	FY2003	FY2004	FY2005	FY2006	FY2007
CBO Outlook 1/31/02	*$127* [a]	-$21	-$14	$54	$103	$128	$166
President's Budget for FY2003 2/4/02		-106	-80	-14	61	86	104
OMB Baseline 2/4/02		-9	41	92	148	172	215
CBO Revised Baseline [b] 3/6/02		5	6	61	111	135	175
CBO Estimate of Pres.'s Budget 3/6/02		-90	-121	-51	24	48	68
House Budget Resolution 3/13/02		-66	-46	8	67	89	113
SBC Budget Resolution 3/22/02		—	-92	-27	26	60	90
OMB MSR 7/15/02		-165	-109	-48	53	60	80
OMB MSR baseline 7/15/02		-150	-62	17	137	174	219
CBO Update 8/27/02		-157	-145	-111	-39	15	52
CBO Budget Outlook 1/31/03		*–158* [a]	-199	-145	-73	-16	26
President's FY2004 Budget 2/3/03		—	-304	-307	-208	-201	-178

SBC = Senate Budget Committee.
MSR – Mid-Session Review
a. Actual surplus for FY2001 and actual deficit for FY2002.
b. These numbers exclude the effects of the economic stimulus law (P.L. 107-147) enacted on March 9, 2001.

The Budget and the Economy

The budget and the economy affect each other. The relationship is an unequal one, with the economy influencing the budget with every economic twinge while even substantial policy changes may disappear in the overall economy with little notice or consequence.

Until the release of the revised, more negative budget estimates in August 2001, the earlier 10-year positive budget forecasts in 2001 had been buoyed by the expectation of a continuation of favorable economic conditions into future years. The previous (until the August 2001 estimates) economic outlook supported the expectations of a continuation of the overall improvement in the budget situation since the early 1990s. Much of that budget improvement came from strong and sustained economic growth along with the congressional and presidential efforts to balance the budget. If those favorable economic conditions should falter (as they did last year), so would a major underpinning of the good budget fortunes of the previous years. What good economic conditions give, bad economic conditions can take away. The unexpectedly lengthy economic sluggishness, the start of a recession in March 2001, (along with the budgetary and economic responses to the September 2001 terrorist attacks), raised outlays, reduced receipts, and substantially changed the budget balance expectations and magnitude from what was forecast a year ago.

CBO's budget report, *The Budget and Economic Outlook: Fiscal Years 2004-2013* (January 2003) in its chapter on *The Uncertainties of Budget Projections*, indicated how significantly the budget outlook can be altered by changing the underlying economic assumptions. The chapter contains optimistic and pessimistic alternative scenarios, for the budget (see Table 5). The optimistic scenario assumes that the positive underlying economic conditions and other factors of the later 1990s (1996-2000) continue into the future. The pessimistic scenario assumes that the favorable conditions of those years were an aberration and that the economy and other underlying factors revert to the conditions that prevailed from 1974 through 1995.

Table 5. CBO's Alternative Scenarios, Cumulative Surpluses/Deficits(-); FY2004-2008, FY2009-FY2013 and FY2004-2013

(in billions of dollars)

	FY2004-FY2008	FY2009-FY2013	FY2004-FY2013
CBO Optimistic Scenario Total Surplus 1/31/03	$566	-$143	$4,490
CBO Baseline 1/31/03	-143	1,479	1,336
CBO Pessimistic Scenario Total Surplus 1/31/03	-855	-1,001	-1,856

Source: CBO, The Budget and Economic Outlook: FY2004-2013, Jan. 31, 2003. CRS calculations.

The result of CBO's exercise is a wide range of possible budget outcomes over the next 10 years. Under the optimistic scenario, the surpluses accumulate over the 10-year period (FY2004-2013) to almost $4.5 trillion. Under the pessimistic scenario, a string of deficits appear, accumulating to almost $1.9 trillion over the same 10 years.

In addition to the alternative scenarios, CBO provides estimates of the effects on the budget of changes in selected economic assumptions underlying the budget estimates and projections (see appendix C in the *Budget and Economic Outlook: Fiscal Years 2004-2013*, January 2003). OMB provides similar measures in the President's budget (see chapter 1 in the Analytical Perspectives volume of the *Budget of the United States Government for FY2003*). CBO estimated (January 2003) that a sustained reduction of 0.1% in the real rate of GDP growth beginning in early 2003, would increase the deficit in FY2003 by $1 billion and in FY2004 by $4 billion. OMB's February 2003 FY2004 budget report estimates that a 1% slower real GDP growth beginning in January 2003 will increase the FY2003 deficit by $9.3 billion and the FY2004 deficit by $30 billion. Estimates are provided in both reports for the effects on the budget of other selected economic variables – inflation, unemployment, and interest rates. Larger changes in the underlying economic variables generally would produce larger changes in the budget numbers.

Selected 107th Congress Legislation

H.Con.Res. 353. The Concurrent Resolution on the Budget for Fiscal Year 2003. Adopted by the House Budget Committee (H.Rept. 107-376) on March 15, 2002, on a party line vote after rejecting numerous amendments. It follows most of the proposals of the Administration. It was adopted by the House on March 20.

S.Con.Res. 100. The Concurrent Resolution on the Budget for Fiscal Year 2003. Adopted by the Senate Budget Committee (H.Rept. 107-141) on March 22, 2002, on a party line vote. Its proposals for defense and homeland security were similar to those of the Administration, but differed in many other areas of the budget.

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FOR ADDITIONAL READING

Also see the CRS Electronic Briefing Book on Taxation at [http://www.congress.gov/brbk/html/ebtxr1.shtml].

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CRS Report RL30854. *Uncertainty in Budget Projections*, by Philip Winters.