BRIEF ANALYSIS
PRESIDENT BUSH'S FY 2007 BUDGET

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President Bush's FY 2007 Budget: More Deficits and Debt

Overview
The nation needed a new budget plan this year, a dramatic and bold acknowledgment from the Bush administration that we need to put our fiscal house back in order. Instead, we got more of the same – more deficits, more debt, and more hiding of our true fiscal condition from the American people.

The Bush administration's new budget is nothing new. It represents the same reckless fiscal course the administration has followed for the last five years. It explodes deficits, but then conceals them by providing only five years of numbers and leaving out large costs, like long-term Alternative Minimum Tax (AMT) reform and realistic ongoing war costs. The result will be more debt passed on to our children and grandchildren.

What Is Left Out of the President's Budget?
Like previous budgets from this administration, this budget seems designed to hide the worsening fiscal outlook. The budget again leaves out large items to conceal the damage it is doing. For example, the budget leaves out:

Full ten-year numbers. The budget does not show figures for the second half of the ten-year budget window. By providing only five years of numbers, the administration conceals the fact that the cost of all of the President's tax cuts explodes outside the five-year budget window – costing $2 trillion over the full ten years, including interest costs.

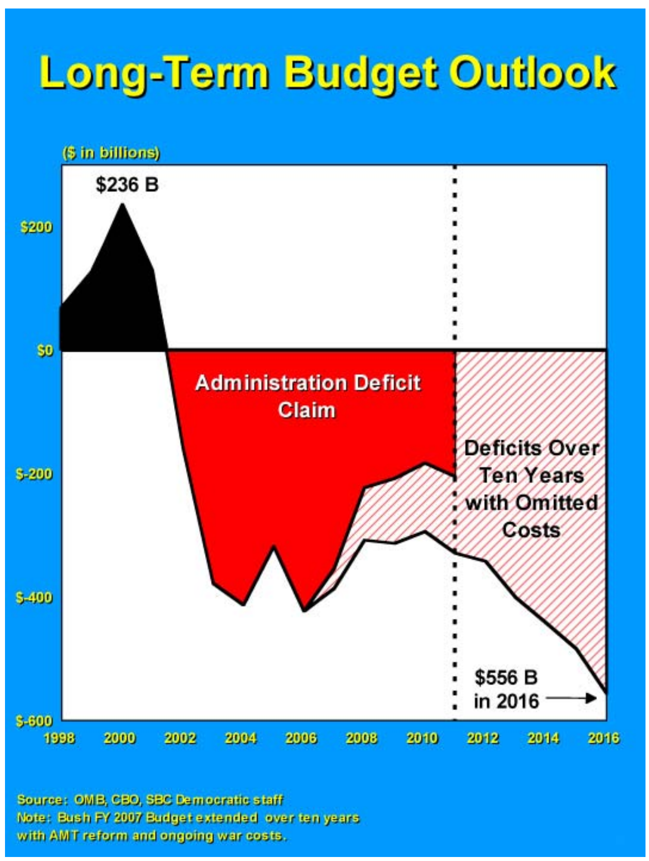
War costs beyond 2007. Despite the fact that we are likely to face an ongoing military commitment in Iraq, Afghanistan, and elsewhere, the administration continues to leave out the cost of long-term ongoing military operations. Although the administration finally included some short-term costs in its calculations – $70 billion for 2006 and $50 billion for 2007, it fails to include anything beyond that. That is unrealistic. We know that the cost beyond 2007 will not be zero. And with expenditures in Iraq and Afghanistan now exceeding $7 billion a month, the cost in 2007 is likely to be more than $50 billion. CBO estimates show us that, even assuming a reasonable drawdown of U.S. forces in Iraq, ongoing military operations may cost $298 billion above what the administration has provided over the 2007-2016 period.

Alternative Minimum Tax (AMT) reform beyond 2006. The administration provides no money for an AMT fix beyond 2006 – despite the fact that this old millionaire's tax is hitting more and more middle class families. Like the tax cuts, the cost of AMT reform explodes outside the five-year budget window – costing $1 trillion over the full ten years, including interest costs.

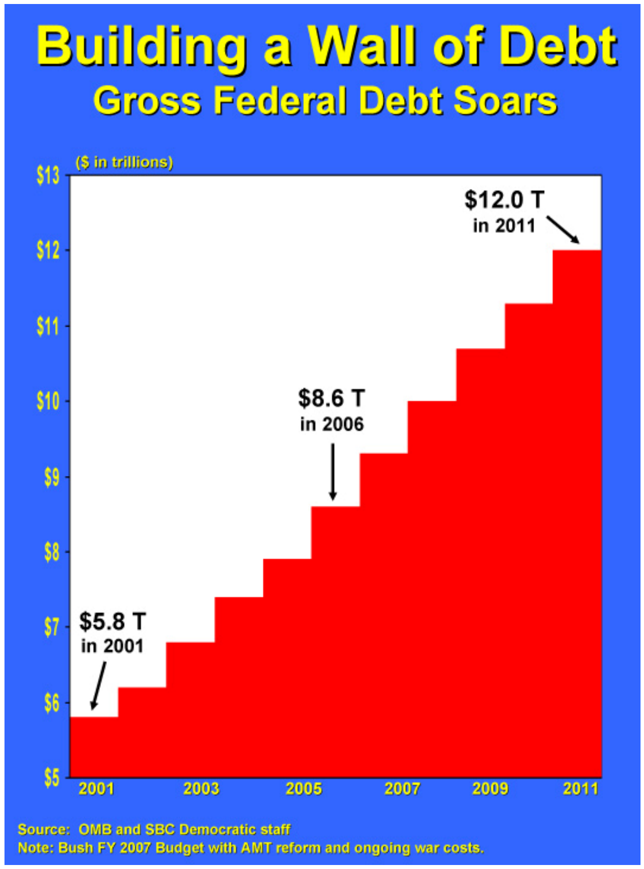
Discretionary spending policy details beyond 2007. The administration also omits any policy details for appropriated spending after the first year. This omission allows the administration to claim it is cutting spending without actually saying what should be cut.

Bush FY 2007 Budget with Omitted Costs						
($ billions)	2006	2007	2008	2009	2010	2011
Bush FY 2007 Budget.....................................	-423	-354	-223	-208	-183	-205
AMT Reform..	0	-22	-45	-55	-66	-77
Ongoing war costs..	0	-9	-37	-43	-33	-29
Debt Service on adjustments	0	-1	-3	-8	-13	-18
Bush FY 2007 Budget with Omitted Costs	-423	-386	-308	-313	-294	-329

True Budget Outlook under Bush Policies
Despite claims that deficits are coming down, under any realistic scenario, it is clear that the deficits will actually worsen. If we extend the budget out over ten years, and add in the cost of AMT reform and CBO's estimate of likely additional ongoing war costs, we see that the deficit will reach $556 billion in 2016 and total $3.9 trillion over ten years. That provides us with a very different picture from the one the administration is showing.



Federal Debt Soaring
Instead of paying down debt in preparation for the retirement of the baby boom generation, the federal debt has exploded. Under this budget, with AMT reform and ongoing war costs added in, gross debt will soar to $12 trillion by 2011. To put this debt increase in perspective, every minute in 2006, the administration's budget policies will add $1,343,525 to the national debt.



Under this administration's watch, we are becoming increasingly reliant on foreigners to buy our debt and finance our deficit spending. Foreign holdings of U.S. debt have gone up 115 percent since 2001, rising from $1.01 trillion in January 2001 to $2.17 trillion in November of last year. It took 42 Presidents 224 years to run up a trillion dollars of external debt. This administration has doubled that amount of external debt in five years.

Tax Cut Proposals
The President's budget once again proposes further tax cuts that primarily benefit the wealthiest, including $1.7 trillion in tax cuts for 2007 through 2016, or $2 trillion if interest costs are included.

Extending the 2001 and 2003 tax cuts. The President proposes making permanent his previously enacted tax cuts.

Extending other expiring tax provisions. The President proposes to extend some other expiring tax cuts. He calls for the permanent extension of the research and experimentation (R&E) tax credit, and extensions through 2006 of Alternative Minimum Tax (AMT) relief, the Work Opportunity and Welfare-to-Work credits, qualified zone academy bonds (QZABs), and the first-time homebuyer credit in the District of Columbia.

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 $21.9 billion over ten years. Revenue gains through 2010 resulting from people paying tax penalties on existing savings vehicles that they are converting to RSAs and LSAs turn to losses in 2011 that increase sharply every year thereafter.

Expanding Health Savings Accounts (HSAs). The President would expand HSAs by providing purchase incentives (above-the-line deduction and refundable tax credit) for high-deductible non-group health insurance plans, and increase the amount that individuals can contribute annually to HSAs. Proposals related to this HSA expansion would reduce revenues by $136 billion over ten years.

Other tax items. The budget includes a variety of revenue proposals and tax preferences for small business investment, charitable giving, and pensions.

Discretionary Spending Proposals

At the same time that the President proposes further tax cuts that primarily benefit the wealthiest, he again proposes to cut funding for domestic programs that benefit the middle class. In total, the budget includes $870.7 billion in discretionary budget authority for 2007 (excluding emergencies), an increase of $27.3 billion, or 3.2 percent, over the 2006 enacted level. Compared to OMB's estimate of the amount of resources needed to maintain purchasing power provided to agencies and programs in 2006, the President proposes to increase funding by $2.1 billion, or 0.2 percent.

As the table below shows, however, that total includes increases for defense, homeland security, and international affairs, while cutting domestic programs other than homeland security by $16.8 billion, or 4.6 percent.

Bush Budget for 2007 Discretionary Programs

Discretionary budget authority; $ billions	Baseline	Bush Budget	Budget Above/ Below Baseline	% Difference
Defense …………………………	444.6	459.7	+15.1	+3.4%
International Affairs ………	32.1	35.1	+3.0	+9.4%
Homeland Security …………….	28.5	29.3	+0.8	+2.9%
Other Domestic	363.4	346.5	-16.8	-4.6%
Total Appropriations	868.6	870.7	+2.1	0.2%

NOTE: Compares 2007 Bush budget request with OMB's estimate of the amount of purchasing power needed in 2007 to maintain 2006 funding levels, excluding emergency funding enacted and requested in 2006 and 2007.

The President's budget also includes defense supplemental emergency funding of $70 billion in 2006 and $50 billion in 2007. For non-defense discretionary programs, the budget requests $18 billion for hurricane relief in 2006 and $2.3 billion for avian flu in 2007.

Key Domestic Discretionary Budget Cuts

Education. The budget provides $54.4 billion for discretionary Department of Education programs, a cut of $2.1 billion, or 3.8 percent, below the comparable 2006 program level. This is the largest cut in the 26-year history of the Education Department.

The budget eliminates funding for 42 education programs, totaling $3.5 billion in 2006. The largest eliminations include: vocational education (-$1.3 billion); education technology (-$272 million); safe and drug-free state grants (-$346.5 million); TRIO Upward Bound and Talent Search (-$456 million); and GEAR-UP (-$303 million). It also proposes to end the Perkins loan program, saving $664 million in 2007. The budget freezes the Pell Grant maximum award at $4,050, where it has been since 2003.

Transportation. The budget includes $900 million for Amtrak, a cut of $394 million, or 30.4 percent below the 2006 enacted level. It provides $2.75 billion for Airport Improvement Program (AIP) capital grants, a cut of $765 million or 22 percent below last year's enacted level.

DOJ Law Enforcement Grants. The budget eliminates funding for the Byrne Justice Assistance grant program, which received $388 million in 2006. For COPS, the administration provides $102 million in new funding, which is a cut of $371 million below 2006 program level. In addition, the budget proposes a larger rescission ($128 million) than the previous year. This rescission more than offsets the 2007 COPS funding.

DHS first responder grants. The budget provides $1.73 billion, a decrease of $573 million or 25 percent below the 2006 level. State formula grants and urban area grants receive increases ($616 million for state grants, up $87 million, and $817 million for urban area grants, up $80 million). However, law enforcement terrorism prevention grants are eliminated (-$385 million) and Firefighter Grants are cut by $355 million or 55 percent.

Community Development Block Grants (CDBG). The budget provides $2.97 billion for the CDBG program, a cut of $736 million, or 20 percent below the 2006 enacted level.

Community Services Block Grants (CSBG). The budget eliminates funding for the CSBG program, which was funded at $630 million in 2006.

Low Income Home Energy Assistance Program. The budget assumes $1.782 billion in regular appropriations for LIHEAP - - a $379 million (17 percent) cut from the enacted level of $2.161 billion. This funding level does not include the $1 billion in mandatory LIHEAP funds included in the 2005 reconciliation bill. The Energy Policy Act of 2005 included an authorization level of $5.1 billion per year for LIHEAP from 2005 through 2007.

National Institutes of Health (NIH). The budget funds NIH at the 2006 level of $28.4 billion. According to the Congressional Research Service, the 2006 enacted level was the first cut in NIH's appropriation since 1970.

Rural Health Programs. The budget cuts rural health programs by $133 million, or 83 percent, including cutting Rural Health Care Services Outreach grants by $28.5 million and eliminating: Rural Hospital Flexibility grants (-$63.5 million); Rural Access to Emergency Devices and

Public Access Defibrillation Demonstration projects (-$1.5 million); and the Denali Commission (-$39.3 million).

Even Steeper Cuts over Five Years. The 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 2007-2011 period show that the President is proposing cutting funding for domestic programs by a total of $183 billion below OMB's January 2006 baseline, excluding emergencies. 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:

- $52.7 billion, or 12.6 percent, in education, training, employment, and social services,
- $28.1 billion, or 16.9 percent, in natural resources and the environment,
- $24.2 billion, or 8.8 percent, in health, and
- $15.3 billion, or 11.3 percent, in transportation programs.

Mandatory Spending Proposals

The President's budget proposes a variety of changes in mandatory spending that would, on a net basis, reduce spending by $1.7 billion in 2007, but increase the deficit over the next decade. Major mandatory changes proposed by the President include: payment cuts to Medicare fee-for-service providers; increased premiums and other reforms to the Pension Benefit Guaranty Corporation; savings in Medicaid legislative proposals; agriculture cuts and fees; restricting food stamp eligibility; reductions in Social Security benefits; and drilling in ANWR.

Medicare. The budget proposes a series of cuts in Medicare payments to fee-for-service providers, totaling $35.9 billion over the next five years, and $105 billion over the next ten years. Some of these cuts over five years include: freezing payments to skilled nursing facilities (SNFs), home health agencies, and inpatient rehabilitation facilities ($10.2 billion); updating inpatient and outpatient hospital payments by less than the growth in inflation ($8.1 billion); cutting hospice and ambulance services payments by 0.4 percent ($840 million); limiting the oxygen rental period to 13 months ($6.6 billion); and phasing out Medicare bad-debt payments to providers ($6.2 billion). The budget proposes no change to override an automatic cut of over four percent in Medicare physician payments that will go into effect in 2007, without legislative action.

The budget proposes to eliminate annual inflation indexing of the income thresholds for income-related Part B premiums. Under current law, starting in 2007, Part B premiums will be increased on a graduated basis for beneficiaries with annual incomes greater than $80,000 ($160,000 per couple). These income thresholds are indexed to inflation. Under the President's proposal, these income thresholds would no longer be indexed for inflation. Over time, more seniors will be subject to higher premiums (similar to the AMT). This proposal would save $1.9 billion over five years.

Separately, the budget assumes regulatory changes to Medicare provider payments that would achieve $5.4 billion in additional savings over five years, including: freezing long-term care hospital payments; reducing payments to long-term care hospitals for certain outlier patients; reducing the payment update for inpatient rehabilitation facilities; and making payment changes for Part B covered drugs, supplies, and wheelchairs.

Social Security. The budget provides $81.6 billion over five years and $712.1 billion over ten years to implement the President's Social Security private accounts proposal. Separately, the budget proposes specific cuts to Social Security benefits, totaling $2.2 billion over five years and $6.3 billion over ten years. Proposed cuts include: eliminating the $255 lump-sum death benefit to surviving spouses and children; requiring full-time school attendance for continued eligibility of a child's Social Security benefits at age 16; tightening enforcement of the windfall elimination provision (WEP) and the government pension offset (GPO); and changing the disability insurance/worker's compensation offset.

Pension Benefit Guaranty Corporation (PBGC). The administration assumes $16.7 billion in PBGC savings over five years as a result of reform proposals which include increasing PBGC premiums above their current levels to improve the financial condition of the program.

Medicaid. The administration proposes policy changes resulting in $1.5 billion in net Medicaid cuts over five years and $5 billion over ten years. This net total includes $4.9 billion in gross Medicaid cuts over five years and $11.9 billion over ten years and new Medicaid spending of $3.5 billion over five years and $6.8 billion over ten years.

> *Medicaid Regulatory Changes* -- In addition, the budget assumes an additional $12.2 billion in Medicaid cuts in the baseline over five years as a result of Medicaid regulatory changes the administration will be pursuing in areas they have identified as payment reform ($3.8 billion), provider tax reform ($2.1 billion), Medicaid services reform ($2.3 billion), pharmacy pay and chase reform ($430 million), and school-based services administration reform ($3.6 billion). The Medicaid baseline is an estimate of the spending that would occur if no changes were made to current law (e.g., no Congressional action) during the period covered by the budget. The budget does not provide a ten year figure for these regulatory savings.

Agriculture and Nutrition. The budget cuts $8.9 billion over ten years from farm programs through a five percent reduction in farm program payments, assessments on sugar, and modifications to the dairy program. It also cuts the federal crop insurance program by increasing producer premiums, raising catastrophic coverage fees, and reducing payments for crop insurance delivery.

The budget raises another $2 billion over ten years through new or increased user fees on farm and conservation programs and marketing and inspection services that will further reduce farm income.

Food Stamp Program. The administration proposes net Food Stamp cuts of $29 million in 2007, $121 million over five years, and $179 million over ten years.

> *Restricting Food Stamp Eligibility for TANF Recipients* -- The administration proposes to cut Food Stamp spending by $75 million in 2007, $710 million over five years, and $1.6 billion over ten years. Under current law, low-income families that receive or are eligible to receive any type of benefit from the Temporary Assistance to Needy Families (TANF) program are considered categorically eligible for food stamps. Categorically eligible families are not subject to the same income and asset tests as other participants. The administration proposes to tighten the eligibility for food stamps by restricting categorical eligibility to only those TANF low-income families receiving cash assistance. CBO scored a similar proposal back in October 2005 and estimated that 225,000 individuals would become ineligible for food stamps.

> *Exclusion of Retirement Savings For Eligibility* -- The administration proposes to exclude retirement savings from the asset test when determining eligibility for the Food Stamp program. The budget assumes this proposal would increase Food Stamp spending by $47 million in 2007, $589 million over five years, and $1.4 billion over ten years.

Energy and Environment. The budget proposes to repeal an oil and gas R&D program which was included in the Energy Policy Act of 2005, saving $210 million over five years and $460 million over ten years. The budget once again assumes receipts from permitting oil and gas drilling in Alaska's Arctic National Wildlife Refuge, resulting in savings of approximately $4 billion (over a five-year and a ten-year period).

*Unemployment Insurance (UI) Integrity***.** The administration assumes $1.7 billion over five years in Unemployment Insurance savings as a result of proposals to reduce improper UI payments.

Tax Credit Outlay Effects. The tax proposals in the budget include a net increase in outlays of $74 billion over the next ten years. These outlay increases occur as a result of the permanent extension of the child tax credit ($52 billion) and marriage penalty relief ($7 billion), and the new proposals related to expanding the use of health savings accounts ($20 billion). Proposals characterized as simplification for families reduce outlays over the ten-year period by $5 billion.

Budget Process Proposals

The President's budget includes a series of budget process proposals.

Automatic Cuts in Medicare. The budget includes one major new budget process proposal: automatic cuts in Medicare if the Medicare Modernization Act's threshold (when general revenue Medicare funding is projected to exceed 45% of Medicare's total spending) is exceeded. The cuts would begin as a four-tenths of one percent reduction to all payments to providers in the year that the threshold is exceeded, and would grow by four-tenths of one percent every year the shortfall continues.

*Mandatory Spending Control***.** The President again proposes that mandatory spending that would increase the deficit in the current year and the budget year should trigger across-the-board cuts in other mandatory spending.

Discretionary Spending Caps. The President proposes separate annual discretionary spending caps for defense and nondefense for 2006, 2007, and 2008, enforced through across-the-board cuts in non-exempt discretionary programs. In addition, a separate category for transportation outlays financed by dedicated revenues would be established for 2006 through 2009. For 2009-2011, separate defense/nondefense caps are eliminated and replaced with overall discretionary caps.

Long-Term Underfunded Obligations. The President has again proposed creating a new point of order against legislation that would worsen the long-term 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 Line Item Veto Act of 1996 attempted to give the President the authority to cancel spending and tax line-items, but the Supreme Court struck down that law as unconstitutional. The President's budget again 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.

Advance Appropriations and Delayed Obligations. The President proposes to continue to cap the annual amount of advance appropriations.

Emergency Spending. Under the budget, each item designated by Congress as emergency spending would require the President's concurrence in order to be scored as an emergency.

Joint Budget Resolution. To give the budget resolution the force of law, the President's budget advocates a joint budget resolution requiring the President's signature.

Biennial Budgeting. The budget proposes to switch from annual budgeting to biennial budgeting. Under biennial budgeting, in the first year of a new Congress, the President would be required to submit to Congress a two-year budget plan. Congress would then pass a two-year budget and enact two-year appropriations bills. The second year of each Congress would be used for considering authorizing legislation.

Automatic Continuing Resolution. The budget proposes that if Congress and the President fail to complete action on appropriations bills by the October 1 start of each fiscal year, an automatic continuing resolution should go into effect to provide funding at the lower of the President's budget or the prior year's level.

Baseline Changes. The President would revise budget baseline calculations to assume the extension of expiring tax provisions, exclude discretionary funding for emergencies, reflect adjustments for pay raises that begin on January 1st of each year rather than on October 1st, and eliminate adjustments for expiring housing contracts and social insurance administrative expenses.

NOTE: All years are fiscal years unless otherwise noted.

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