BRIEF ANALYSIS
PRESIDENT BUSH'S FY 2006 BUDGET

PREPARED BY: DEMOCRATIC STAFF, SENATE BUDGET COMMITTEE

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FY 2006 Budget Would Worsen Nation's Fiscal Outlook

Overview

If we pull back the curtain on President Bush's FY 2006 Budget, we see that it would further worsen the nation's fiscal outlook. If the proposals in the budget are adopted, deficits and debt will continue to explode and the nation's long-term economic security will be threatened.

Bush administration claims that this budget will cut the deficit in half by 2009 are not credible. The budget conceals the damage it is doing by providing only five years of numbers and simply leaving out major items costing hundreds of billions of dollars.

What Is Left Out of the President's Budget?

The budget this year again leaves out major budget items to conceal the damage it is doing to the nation's fiscal outlook. The budget is missing the following items:

The second five years. The budget does not show budget numbers for the second half of the 10-year budget window. This hides the fact that the President's tax policies — whose costs explode after 2010 — along with his other proposals would push the government deeper and deeper into debt.

War. The budget does not include any funding to pay for the wars in Iraq and Afghanistan beyond 2005. Though exact war costs cannot be known, they clearly will be more than the zero shown in the President's budget. In addition to the $81 billion supplemental expected in 2005, CBO projects that ongoing military operations will cost $383 billion over the 2006-2015 period.

Alternative minimum tax (AMT). The budget provides no resources to reform the AMT so that it does not become a tax trap for millions of middle-class families. Last year, the President's budget at least showed the cost of a one-year "patch." But this year's budget omits any fix at all. The ten-year cost of fixing the AMT is $774 billion, including interest.

Social Security privatization transition borrowing. The budget fails to include any of the costs associated with the President's proposal to privatize Social Security. The administration itself estimates that the transition to private accounts to replace Social Security will cost $754 billion for 2006 through 2015. But even this estimate conceals its true cost, because it assumes the program slowly phases in starting in 2009. According to the Center on Budget and Policy

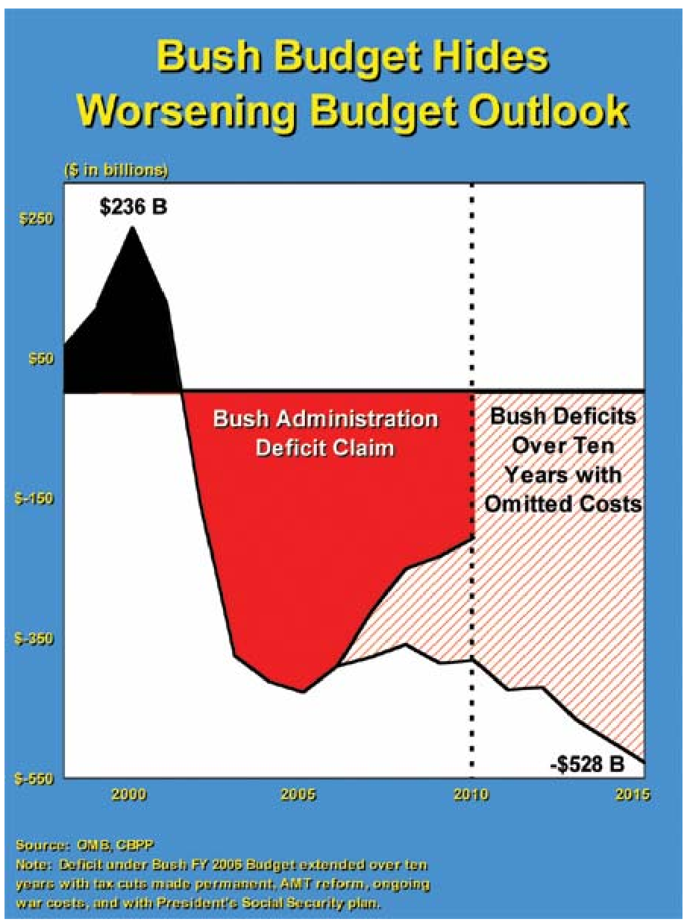
Priorities, the cost of the President's proposal is $1.3 trillion in the first 10 years after full implementation and $4.5 trillion in the first 20 years.

Policy details for appropriations beyond 2006. The budget also omits any policy details for appropriated spending after the first year. The budget provides spending projections for broad discretionary spending aggregates, but hides the specific program cuts needed to hit those targets.

What 150 programs? The administration made a great fanfare about cutting or eliminating more than 150 ineffective government programs in this budget, but they have yet to be identified. When reporters challenged the administration to supply a list of the targeted programs, they were told that the list was not available.

The Real Fiscal Outlook Under the President's Policies

Under any realistic scenario, it is clear that large deficits will continue on into the future. If we extend the President's budget out over 10 years and factor in some of the costs that have been left out, we see a very different picture. For example, if we assume the President's tax cuts are made permanent, AMT is reformed, we face ongoing war costs, and we include the cost of the President's Social Security privatization plan, we can expect to see deficits reaching $528 billion in 2015.



Tax Cut Proposals

The budget includes $1.4 trillion in tax cuts for 2006 through 2015 ($1.6 trillion if debt service is included). These revenue reductions are hidden by the administration's unconventional "baseline" for revenues, which includes the assumption that most of the President's tax cuts will be made permanent.

> *Extending the 2001 and 2003 tax cuts.* The President proposes making permanent his previously enacted tax cuts. This has a budget impact of $1.2 trillion for 2006 through 2015 and a total deficit impact (including interest) of $1.3 trillion.
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> *Extending other expiring tax provisions.* The President proposes to extend some other expiring tax cuts, but not all. He calls for the permanent extension of the research and experimentation (R&E) tax credit, a one-year extension of the Welfare-to-Work credit, and a two-year extension of qualified zone academy bonds (QZABs). The budget, however, is silent about the other 60 or so expiring tax provisions identified by CBO in its recent budget outlook.
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> *Tax preferred savings vehicles.* The President has again proposed a significant expansion of tax-free savings accounts. He proposes to consolidate and expand the three current types of IRAs into retirement savings accounts (RSAs). In addition, the President proposes establishing lifetime savings accounts (LSAs), which would allow taxpayers to shelter more income from taxation. Together, these proposals reduce revenues by $15.1 billion over 10 years. Revenue gains in early years caused by people paying tax penalties on existing savings vehicles that they are converting to RSAs and LSAs would be followed by large revenue losses in later years.
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> *Other tax items.* The budget includes a variety of revenue proposals and tax preferences for health insurance, charitable giving, affordable housing construction, pensions, hybrid vehicles, and private highway projects.

Discretionary Spending Proposals

The President again proposes to cut funding for domestic programs that benefit the middle class at the same time that he proposes further tax cuts that primarily benefit the wealthiest Americans. In total, the budget includes $840.3 billion in discretionary budget authority for 2006, an increase of $11.7 billion, or 1.4 percent over 2005, including advance funding provided for bioshield in 2005 (an increase of $14.2 billion, or 1.7 percent, excluding bioshield funding). Compared to CBO's estimate of the amount of resources needed to maintain purchasing power provided to agencies and programs in 2005, the President proposes to cut funding by $7.3 billion, or 0.9 percent. As the table below shows, however, that sum includes increases above baseline in defense, homeland security, and international affairs, while cutting domestic programs other than homeland security by $19.3 billion or 5.4 percent.

Bush Budget for 2006 Discretionary Programs				
Discretionary budget authority; $ billions	Baseline	Bush Budget	Budget Above/ Below Baseline	% Difference
Defense ……….	430.7	438.8	+8.2	+1.9%
International Affairs …………... .	30.5	33.7	+3.2	+10.4%
Homeland Security	28.2	28.8	+0.7	+2.3%
Other Domestic	358.3	339.0	-19.3	-5.4%
Total Appropriations	847.6	840.3	-7.3	-0.9%

NOTE: Compares 2006 Bush budget request with CBO's Jan 2005 estimate of the amount of purchasing power needed in 2006 to maintain 2005 funding levels, excluding funding provided in supplementals.

Key Domestic Discretionary Budget Cuts

Education. The budget cuts funding for discretionary Department of Education programs by $1.3 billion, or 2.3 percent, below the amount needed to maintain purchasing power at the current level, and by $530 million, or 0.9 percent, below the 2005 enacted level.

The budget eliminates funding for 48 education programs, totaling $4.3 billion in 2005. The largest eliminations include vocational education programs – $1.3 billion, education technology state grants – $496 million, Safe and Drug-Free state grants – $437 million, TRIO Upward Bound and Talent Search programs – $458 million, GEAR-UP – $307 million, Even Start – $225 million, and comprehensive school reform – $205 million.

The President's $1.5 billion high school initiative is more than offset by cuts in existing programs targeted to high schools, including the elimination of all vocational education programs – $1.3 billion, the TRIO Upward Bound and Talent Search programs – $458 million, and GEAR-UP program – $307 million. The budget also cuts adult education by $370 million, or 63 percent.

First Responders. The budget cuts overall first responder funding by $1.6 billion, or 38 percent, below the 2005 level of $4.1 billion. The budget cuts state first responder formula grants by $280 million, or 26 percent, below the 2005 level; and Firefighter Grants by $215 million, or 30 percent, below the 2005 level at the Department of Homeland Security. At the Department of Justice, the budget cuts COPS funding by $477 million, or 96 percent, below the 2005 level; and eliminates Byrne Memorial Justice Assistance Grants – a cut of $529 million below the 2005 level.

Transportation. The budget cuts national passenger rail funding by $866 million, or 71 percent, compared to CBO's inflated baseline. According to additional details in the budget, the distribution of the remaining $360 million in federal funding will change significantly. Amtrak will no longer receive any funding from the federal government, effectively forcing it into bankruptcy. Instead, the federal government will provide $360 million in federal funding for national passenger rail through the Surface Transportation Board (STB). STB would use the funding to maintain existing commuter services and freight traffic along the Northeast Corridor and elsewhere.

Environment and Natural Resources. The budget proposes $28 billion in discretionary spending for environment and natural resources. This represents a cut of $3.3 billion, or 11 percent, below CBO's baseline.

The budget provides $4.3 billion for the Army Corps of Engineers, a cut of $332 million, or 7 percent, from last year's level; and $456 million, or 10 percent, below CBO's baseline.

Veterans' Medical Services. The budget provides $28.9 billion for veterans' medical services – $700 million, or 2.5 percent over the 2005 enacted level of $28.2 billion. However, the budget also includes $2.5 billion in new enrollment fees and $1.8 billion in increased prescription drug co-payments over 10 years, which are classified as mandatory spending in 2006.

Community and Economic Development. The budget eliminates $5.7 billion in funding for 18 community development programs including HUD's Community and Economic Development Block Grants and creates a new $3.7 billion grant program at the Department of Commerce. Overall, this proposal cuts community and economic development funding by approximately $2.1 billion, or 36 percent, below the amount needed to keep pace with inflation.

Manufacturing Extension Partnership. The budget reduces funding for the Manufacturing Extension Partnership by $61 million, or 56 percent, below the 2005 level. In addition, it proposes to terminate the Advanced Technology Program.

LIHEAP. The budget cuts LIHEAP funding by $183 million, or 8 percent, below the 2005 level. This represents a 10 percent loss in purchasing power for this program.

Even Steeper Cuts over Five Years. The 2006 budget fails to provide any account-level detail on discretionary spending after the first year. The Bush administration claims savings from reduced spending on domestic accounts, without detailing where those cuts will come from. However, aggregate budget function totals provided for the 2006-2010 period show that the President is proposing cutting funding for domestic programs by a total of $179 billion below CBO's January 2005 baseline, adjusted to exclude the extension of the 2005 disaster supplemental. The aggregate function totals make clear that the President's policies will lead to steep cuts in key domestic priorities, including five-year cuts of:

- $15.7 billion, or 9.3 percent, in veterans' benefits and services,
- $38.6 billion, or 9.2 percent, in education, training, employment, and social services,
- $25.6 billion, or 15.5 percent, in natural resources and the environment,
- $24.2 billion, or 8.7 percent, in health, and
- $7.2 billion, or 3.4 percent, in administration of justice.

Mandatory Spending Proposals

The President's budget proposes a variety of changes in mandatory spending that would reduce spending by a net of $5.3 billion in 2006 and $71 billion over the next decade ($138 billion in reductions in mandatory programs, offset by $67 billion in increased refundable tax credits). Major mandatory cuts proposed by the President include: estimated savings in the Medicaid and State Children's Health Insurance programs – $45 billion, Pension Benefit Guaranty Corporation – $26.5 billion, Power Marketing Administrations (PMAs)– $12 billion, spectrum – $11 billion, agriculture and nutrition – $10 billion, education – $11 billion, and veterans – $4 billion.

Medicaid/SCHIP. The budget proposes approximately $45 billion in Medicaid/SCHIP cuts over ten years, including roughly $60 billion in Medicaid cuts and $16.5 billion in new Medicaid/ SCHIP spending initiatives. The $60 billion in Medicaid cuts are largely from what the administration calls "inappropriate federal spending on Medicaid intergovernmental transfers and other overpayments." The proposed $16.5 billion for Medicaid and SCHIP spending coverage initiatives includes $11.3 billion to enroll more children in Medicaid and SCHIP, $2.9 billion to expand access for people with disabilities, and $560 million for Transitional Medical Assistance.

Pension Benefit Guaranty Corporation (PBGC). The budget proposes to save $26.5 billion by requiring employers to make up funding shortfalls in their defined benefit pension plans within a "reasonable period of time;" establish funding targets to address a plan's risk of termination; set insurance premiums paid by plans to PBGC to reflect a plan's risk of termination; require companies to pay for additional benefits immediately if they are financially weak; and require plans to provide workers with timely information on the true financial health of pension plans and make that information publicly available. These proposals also result in a revenue loss of $12.7 billion.

PMAs. The budget includes a proposal that calls for PMAs to annually raise electricity rates to bring them closer to market levels, providing $12.4 billion in savings over ten years.

Spectrum. The budget raises $5 billion by extending the current authority for the FCC to auction spectrum, which expires at the end of 2007. It also again proposes a new license fee and an analog spectrum lease fee raising another $6 billion in receipts.

Agriculture and Nutrition. The budget cuts $5.7 billion over 10 years from farm programs through restrictions on marketing loans, a 5 percent reduction in farm program payments, assessments on sugar, and modifications to the dairy program. It also cuts $1.3 billion from the federal crop insurance program by increasing producer premiums, raising catastrophic coverage fees, and reducing delivery costs. Finally, the budget cuts $1 billion in the Food Stamp program by stripping states of the flexibility to streamline eligibility and coordinate it with the states' TANF funded program.

The budget raises another $1.9 billion through increased user fees for inspections that will further reduce farm income.

Education. The budget proposes a variety of changes in the student loan programs and uses some of the savings to pay for increases in the Pell Grant program, for a net savings of $10.7 billion over 10 years. Even though the Pell Grant program is discretionary, the budget proposes to use mandatory funding to retire the $4.3 billion Pell Grant shortfall and raise the maximum Pell Grant by $100 in each of the next five years; these changes cost $15 billion over 10 years. In addition to changes in the student loan program, which include benefit increases as well as lender changes for a net savings of $19.6 billion, the budget proposes to end the Perkins loan program and recall $6 billion in federal Perkins Loan revolving funds held by participating colleges.

Veterans' Health Care. The administration proposes to charge certain veterans with non-service connected disabilities a $250 annual user fee, which would raise $2.5 billion over 10 years. The administration also proposes to increase the co-payment charged to many veterans for prescription drugs from the current $7 to $15, raising another $1.8 billion.

Health Coverage. The administration proposes over $125 billion (receipt and outlay effects) in tax-related proposals to expand health coverage. These proposals include $74 billion for health insurance tax credits, $28.5 billion for Health Savings Accounts (HSAs), and $22.7 billion for rebates to small employers contributing to HSAs.

Budget Process Proposals

The President's budget includes a series of budget process proposals that would favor the enactment of more tax cuts, focus budget discipline entirely on spending, and enhance the budgetary powers of the President to the detriment of Congress.

Discretionary Spending Caps. The budget proposes annual caps for 2005, 2006, and 2007 on total discretionary, defense discretionary, nondefense discretionary, highways, and mass transit spending, enforced through across-the-board cuts in non-exempt discretionary programs. For 2008, 2009, and 2010, it proposes annual caps on total discretionary spending only – even though his budget provides no account-level detail after 2006.

Pay-As-You-Go Rule. The President proposes to extend the pay-as-you-go rule ("paygo") for mandatory spending only. Tax cuts would be exempt, with the revenue impact of tax changes no longer included in paygo calculations. Because tax changes would not be subject to paygo, tax breaks would not trigger any spending cuts under the President's plan, no matter how much those tax breaks would increase the deficit. Moreover, the President would prohibit revenue increases from being used to offset increases in mandatory spending.

Emergency Spending. Each item designated by Congress as emergency spending would require the President's concurrence in order for it to be exempted for purposes of enforcing the discretionary caps and paygo.

Underfunded Obligations. The President's budget would create a new point of order against legislation that would worsen the long-term (75 years) underfunded obligations of major entitlements including Social Security, Medicare, Federal civilian and military retirement, veterans' disability compensation, and Supplemental Security Income.

Line-Item Veto. The Supreme Court struck down as unconstitutional the Line Item Veto Act of 1996, which attempted to give the President the authority to cancel spending and tax line-items. The President's budget proposes a new line-item veto, giving the President the authority to defer new spending whenever the President determines that the spending is not an essential government priority.

NOTE: All years are fiscal years unless otherwise noted.