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The President's Budget and the Return of Deficits

**by U.S. Representative John Spratt
Ranking Member, House Budget Committee**

President Bush came to the White House with an advantage few presidents have enjoyed: a budget in surplus. Looking out over ten years, his Office of Management and Budget predicted a surplus of \$5.6 trillion. A surplus so large seemed to suggest that we could have it all. We could do more for defense and more for education too, and still have room for big tax cuts. We could add drug coverage to Medicare and still save the Social Security surplus, using it to buy back some \$3.5 trillion in Treasury bonds held by the public.

In less than a year, \$4 trillion of the surplus has vanished, a result of tax cuts, terrorists, and recession. The President's budget for next year requests more tax cuts, \$675 billion over ten years, on top of the \$1.350 trillion in tax cuts passed last year. His budget also requests more for defense, \$520 billion more over ten years than needed to cover inflation. If implemented, the President's budget would take another trillion dollars off the ten-year surplus, leaving \$660 billion of the original \$5.6 trillion surplus, all of it coming from the Social Security trust fund. Rather than saving the Social Security surplus, the government will revert to borrowing and spending two-thirds of the surplus in the Social Security trust fund, or \$1.650 trillion, along with all \$556 billion of the surplus in the Medicare trust fund.

The understandable focus of the President's budget is national security, including a wholly new category called "homeland defense." In Congress, both Democrats and Republicans stand foursquare with the president, committed to pay whatever it takes to win the war on terrorism and to support our men and women in uniform. But without quibbling over the cost, we think it is fair to question whether this effort should be funded by borrowing from the Social Security and Medicare trust funds, particularly with 77 million baby boomers beginning to retire in 2008.

Turn to Table S-16 in the President's budget and you will find that, by the Administration's accounting, last year's tax cut is the largest cause of the depleted surplus. 23% of the surplus has disappeared due to the economy and 17% due to technical misjudgments in the original estimates. 18% has been taken up by legislation passed last year, dealing mostly with terrorism and homeland security. 43% of the decline in the surplus is due to the tax cut enacted last June.

This is a radical reversal, and as you might expect, there are impacts throughout the President's budget on state and local government. Here are a few examples:

Highways and Public Transportation

When Congress passed the Transportation Equity Act for the 21st Century (TEA-21), we adopted a new formula for remitting federal gasoline taxes to the states. As a result, South Carolina's pay-out from the highway trust fund has jumped from an average of about \$230 million a year under the Intermodal Surface Transportation Equity Act (ISTEA) to well over \$400 million under TEA-21. The highway trust fund is now feeling the recession. Receipts are off by nearly \$9 billion. The Bush Administration's budget makes no effort to replenish this short-fall from other revenues. The result for South Carolina depends on whom you ask, but most estimate a loss for our state of about \$110 million in highway funds, or about 25% of what the Department of Transportation will receive this year. Congress will try to make up that short-fall, but with a tight budget, we may not be able to replace the full amount.

Education

Over the past five years, Congress has raised appropriations for education by an average of 13% a year. The President's budget breaks from this trend and requests an increase for next year of only 2.8%. His budget seeks \$1 billion more for the Individuals with Disabilities Education Act (IDEA) and \$1 billion more for Title I, but offsets these increases by cuts in other titles of the Elementary and Secondary Education Act (ESEA) and by eliminating 28 programs.

In December, Congress and President Bush wrapped up a bi-partisan move to renew and rewrite ESEA. The Bush Administration proudly dubbed the new version "Leave No Child Behind." In passing the new ESEA, Congress authorized spending at a level of \$26.3 billion, largely to offset the costs of testing and remediation that the new law will impose on local school districts. The President's budget requests only \$22.1 billion, or \$4.2 billion less than the amount authorized by the bill he signed into law near the end of last year.

Community and Regional Development

The major programs and agencies that fall under this heading include the Federal Emergency Management Agency (FEMA), Community Development Block Grants, the Economic Development Administration, the Appalachian Regional Commission, rural development programs in the Department of Agriculture, the Small Business Administration's disaster loans, and Empowerment Zones.

FEMA: All of the President's budget requests under the heading of Community and Regional Development add up to \$14.7 billion. This is a \$2.7 billion increase over the level needed to maintain purchasing power at this year's level. But all of the increase stems from additional funding provided FEMA in the President's budget. The President's budget gives FEMA a hefty increase to fund homeland security, but then offsets the plus-up by cutting other community development programs.

The President's budget requests \$6.6 billion for FEMA, an increase of \$3.4 billion over the amount needed to maintain purchasing power at this year's level. This includes \$3.6 billion for

state and local terrorism preparedness, a \$3.2 billion increase over this year's level. The additional funding for preparedness goes toward grants to train and equip "first responders" to emergencies, which includes firefighters, police, and emergency medical technicians.

In a pattern that runs throughout this budget, the President cuts a number of other FEMA programs, discontinuing, for example, the federal subsidy for flood insurance on vacation homes in order to offset the additional funding for homeland security.

Community Development Block Grants (CDBGs): The President's budget requests \$4.7 billion for CDBGs, which is nearly \$400 million less than the level the Congressional Budget Office (CBO) says is needed to maintain purchasing power at this year's level.

Economic Development Administration: The President's budget requests \$317 million for the Economic Development Administration, \$24 million below the level needed to maintain purchasing power at this year's level.

Appalachian Regional Commission: The President's budget requests \$66 million for the Appalachian Regional Commission, or \$6 million less than the level needed, according to CBO, to maintain purchasing power at the 2002 level.

Rural Community Advancement: The President's budget provides \$791 million for the Rural Community Advancement program, a \$7 million cut below the level needed, according to CBO, to maintain purchasing power at the 2002 level.

Empowerment Zones: The President's budget includes no funding for urban or rural empowerment zones for 2003. Last year, urban empowerment zones received \$45 million in appropriated funds and rural empowerment zones received \$15 million in appropriated funds.

Law Enforcement

State and Local Law Enforcement Grants: The President's budget slightly increases funding for federal law enforcement programs, but substantially cuts state and local justice assistance. His budget requests \$752 million for state and local law enforcement assistance, which is a \$1.7 billion (or 69%) cut below the level needed to maintain purchasing power. The budget eliminates state and local law enforcement programs such as the State Criminal Alien Assistance Program, Edward Byrne formula and discretionary grants, and Local Law Enforcement Block Grants. It cuts programs such as the Violence Against Women Act Grants, Juvenile Incentive Block Grants, drug courts, and residential substance abuse treatment, and creates a new Justice Assistance Grant Program in Community Oriented Policing Services (COPS) to replace state and local law enforcement grants eliminated in the President's budget.

Community Oriented Policing Services (COPS): Community Oriented Policing Services is a Clinton Administration program that has offered grants to hire community police

officers. The Bush Administration's budget eliminates the traditional grants to hire and retrain new police officers, funded at \$330 million for 2002. The COPS budget would instead include a new Justice Assistance Grant Program, funded at \$800 million for 2003. Justice Assistance Grants would fund state and local law enforcement, prosecution, prevention, and corrections, with an earmark of \$60 million for Boys and Girls Clubs.

Other Programs

Land and Water Conservation Fund: Two years ago, when the budget began to show a surplus, Congress decided to dedicate revenues from off-shore drilling to the Land and Water Conservation Fund. Like last year, the President's budget claims to fully fund at \$900 million all the programs associated with the Land and Water Conservation Fund (LWCF). But, also like last year, his budget accomplishes this feat by using LWCF funding for programs not traditionally associated with it. Full funding would mean \$900 million split evenly between federal land acquisition and state land acquisition. In fact, the President's budget provides only \$486 million for the traditional purposes of the Fund, which is \$88 million less than last year and a lot less than Congress anticipated two years ago.

Social Services Block Grant (Title XX): The budget freezes funding for the Social Services Block Grant at the 2002 enacted level of \$1.7 billion. This grant provides states with broad discretion to use these funds for social services such as child care, child welfare, home-based services, employment services, adult protective services, prevention and intervention programs, and special services for the disabled.

LIHEAP: The budget cuts funding for the Low-Income Heating and Energy Assistance Program (LIHEAP) program by \$300 million (15 percent) compared with the 2002 enacted level, providing \$1.4 billion in regular and \$300 million in emergency funding. Because the entire \$300 million reduction comes out of regular LIHEAP funds (which fall from the 2002 enacted level of \$1.7 billion), the budget cuts these formula grants to states by 17.6 percent compared with the 2002 enacted level. South Carolina received \$11.4 million in 2002 and would lose some \$2 million in LIHEAP funds if the President's cut is enacted.

Child Care: The budget freezes funding for the Child Care and Development Fund at the 2002 enacted level of \$4.8 billion, providing \$2.1 billion in discretionary funding for the Child Care and Development Block Grant (CCDBG) and \$2.7 for mandatory child care programs. This cuts funding for CCDBG by \$40 million compared with CBO's estimate of the amount necessary to maintain purchasing power at the 2002 level in 2003. The budget freezes mandatory funding at the 2002 enacted level through 2012, eroding purchasing power further in each year.

Outlook

In only a year, the forecast of the budget has done an about-face and begun to back-slide into deficits reaching well into the future. The budget has been hit by recession and war, but long

after the economy has recovered, and, we hope, the war on terrorism has wound down, these deficits will persist unless there are major changes in the federal budget. Since national defense, Social Security, and Medicare often take priority in the budget over inter-governmental transfers, the consequences for state and local government could be significant.

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