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The Budget for Fiscal Year 2004

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Summary

The Administration's fiscal year (FY) 2004 *Mid-Session Review* (MSR; July 15, 2003) estimated the FY2004 deficit at $475 billion, up from the $307 billion deficit included in the President's February 2003 budget proposal. Policy differences, a weaker economy than expected, and other estimating factors produced the growth in the deficit estimate. The Administration's policies underlying the July estimates "do not reflect ... expected but undetermined additional costs arising from ongoing operations in Iraq, extending beyond 2003." (OMB, Mid-Session Review, July 15, 2003, p.1.) By FY2008, the last year forecast in the MSR, the deficit has fallen to $226 billion.

On January 31, 2003, the Congressional Budget Office (CBO) released the first of its budget reports (CBO will release its mid-year budget report in August). The baseline estimates from CBO run through FY2013. CBO's baseline estimates are similar in construction to the current services baseline produced by the Office of Management and Budget (OMB) for the President. CBO's baseline had a $145 billion deficit in FY2004, that would become a surplus of $65 billion in FY2008. Because the CBO baseline estimates are constrained by existing policy at the time they are produced, they incorporate the scheduled expiration of the 2001 tax cuts at the end of calendar year 2010. The result is a rapid increase in receipts between FY2011 and FY2013, producing substantial surpluses in those years. Under CBO baseline estimates — which CBO points out contain policy assumptions that may not hold — the surplus would reach $508 billion in FY2013.

In March, CBO released its report analyzing the President's policies. CBO's estimates of the President's budget, a recasting of the policies using CBO assumptions and budget estimating methods, raise the expected deficit for FY2004 to $338 billion from the OMB estimated $307 billion. The report also included an update to CBO's January baseline that pushed the deficit for FY2004 to $200 billion from $145 billion. These baseline revisions move the return-to-a-surplus from FY2007 to FY2008 and reduce the cumulative FY2004-FY2013 surplus from $1,336 billion (January) to $891 billion (March).

Congress adopted the conference report (H.Rept. 108-71, H.Con.Res. 95) on the budget resolution on April 11. The resolution contained different sized tax-cut reconciliation instructions for the House ($550 billion) and the Senate ($350 billion). The resolution also set the spending limits for FY2004. On May 9, the House passed its tax-cut reconciliation bill (H.R. 2); on May 15, the Senate passed its reconciliation bill (S. 1054, substituting its text for the text of H.R. 2). Congress adopted the $350 billion tax-cut conference report (H.Rept. 108-126) on the reconciliation tax cut on May 23. The bill became law (P.L.108-27) on May 28.

Congress is currently working its way through the 13 regular appropriations for FY2004. As of July 16, 2003, the House had passed six; the Senate had passed two. This report will be updated as events warrant.

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Background and Analysis

Presidents generally submit their budget proposals for the upcoming fiscal year (FY) early in each calendar year. For FY2004, the Bush Administration released its budget document (*The Fiscal Year 2004 Budget of the U.S. Government)* on February 3, 2003. The multiple volumes contained general and specific descriptions of the Administration's policy proposals and expectations for the budget for FY2004 and for the years through FY2008, with information on the revenue changes through FY2013 and a section on long-term fiscal issues facing the nation. The full set of budget documents (*Budget*, *Appendix*, *Analytical Perspectives*, *Historical Tables*, among several others) contain extensive and detailed budget 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. In addition to its presentation of the Administration's proposals, the budget documents are an annual basic reference source for federal budget information.

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 legislation, the Administration often revises its original proposals because of interactions with Congress and changing circumstances in the economy and the world.

Budget Totals

Table 1 contains budget estimates and proposals for FY2003 and FY2004 from the Congressional Budget Office (CBO), the Administration (the Office of Management and Budget, OMB), the revisions produced by OMB and CBO throughout the year, and, as they become available, from congressional budget resolutions. Differences in totals occur because of differing underlying economic, technical, and budget-estimating assumptions and techniques as well as differences in policy assumptions. Most *policy* generated dollar differences between the Administration and congressional proposals or assumptions for an upcoming fiscal year are often relatively small compared to the budget as a whole. These small differences may grow, sometimes substantially, producing widely divergent budget paths over time. Budget estimates should be expected to change over time from those originally proposed by the President or Congress.

The terrorist attacks on the United States on September 11, 2001, the 2001 recession and the continuing economic uncertainty, changes from expected or proposed policies, and changes in the technical components of the underlying budget-economic relationships, all contributed to the large deterioration in the budget outlook over the last two years.

Table 1. Budget Estimates for FY2003 and FY2004
(in billions of dollars)

	Receipts	Outlays	Deficit(-)/ Surplus
Actual for FY2000	*$2,025*	*$1,789*	*$236*
Actual for FY2001	*1,991*	*1,864*	*127*
Actual for FY2002	*1,853*	*2,011*	*-158*
FY2003 Estimates in 2003			
CBO B&E Outlook, 1/31/03	1,922	2,121	-199
OMB, Budget, 2/3/03	1,836	2,140	-304
OMB, Budget, Current Services, 2/3/03	1,867	2,131	-264
CBO Revised Baseline, 3/7/03	1,891	2,137	-246
CBO Estimates of the President's Policies, 3/7/03	1,856	2,143	-287
House FY2004 Budget Resolution, 3/21/03	1,855	2,143	-288
Senate FY2004 Budget Resolution, 3/26/03	1,865	2,148	-282
Conference FY2004 Budget Resolution, 4/11/03	1,835	2,182	-347
OMB Mid-Session Review, 7/15/03	1,756	2,212	-455
OMB Mid-Session Review, Baseline, 7/15/03	1,756	2,210	-155
FY2004 Estimates			
CBO B&E Outlook, Baseline, 1/31/03	2,054	2,199	-145
OMB, Budget, 2/3/03	1,922	2,229	-307
OMB, Budget, Current Services, 2/3/03	2,031	2,189	-158
CBO Revised Baseline, 3/7/03	2,024	2,224	-200
CBO Estimates of the President's Policies, 3/7/03	1,907	2,245	-338
House FY2004 Budget Resolution, 3/21/03	1,908	2,232	-324
Senate FY2004 Budget Resolution, 3/26/03	1,958	2,246	-287
Conference FY2004 Budget Resolution, 4/11/03	1,883	2,268	-385
OMB Mid-Session Review, 7/15/03	1,797	2,272	-475
OMB Mid-Session Review, Baseline, 7/15/03	1,794	2,252	-458

B&E Outlook = The *Budget and Economic Outlook,* CBO.

Budget Proposals and Estimates

CBO's first budget report for FY2004, the *Budget and Economic Outlook: Fiscal Years 2004-2013* (January 2003), contained baseline estimates and projections for FY2003 through FY2013.[1] CBO's report showed that, under current policies, the budget remains in deficit through FY2006, when the deficit falls to $16 billion. The baseline projections show small surpluses beginning in FY2007 and growing rapidly in FY2011 through FY2013 as revenues rapidly grow with the scheduled expiration of the 2001 tax reductions from the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA; P.L. 107-16, June 2001).

President Bush's FY2004 budget called for additional tax cuts and both increased and decreased spending (as measured against baseline estimates) depending on the activity. The proposed policy changes increase the FY2004 deficit to $307 billion from OMB's baseline estimate of $158 billion. OMB's current service baseline estimates move into a small ($5 billion) surplus in FY2006 while the President's proposals produce a deficit of $201 billion in that year and keep the budget in deficit at least through FY2008, the last year of the Administration's estimates.[2]

The Administration's budget did not include any cost estimates for the (then future) war in Iraq, additions to homeland security funding, or for non-war defense related spending. On March 24, 2003, the President asked Congress for a $75 billion supplemental appropriation for FY2003, which increases outlays in FY2004.

The Administration argued that the tax cuts are needed to boost the lagging economy and that the acceleration of economic growth resulting from the tax cuts will lead to the recovery of much of the lost revenue over future years. The President's Council of Economic Advisors, in its annual report stated,

> Although the economy grows in response to tax reductions (because of higher consumption in the short run and improved incentives in the long run), it is unlikely to grow so much that lost tax revenue is completely recovered by the higher level of economic activity.[3]

Both OMB's and CBO's FY2004 budget documents were produced prior to the completion of final work on the FY2003 appropriations. This forced both agencies to estimate the (discretionary) spending levels Congress would approve and the President agree to for FY2003. This left the year-to-year comparison even more uncertain than it usually is.

CBO's March report, *An Analysis of the President's Budgetary Proposals for Fiscal Year 2004* (APBP) revised the CBO baseline (by incorporating the budgetary effects of the Consolidated Appropriations Resolution FY2003 (CAR 2003), P.L.

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[1] Baseline estimates provide a foundation from which to measure proposed policy changes. They extrapolate current policies into the future based on expectations of future economic conditions, other factors that affect the budget, and rules set by Congress that CBO must follow in creating baseline estimates. They are not meant to predict future budget outcomes.

[2] The long-run outlook for government policies existing in FY2003, that are found in the budget (p. 41), indicate that, without substantial changes from those policies, the budget remains in deficit through much of this century.

[3] Council of Economic Advisers, *Economic Report of the President*. Feb. 2003. pp. 57-58

108-7, February 20). The report reestimated the Administration's FY2004 budget proposal using CBO's assumptions and budget estimating methods.[4] CBO increased its own baseline deficits by $47 billion in FY2003 and by $55 billion in FY2004. CBO attributed $22 billion of the $55 billion increase in the deficit in FY2004 to legislative changes since January (almost all from the CAR 2003. The remainder of the change was attributed to technical changes.

Over the 10-year period covered in the March CBO report, CBO writes,

> For the 2004-2013 period, CBO has reduced its projection of the cumulative surplus by $446 billion [— dropping it from $1,336 billion to $891 billion —], nearly three-quarters of which derives from enactment of the omnibus appropriation act in February.[5]

The deterioration in the budget outlook since the January estimates also delayed, by one year, from FY2007 to FY2008, the expected date when CBO's baseline deficit would move into surplus.

CBO's estimates of the President's policies produced results similar to those in the President's budget, with little cumulative difference in the amounts generated. CBO estimated a cumulative deficit of $1.2 trillion under the President's policies over the five years (FY2004-FY2008) while the Administration estimated $1.1 trillion.[6] CBO's estimates of the Administration's proposals showed increasing deficits or eliminating surpluses compared to the revised CBO baseline in each of the 10 years covered. CBO estimated that about two-thirds of the increases in the deficits in its estimates of the President's proposals, excluding higher net interest, resulted from lower revenues (including the effect of the tax cuts proposed in the President's budget).

The House FY2004 budget resolution (H.Con.Res. 95) included, in its reconciliation instructions, the President's request for a $726 billion economic stimulus tax cut (only part of which was under reconciliation). The Senate-passed resolution (S.Con.Res. 23) contained reconciliation instructions for a $350 billion tax cut. The conference agreement on the resolution (H.Con.Res. 95; H.Rept. 108-71) included different reconciliation instructions for the House and Senate. The reconciliation instructions for the House included tax cuts of $550 billion; the reconciliation instructions for the Senate included tax cuts of $350 billion. The resolution had a $385 billion deficit in FY2004, becoming a small, $9.8 billion surplus in FY2012. (A $350 billion tax cut and spending increase reconciliation bill, H.R. 2, cleared Congress on May 23.)

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[4] The CBO report came out before the adoption of the FY2003 supplemental appropriations (P.L.108-11, April 6) and therefore did not include any effect the legislation will have on FY2004's outlays and deficit.

[5] Congressional Budget Office, *An Analysis of the President's Budgetary Proposals for FY2004*, March 2003, p. 3.

[6] Ibid., p. 1.

Uncertainty in Budget Projections

All budget estimates and projections are inherently uncertain. Their dependence on assumptions that are themselves subject to substantial variation over relatively short time periods makes budget estimates and projections susceptible to fairly rapid and dramatic changes. The last couple of years have demonstrated this volatility. The original proposals and estimates for FY2002, made in early 2001, changed drastically over the 20 to 21 months of congressional and presidential action on the budget. (The budget estimates for five to 10 years in the future that are included in the OMB and CBO budget documents are subject to even greater variability.) The early 2001 estimates for FY2002 estimated a *surplus* of $231 billion to $313 billion. The year ended on September 30, 2002 with a *deficit* of $158 billion. The September 2001 terrorist attacks on the United States, the legislation adopted in response, the bursting of the stock market bubble, the weak economy, and a shift in critical underlying budget relationships, all contributed to a large change in the year's budget outcome from the originally proposed or estimated amounts.

Information in chapter 5 (The Uncertainties of Budget Projections) of CBO's budget report, *The Budget and Economic Outlook: Fiscal Years 2004-2013* (January 2003), indicates how significantly the budget outcome can be altered by changes in economic and related technical factors that underpin the budget estimates. The chapter contains optimistic and pessimistic alternative scenarios for its baseline projection. The optimistic scenario assumes that the favorable economic and budget conditions of the late 1990s and 2000 recur. The pessimistic scenario assumes that the economy and the budget revert to the unfavorable conditions that prevailed in the 1970s and most of the 1980s.

The numbers in Table 2 are calculated from data in the January 2003 CBO budget report. The results reflect the wide range of possible budget outcomes with the same policies but different underlying assumptions about the economy and the relationship of the budget to the economy. The spread results from varying reasonable assumptions about future economic conditions and technical components that underlie the budget estimates.

The President's budget includes, in the section, "Charting a Course for the Federal Budget," the statement that "... five-year projections are fraught with uncertainty. The ... error in projecting the surplus or deficit since 1982 ... has been a $90 billion average absolute forecasting error for the first year alone. A 90-percent confidence range for 2008 would stretch all the way from a $281 billion surplus to a $661 billion deficit, a range of nearly $1 trillion."[7] The divergence expands as one moves further into the future.

[7] Office of Management and Budget. *Budget of the U.S. Government for FY2004*, Feb. 3, 2003, p. 28.

Table 2. CBO's Alternative Scenarios, Cumulative Surpluses/Deficits(-); FY2004-2008 and FY2004-2013
(in billions of dollars; January 31, 2003)

	FY2004-FY2008	FY2004-FY2013
CBO Optimistic Scenario Cumulative Surplus	$566	$4,490
CBO Baseline 1/31/03	-143	1,336
CBO Pessimistic Scenario Cumulative Deficit	-855	-1,856

Source: CBO, *The Budget and Economic Outlook: Fiscal Years 2004-2013*, Jan. 2003, p.106; CRS calculations.

Budget projections are very dependent on the underlying assumptions about the direction of the economy and future government policy and how these interact. Any deviation from the underlying assumptions used in the budget estimates, such as faster or slower economic growth, higher or lower inflation, differences from the existing or proposed spending and tax policies, or changes in the technical components of the budget models can, and usually do, have substantial effects on moving the budget outcomes away from the earlier budget estimates and projections.

Budget Action

CBO and the Administration released their first budget reports for the next fiscal year, FY2004, in late January and early February 2003. CBO's report provided baseline estimates for fiscal years 2003 through 2013. OMB's documents provided estimates for FY2004 through FY2008 with a few instances of estimates of cumulative amounts for fiscal years 2004 through FY2013 (these are limited to revenues and provide almost no data for the individual fiscal years after FY2008).

The Joint Committee on Taxation put out its estimates of the President's revenue provisions on March 4, 2003. In mid-March, CBO made available its report, *An Analysis of the President's Budgetary Proposals for FY2004*, which used the tax estimates of the Joint Committee on Taxation in its analysis.

The House and Senate Budget Committees adopted their own, differing, versions of the FY2004 budget resolution (H.Con.Res. 95; S.Con.Res. 23) in mid-March. The House, after the Republican leadership had to modify the committee-passed resolution to assure enough support for passage, passed (215-212) its version on March 21.

The Senate spent more than a week considering its resolution. After adopting and rejecting numerous amendments, the Senate adopted the resolution on March 26.[8] One of the amendments that was adopted limited the size of the tax-cut to $350

[8] The Senate substituted the text of its resolution, S.Con.Res. 23, for the text of the House-
(continued...)

billion (from the committee adopted level of $698 billion). The resolution moved to a conference committee April 1, 2003. The conference reported its agreement on April 10 (H.Rept. 108-71). The agreement included different tax cut reconciliation instructions for the House and Senate. The House reconciliation instructions would let it cut taxes (over 11 years) by up to $550 billion (down from the $726 billion in the House-passed resolution). The Senate reconciliation instructions limited it to tax cuts of $350 billion. Without other constraints, this would have allowed a $550 billion tax cut to emerge from a conference on the tax cut legislation. The $550 billion would have been protected from a Senate filibuster by the reconciliation rules. To make sure the budget resolution conference report could clear the Senate, the Senate leadership agreed that the eventual tax cut would not exceed $350 billion.

The House Ways and Means Committee reported the reconciliation tax cut legislation (H.R. 2; H.Rept. 108-94) on May 8. The legislation provided for the $550 billion tax cut included in the House version of the conference agreement on the budget resolution. The House passed the bill on May 9.

The Senate Finance Committee reported its *initial* version of the reconciliation tax cut (S. 2; no report) on May 9. Rules on reconciliation legislation sent the bill back to the Finance Committee. The Committee re-reported the legislation, now S. 1054 (again, no report) on May 13. The Senate adopted the legislation on May 15, after substituting the text of S. 1054 for that of H.R. 2.

On May 23, after extensive leadership negotiations between the House and Senate, an agreement was reached resolving the differences between the House- and Senate-passed versions of the reconciliation tax cut legislation. The agreement was formalized by the conference committee's report (H.Rept. 108-126) on May 22. The House adopted the agreement in the early morning hours of May 23. The Senate adopted it before noon on May 23. The agreement provided $350 billion in tax cuts and small spending increases through FY2013. The majority of the tax cuts expire at the end of calendar year 2004. The President signed the legislation into law (P.L. 108-27) on May 28.

Congress is currently working its way through the 13 regular appropriations for FY2004. As of July 16, 2003, the House had passed six; the Senate had passed two. Congress is expected to continue considering the appropriations through the summer.

Outlays

The Administration's FY2004 budget proposed $2,229 billion in outlays for FY2004, rising to $2,711 billion in FY2008, the last year forecast in the President's budget. The current services baseline in the President's budget (estimates of what future outlays would be if policies remained unchanged over the forecast period) showed outlays of $2,189 billion in FY2004 growing to $2,541 billion in FY2008.

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[8] (...continued)
passed resolution, H.Con.Res. 95.

Table 3. Outlays for FY2003-2008 and FY2013

(in billions of dollars)

	FY2002	FY2003	FY2004	FY2005	FY2006	FY2007	FY2008	FY2013
CBO Adjusted Baseline, 1/31/03	*$2,011* [a]	$2,121	$2,199	$2,298	$2,3878	$2,4795	$2,583	$3,167
President's F04 Budget, 2/3/03		2,140	2,229	2,343	2,464	2,576	2,711	—
President's FY04 Current Services, 2/3/03		2,131	2,189	2,276	2,348	2,440	2,541	—
CBO Revised Baseline, 3/03		2,137	2,224	2,328	2,417	2,513	2,621	3,215
CBO Est. of the President's Policies,3/03		2,143	2,245	2,370	2,491	2,606	2,739	3,452
House FY2004 Budget Resolution, 3/21/03		2,143	2,232	2,337	2,450	2,556	2,675	3,335
Senate FY2004 Budget Resolution,3/26/03		2,148	2,246	2,372	2,491	2,607	2,734	3,338
Conference FY2004 Budg. Res. 4/11/03		2,182	2,268	2,375	2,494	2,607	2,737	3,387
OMB MSR 7/15/03		2,212	2,272	2,338	2,452	2,573	2,706	—
OMB MSR, Baseline, 7/15/03		2,210	2,252	2,304	2,377	2,481	2,587	—

a. Actual outlays for FY2002.

The Administration's proposals would raise outlays $89 billion above the Administration's proposed FY2003 level and $40 billion above its FY2004 current services baseline outlay estimate. The dollar difference between the current services baseline outlay estimate for FY2004 and the outlay amount in the President's FY2004 proposal provides the cost of the Administration's proposed policy changes in FY2004. The change from FY2003 to FY2004 (the $89 billion increase) combines policy changes from one year to the next with relatively automatic growth in large parts of the budget. These automatic increases include cost-of-living adjustments, growth in populations eligible for program benefits, and inflation driven increases. The President's budget does not include estimated costs of any potential conflict with Iraq for either FY2003 or FY2004.

Total outlays, in the President's budget, were projected to grow at an average annual rate of 5.0% between FY2004 and FY2008. When the components of spending are examined, the budget functions showed the health budget function increasing at an annual average rate of 7.9%, the Medicare function increasing at an annual average rate of 7.8%, and net interest increasing at an annual average rate of 9.6% over these years.[9, 10] These three functions account for over 53% of the total outlay increase during this period. All of the other fifteen budget functions have a lower annual growth rate than that of total outlays.[11] The relatively low growth in

[9] Budget functions group, "budget data according to the major purpose served" rather than by agency or program. OMB, *Budget of the U.S. Government for FY2004, Analytical Perspectives*, p. 463.

[10] The Energy budget function has an even higher rate of increase, growing by an annual average rate of 18.3%, but since it only makes up 0.04% of total outlays in FY2004 and 0.07% of outlays in 2008, it therefore has little effect on the overall change in outlays.

[11] The two budget functions, "allowances", and "undistributed offsetting receipts", were (continued...)

some budget functions (agriculture 0.8%, education, training, employment, and social services 1.2%, general government 1.2%, and natural resources and environment 1.5%), growth that is lower than the expected rate of inflation, will reduce these functions' spending in real terms and as shares of total spending.

The CBO baseline, which assumed no changes from existing government policy, had FY2004 outlays of $2,298 billion, FY2008 outlays of $2,583 billion, and, because CBO's estimates extended through FY2013, FY2013 outlays of $3,167 billion.[12]

The revisions in CBO's March report raised estimated FY2004 outlays by $25 billion, to $2,224 billion (mostly because of the inclusion of the effects of adopting the Consolidated Appropriations Resolution, 2003 (P.L. 108-7)) in February. Each of the succeeding year's outlays in the CBO revisions were larger than they were in the February baseline. CBO's baseline outlays grow by an annual average rate of 4.2% between FY2004 and FY2008 (and by the same rate for the FY2004-FY2013 period). Total discretionary spending, including defense and homeland security, grows by approximately 2.5% a year over both the 5- and 10-year period. Mandatory spending, including Social Security and Medicare, would grow at average annual rates of 4.7% (FY2004-FY2008) and 5.4% (FY2004-FY2013). Because CBO's baseline shows the budget with a surplus starting in FY2008, net interest declines in the second five years after growing quickly in the first five years. Over the 10 years, net interest grows at an annual average of 1.5% (it grows at an average annual rate of 7.8% over the five years, FY2004-FY2008). If the deficits do not disappear, as they would not under the Administration's proposals, the net interest growth would not fall.

CBO's March reestimates of the President's proposals produced larger outlays than the President's proposals. They were $16 billion higher (to $2,245 billion) in FY2004. For FY2008, CBO's reestimates pushed total outlays to $2,739 billion (the Administration's number was $2,711 billion). For the years covered by the President's budget, CBO's reestimates raised outlays by $20 billion to $30 billion a year above the Administration's estimates. By FY2013, the Administration's outlay proposals, under the CBO reestimates, reached $3,279 billion.

The House- and Senate-passed budget resolutions contained different levels of spending for FY2004 and subsequent years and the differences in components of that spending. The House resolution had $2,232 billion in outlays for FY2004, while the Senate amount was $2,246 billion. By FY2013, the House resolution had outlays of $3,289 billion and the Senate resolution had outlays of $3,338 billion, not a very large difference over ten years. The House included instructions to cut spending in a wide selection of many mandatory programs, stating that there should be that much in "waste, fraud, and abuse" in the programs affected to avoid diminishing their

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[11] (...continued)
excluded from the total number of functions.

[12] Essentially followed the same rule used by the Administration's to produce its current services baseline estimates. CBO and OMB used different budget models and a number of different underlying assumptions

effectiveness. The Senate resolution had very constrained growth in non-defense, non-homeland security discretionary spending in the second five years of the period.

The conference report (H.Rept. 108-71) included outlays of $2,268 billion in FY2004 and $3,387 billion in FY2013. In addition, the conference agreement required most of the authorizing committees in the House and Senate to report the amount of "waste, fraud, and abuse" within the programs under their jurisdiction to their respective Budget Committees.

Receipts

The Administration's FY2004 budget included proposals to speed up and make permanent many of the tax changes enacted over the last two years. The Administration divided its revenue proposals over FY2004-FY2008 period into an economic growth package ($390 billion over FY2004-FY2008); tax incentives ($72 billion); tax simplification (which raises receipts by $13 billion); extending expiring tax provisions ($40 billion); and miscellaneous changes (which raise receipts by $2 billion). The total proposal would reduce revenues from current services baseline levels by $493 billion between FY2004 and FY2008 and by $1,461 billion between FY2004 and FY2013.[13]

The proposed changes would slow the growth in receipts but would not stop them. They grow from $1,922 billion in FY2004 to $2,521 billion in FY2008. The Administration claimed that the economic growth tax-cut proposals would speed economic growth by enough to recover some or all of the forgone revenue (a claim countered by CBO's March report that included dynamic macro-economic estimates, estimates that included the effects of the tax cuts on the economy in the budget estimates). None of the three budget models CBO used to calculate the tax-cut's effect on future revenues (or outlays) showed more than a minimal feed-back effect.

CBO's baseline estimates, using a somewhat different set of underlying assumptions than the Administration, estimated that FY2004 revenues will total $2,054 billion. The CBO estimates also assumed that the automatic expiration of the tax cuts of EGTRRA will occur at the end of 2010. The result is a large jump in revenues in the fiscal years after FY2010. CBO estimated that extending all the EGTRRA tax provisions that would otherwise expire before FY2013, would reduce cumulative revenues over the FY2004-2013 period by $785 billion (from cumulative

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[13] These estimate are from the Treasury's *General Explanations of the Administration's Fiscal Year 2004 Revenue Proposals*. The President's budget shows a $441 billion revenue reduction (from baseline estimates) for the FY2004-FY2008 period and a $1,307 billion reduction for the FY2004-FY2013 period. The Treasury's estimates were produced after the release of the President's budget and reflect adjustments to these estimates. See also the CRS Report RS21420, *President Bush's 2003 Tax Cut Proposal: A Brief Overview*, and the CRS Issue Brief IB10110, *Major Tax Issues in the 108th Congress* for more information on the proposals.

baseline revenues of $27,923 billion)[14]. The estimated effect of eliminating the expiring provisions of EGTRRA would be most dramatic after FY2010. In FY2010, the revenue reductions from baseline revenue estimates would be $32 billion; in FY2011 it would jump to $156 billion and in FY2013, to $260 billion.

Table 4. Receipts for FY2002-2008 and FY2013
(in billions of dollars)

	FY2002	FY2003	FY2004	FY2005	FY2006	FY2007	FY2008	FY2013
CBO Adjusted Baseline, 1/31/03	*$1,853* [a]	$1,922	$2,054	$2,225	$2,370	$2,505	$2,648	$3,674
President's F04 Budget, 2/3/03		1,836	1,922	2,135	2,263	2,398	2,521	—
President's FY04 Current Services 2/3/03		1,867	2,031	2,235	2,352	2,469	2,593	—
CBO Revised Baseline, 3/7/03		1,891	2,024	2,205	2,360	2,504	2,647	3,674
CBO Est. of the President's Policies,3/7/03		1,856	1,907	2,100	2,273	2,433	2,573	3,350
House FY2004 Budget Resolution, 3/21/03		1,855	1,908	2,107	2,282	2,444	2,587	3,372
Senate FY2004 Budget Resolution, 3/26/03		1,865	1,959	2,154	2,321	2,479	2,620	3,497
Conference FY2004 Budg. Res. 4/11/03		1,835	1,883	2,082	2,277	2,441	2,586	3,424
OMB MSR 7/15/03		1,756	1,797	2,033	2,215	2,360	2,480	—
OMB MSR, Baseline, 7/15/03		1,756	1,794	2,063	2,267	2,403	2,525	—

a. Actual receipts for FY2002.
NA = Not available

CBO's March 2003 revised estimates reduced CBO's baseline revenue estimates between FY2004 and FY2006, after which they equaled the January estimates. The CBO estimates of the President's proposals were lower than the revenues in the President's proposal over those same years. For FY2007 and FY2008, CBO's estimates of the President's proposed level of revenues exceed the President's proposed level.

The House (H.Con.Res.95) and Senate (S.Con.Res.23) budget resolutions included different reconciliation instructions. The House included an estimated $726 billion revenue reduction over 11 years, closely matching the President's tax cut proposals. The Senate included reconciliation instructions of not more than $350 billion. Much of the remainder of the President's tax proposal was incorporated in the resolution, but not under reconciliation. The conference on the budget resolution produced separate tax cut reconciliation instructions for the House Ways and Means Committee and the Senate Finance Committee. Reconciliation instructions required the Ways and Means Committee to reduce receipts by $550 billion ($535 billion in tax cuts and $15 in increased outlays). The Finance Committee was instructed to reduce taxes by no more than $350 billion.

Soon after the House adopted the conference report (H.Rept. 108-71) on the budget resolution (April 11), the Senate indicated that no eventual tax cut legislation

[14] This estimate does not include the larger interest payments resulting from the larger deficits or smaller surpluses occurring over this period that increases public debt.

exceeding $350 billion would be presented to the Senate. This indicated that the eventual conference on the tax cut would not include a tax cut larger than $350 billion. Any larger tax cut would be unlikely to clear the Senate. Many House members, expecting the larger tax cut amount ($550 billion) to eventually emerge from a conference committee on the tax cut legislation, were unhappy with the Senate's internal agreement.

The Committee on Ways and Means reported (H.Rept. 108-94) out the reconciliation bill, H.R. 2 (the Jobs and Growth Reconciliation Tax Act of 2003), worth $550 billion, including some increased outlays, on May 8. The House passed it on May 9. The Committee on Finance reported S. 2 (with no written report), its version of the reconciliation bill, on May 9. It contained revenue reductions of $350 billion (and some increases in outlays). Procedural issues required the Committee on Finance to report (again with no written report) a new bill (S. 1054) containing essentially the same contents as S. 2. The Committee reported the bill on May 13. The Senate, after substituting the text of S. 1054 for the text of H.R. 2, passed the $350 billion reconciliation bill on May 15.

On May 22, after extensive Republican leadership discussions over the reconciliation bill, a compromise was reached on a $350 reconciliation bill. The conference committee on the legislation endorsed the agreement and reported (H.Rept. 108-126) the modified H.R. 2 on May 22. The Housed passed the bill in the very early hours of May 23. The Senate passed the bill before noon on May 23. The President signed it into law (P.L. 108-27) on May 28.[15]

Deficits and Surpluses

Surpluses and deficits are the residuals left after Congress and the President set policies for spending and receipts. Surpluses reduce federal debt held by the public which leads to lower net interest payments; deficits increase government debt held by the public, increasing the government's net interest payments. 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) was a major focus of the budget debate in the late 1980s and throughout the 1990s. The President's FY2004 budget had a deficit of $307 billion in FY2004. CBO's reestimates of the President's proposals put it at $338 billion.

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[15] Most of the major provisions of the legislation are scheduled to expire after calendar year 2004 or, if not then, than after calendar year 2008. These expirations kept the total change from exceeding the $350 billion limit set by the agreement. Extending the provisions through 2013 would raise the estimated cost of the legislation to near $1 trillion over the 11 years.

Table 5. Surpluses/Deficits(-) for FY2004-FY2008 and FY2013
(in billions of dollars)

	FY2002	FY2003	FY2004	FY2005	FY2006	FY2007	FY2008	FY2013
CBO Adjusted Baseline, 1/31/03	*-$158* [a]	-$199	-$145	-$73	-$16	$26	$65	$508
President's F04 Budget, 2/3/03		-304	-307	-208	-201	-178	-190	—
President's FY04 Current Services 2/3/03		-264	-158	-40	5	29	51	—
CBO Revised Baseline, 3/7/03		-246	-200	-123	-57	-9	27	459
CBO Est. of the President's Policies,3/7/03		-287	-338	-270	-218	-173	-166	-102
House FY2004 Budget Resolution, 3/21/03		-288	-324	-230	-168	-111	-87	37
Senate FY2004 Budget Resolution, 3/26/03		-282	-287	-218	-169	-128	-114	159
Conference FY2004 Budg. Res. 4/11/03		-347	-385	-294	-217	-166	-151	37
OMB MSR 7/15/03		-455	-475	-304	-238	-213	-226	—
OMB MSR, Baseline, 7/15/03		-455	-458	-241	-110	-78	-62	—

a. Actual deficit for FY2002.

The Administration's Mid-Session Review (July 15, 2003; MSR) raised the FY2004 deficit estimate to $475 billion, without reflecting "what the Administration has previously indicated are expected but undetermined additional costs arising from the ongoing operations in Iraq, extending beyond 2003."[16] The MSR also showed that, if the Administration's current proposals are implemented, the budget would remain in deficit throughout the five years covered by the estimates, falling from $475 billion in FY2004 to $226 billion in FY2008. Under the February 2003 budget estimates, the deficit would have fallen slowly from $307 billion in FY2004 to $190 billion in FY2008. The Administration's February current services baseline, the estimate without policy change, had a deficit of $158 billion in FY2004, becoming a surplus of $51 billion in FY2008.

CBO's January baseline estimates had the budget returning to surplus in FY2007 and then growing through FY2013. CBO's March revisions increased the near-term deficits and slowed, by one year, the movement to surplus. The growth in the surplus, especially after FY2010, was boosted dramatically by the scheduled expiration of the 2001 tax cut.

The House Budget Committee's adopted budget resolution would move the budget into surplus in FY2010; the Senate Budget Committee's resolution would move the budget into surplus in FY2013. Both the House- and Senate-passed budget resolutions amended the two committees' resolutions and showed the budget moving back into surplus in FY2012.

The MSR current services baseline estimate is $458 billion for FY2004, falling to $62 billion in FY2008. The differences between these numbers and the policy

[16] OMB, *Mid-Session Review*, July 15, 2003, p.1.

driven numbers measures the cost of those policies, in this case a $506 billion cumulative increase in the deficit.

Over a longer period, one running far into the century, the Administration indicates that it expects, under existing policies and assumptions, large and continually growing deficits. The retirement of the baby boom generation, beginning in large numbers in the next decade, will rapidly drive up spending on Social Security, Medicare, and other programs for the elderly, increasing the deficit (or reducing the surplus, if there is one) and putting a severe strain on both the budget and the economy.

The Budget and the Economy

The budget and the economy affect each other. The relationship is an unequal one, with small economic changes having a more significant effect on the budget than large budget policy changes have on the economy. The worse-than-expected economic conditions over the last two years played a substantial role, directly or indirectly, in the deterioration of the budget outlook over those years.

The positive budget outlook forecast in early 2001 was substantially based on the favorable future economic conditions that were then expected. The positive outlook continued the overall improvement in the budget situation since the early 1990s. Much of this improvement had come from strong and sustained economic growth (and the rest from efforts to reduce the deficit and other changes). When those favorable economic conditions faltered, so did a significant portion of the positive budget outcomes of the previous few years. What good economic conditions give, bad economic conditions can take away. The unexpectedly lengthy economic weakness, the start of a recession in March 2001, the lengthy fall in the stock market, the policy responses to the September 2001 terrorist attacks, along with negative changes in the technical components of the budget estimates, raised outlays, reduced receipts, and eliminated the previously expected surpluses.

The FY2004 presidential budget documents and CBO's budget report included discussions of the expected economic outlook and the budget's sensitivity to changes in selected economic variables. Both reports include a table showing the budget's sensitivity to changes in selected economic variables (this year, it is found in chapter 2 of the *Analytical Perspectives* volume of the President's budget and in chapter 5 of CBO's report). The effects of the variables are generally symmetrical. A higher rate of real economic growth (than assumed in the budget proposal) has approximately the same effect on the budget as same-sized lower rate of economic growth has, but in the opposite direction. If a 1% lower rate of economic growth reduces the surplus (or increases the deficit) by $30 billion in FY2004 (from the OMB table; Table 2-6, p. 32, *The Budget of the United States Government, Fiscal Year 2004, Analytical Perspectives*), a 1% higher than expected rate of economic growth would reduce the deficit (or increase the surplus) by approximately $30 billion. Changes in other variables generally have a smaller effect on the budgetary balance than changes in real GDP. Sustained changes in the underlying economic variables tend to produce larger changes in the budget numbers than the effect of one or two year change.

Legislation

H.Con.Res. 95

The Concurrent Resolution on the Budget for Fiscal Year 2004. Adopted by the House Budget Committee (H.Rept. 108-37) on March 17, 2002, on a party-line vote after rejecting numerous amendments. It follows many of the proposals of the Administration. After some adjustments by the House leadership to assure passage, it was adopted by the House (215-212) on March 21. A conference agreement (H.Rept. 108-71) on the resolution cleared Congress on April 11.

S.Con.Res. 23

The Concurrent Resolution on the Budget for Fiscal Year 2004. Adopted by the Senate Budget Committee (no report but a committee print, S.Prt. 10-19) on March 14, 2002, on a party-line vote. As passed, the resolution included reconciliation instructions for approximately half of the President's economic stimulus tax cut proposal. The language of S.Con.Res. 23 was substituted for the contents of the House-passed resolution, H.Con.Res. 95.

H.R. 2

The Jobs and Growth Tax Relief Reconciliation Act of 2003. The legislation implemented the reconciliation instructions from the FY2004 budget resolution. It cleared the House on May 9, 2003. A modified version passed the Senate on May 15. After difficult negotiations between the House and Senate leadership, the conference agreement (H.Rept. 108-126) cleared Congress on May 23. The President signed the bill into law (P.L.108-27) on May 28. The legislation would cut taxes (and includes in that amount small outlay increases) by $350 billion.

For Additional Reading

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