BUDGET CONCEPTS AND BUDGET PROCESS

12. BUDGET CONCEPTS

The budget system of the United States Government provides the means for the President and the Congress to decide how much money to spend, what to spend it on, and how to raise the money they have decided to spend. Through the budget system, they determine the allocation of resources among the agencies of the Federal Government and between the Federal Government and the private sector. The budget system focuses primarily on dollars, but it also allocates other resources, such as Federal employment. The decisions made in the budget process affect the Nation as a whole, State and local governments, and individual Americans. Many budget decisions have worldwide significance. The Congress and the President enact budget decisions into law. The budget system ensures that these laws are carried out.

This chapter provides an overview of the budget system and explains some of the more important budget concepts. It includes summary dollar amounts to illustrate major concepts. Other chapters of the budget documents discuss these amounts and more detailed amounts in greater depth.

The following section discusses the budget process, covering formulation of the President's Budget, action by the Congress, and execution of enacted budget laws. The next section provides information on budget coverage, including a discussion of on-budget and off-budget amounts, functional classification, presentation of budget data, types of funds, and full-cost budgeting. Subsequent sections discuss the concepts of receipts and collections, budget authority, and outlays. These sections are followed by discussions of Federal credit; surpluses, deficits, and means of financing; Federal employment; and the basis for the budget figures. A glossary of budget terms appears at the end of the chapter.

Various laws, enacted to carry out requirements of the Constitution, govern the budget system. The chapter refers to the principal ones by title throughout the text and gives complete citations in the section just preceding the glossary.

THE BUDGET PROCESS

The budget process has three main phases, each of which is related to the others:

1. Formulation of the President's Budget;
2. Action by the Congress; and
3. Execution of enacted budget laws.

Formulation of the President's Budget

The Budget of the United States Government consists of several volumes that set forth the President's fiscal policy goals and priorities for the allocation of resources by the Government. The primary focus of the Budget is on the budget year—the next fiscal year for which the Congress needs to make appropriations, in this case 2012. (Fiscal year 2012 will begin on October 1, 2011, and end on September 30, 2012.) The Budget also covers the nine years following the budget year in order to reflect the effect of budget decisions over the longer term. It includes the funding levels provided for the current year, in this case 2011, which normally allows the reader to compare the President's Budget proposals with the most recently enacted levels. However, this year many programs and activities are operating under a continuing resolution that will expire on March 4, 2011 (see "Basis for Budget Figures" later in this chapter). The Budget also includes data on the most recently completed fiscal year, in this case 2010, so that the reader can compare budget estimates to actual accounting data.

In a normal year, the President begins the process of formulating the budget by establishing general budget and fiscal policy guidelines, usually by the spring of each year, at least nine months before the President transmits the budget to the Congress and at least 18 months before the fiscal year begins. (See the "Budget Calendar" later in this chapter.) Based on these guidelines, the Office of Management and Budget (OMB) works with the Federal agencies to establish specific policy directions and planning levels, both for the budget year and for at least the following four years, and in this case, the following nine years, to guide the preparation of their budget requests.

During the formulation of the budget, the President, the Director of OMB, and other officials in the Executive Office of the President continually exchange information, proposals, and evaluations bearing on policy decisions with the Secretaries of the departments and the heads of the other Government agencies. Decisions reflected in previously enacted budgets, including the one for the fiscal year in progress, reactions to the last proposed budget (which the Congress is considering at the same time the process of preparing the forthcoming budget begins), and evaluations of program performance all influence decisions concerning the forthcoming budget, as do projections of the economic outlook, prepared jointly by the Council of Economic Advisers, OMB, and the Treasury Department.

In early fall, agencies submit their budget requests to OMB, where analysts review them and identify issues

that OMB officials need to discuss with the agencies. OMB and the agencies resolve many issues themselves. Others require the involvement of White House policy officials and the President. This decision-making process is usually completed by late December. At that time, the final stage of developing detailed budget data and the preparation of the budget documents begins.

The decision-makers must consider the effects of economic and technical assumptions on the budget estimates. Interest rates, economic growth, the rate of inflation, the unemployment rate, and the number of people eligible for various benefit programs, among other factors, affect Government spending and receipts. Small changes in these assumptions can alter budget estimates by many billions of dollars. (Chapter 2, "Economic Assumptions," provides more information on this subject.)

Thus, the budget formulation process involves the simultaneous consideration of the resource needs of individual programs, the allocation of resources among the agencies and functions of the Federal Government, and the total outlays and receipts that are appropriate in light of current and prospective economic conditions.

The law governing the President's budget requires its transmittal to the Congress on or after the first Monday in January but not later than the first Monday in February of each year for the following fiscal year, which begins on October 1. The budget is routinely sent to the Congress on the first Monday in February, giving the Congress eight months to act on the budget before the fiscal year begins.

Congressional Action [1]

The Congress considers the President's budget proposals and approves, modifies, or disapproves them. It can change funding levels, eliminate programs, or add programs not requested by the President. It can add or eliminate taxes and other sources of receipts or make other changes that affect the amount of receipts collected.

The Congress does not enact a budget as such. Through the process of adopting a planning document called a budget resolution (described below), the Congress agrees on targets for total spending and receipts, the size of the deficit or surplus, and the debt limit. The budget resolution provides the framework within which individual congressional committees prepare appropriations bills and other spending and receipts legislation. The Congress provides spending authority—funding—for specified purposes in appropriations acts each year. It also enacts changes each year in other laws that affect spending and receipts. Both appropriations acts and these other laws are discussed in the following paragraphs.

In making appropriations, the Congress does not vote on the level of outlays (spending) directly, but rather on budget authority, or funding, which is the authority provided by law to incur financial obligations that will result in outlays. In a separate process, prior to making appropriations, the Congress usually enacts legislation that authorizes an agency to carry out particular programs, authorizes the appropriations of funds to carry out those programs, and, in some cases, limits the amount that can be appropriated for the programs. Some authorizing legislation expires after one year, some expires after a specified number of years, and some is permanent. The Congress may enact appropriations for a program even though there is no specific authorization for it or its authorization has expired.

The Congress begins its work on its budget resolution shortly after it receives the President's budget. Under the procedures established by the Congressional Budget Act of 1974, the Congress decides on budget targets before commencing action on individual appropriations.

[1] For a fuller discussion of the congressional budget process, see Bill Heniff Jr., Introduction to the Federal Budget Process (Congressional Research Service Report 98–721), and Robert Keith and Allen Schick, Manual on the Federal Budget Process (Congressional Research Service Report 98–720, archived).

BUDGET CALENDAR

The following timetable highlights the scheduled dates for significant budget events during a normal budget year:

Date	Event
Between the 1st Monday in January and the 1st Monday in February	President transmits the budget
Six weeks later	Congressional committees report budget estimates to the Budget Committees
April 15	Action to be completed on congressional budget resolution
May 15	House consideration of annual appropriations bills may begin even if the budget resolution has not been agreed to.
June 10	House Appropriations Committee to report the last of its annual appropriations bills.
June 15	Action to be completed on "reconciliation bill" by the Congress.
June 30	Action on appropriations to be completed by the House
July 15	President transmits Mid-Session Review of the Budget
October 1	Fiscal year begins

The Act requires each standing committee of the House and Senate to recommend budget levels and report legislative plans concerning matters within the committee's jurisdiction to the Budget Committee in each body. The House and Senate Budget Committees then each design and report, and each body then considers, a concurrent resolution on the budget—a congressional budget plan, or budget resolution. The budget resolution sets targets for total receipts and for budget authority and outlays, both in total and by functional category (see "Functional Classification" later in this chapter). It also sets targets for the budget deficit or surplus and for Federal debt subject to statutory limit.

The congressional timetable calls for the House and Senate to resolve differences between their respective versions of the congressional budget resolution and adopt a single budget resolution by April 15 of each year.

In the report on the budget resolution, the Budget Committees allocate the total on-budget budget authority and outlays set forth in the resolution to the Appropriations Committees and the other committees that have jurisdiction over spending. (See "Coverage of the Budget," later in this chapter, for more information on on-budget and off-budget amounts.) Once the Congress resolves differences between the House and Senate and agrees on a budget resolution, the Appropriations Committees are required to divide their allocations of budget authority and outlays among their subcommittees. The Congress is not allowed to consider appropriations bills (so-called "discretionary" spending) that would breach or further breach an Appropriations subcommittee's target. The Congress is not allowed to consider legislation that would cause the overall spending target for any such committee to be breached or further breached. The Budget Committees' reports may discuss assumptions about the level of funding for major programs. While these assumptions do not bind the other committees and subcommittees, they may influence their decisions.

The budget resolution may also contain "reconciliation directives" (discussed below) to the committees responsible for tax laws and for mandatory spending—programs not controlled by annual appropriation acts—in order to conform the level of receipts and this type of spending to the targets in the budget resolution.

Since the concurrent resolution on the budget is not a law, it does not require the President's approval. However, the Congress considers the President's views in preparing budget resolutions, because legislation developed to meet congressional budget allocations does require the President's approval. In some years, the President and the joint leadership of Congress have formally agreed on plans to reduce the deficit or balance the budget. These agreements were then reflected in the budget resolution and legislation passed for those years.

Once the Congress approves the budget resolution, it turns its attention to enacting appropriations bills and authorizing legislation. Appropriations bills are initiated in the House. They provide the budgetary resources for the majority of Federal programs, but only a minority of Federal spending. The Appropriations Committee in each body has jurisdiction over annual appropriations. These committees are divided into subcommittees that hold hearings and review detailed budget justification materials prepared by the Executive Branch agencies within the subcommittee's jurisdiction. After a bill has been drafted by a subcommittee, the full committee and the whole House, in turn, must approve the bill, sometimes with amendments to the original version. The House then forwards the bill to the Senate, where a similar review follows. If the Senate disagrees with the House on particular matters in the bill, which is often the case, the two bodies form a conference committee (consisting of some Members of each body) to resolve the differences. The conference committee revises the bill and returns it to both bodies for approval. When the revised bill is agreed to, first in the House and then in the Senate, the Congress sends it to the President for approval or veto.

Since 1977, when the start of the fiscal year was established as October 1, there have been only three fiscal years (1989, 1995, and 1997) for which the Congress agreed to every appropriations bill by that date. When one or more appropriations bills has not been agreed to by this date, Congress usually enacts a joint resolution called a "continuing resolution," (CR) which is an interim or stopgap appropriations bill that provides authority for the affected agencies to continue operations at some specified level until a specific date or until the regular appropriations are enacted. Occasionally, a CR has funded a portion or all of the Government for the entire year.

The Congress must present these CRs to the President for approval or veto. In some cases, Presidents have rejected CRs because they contained unacceptable provisions. Left without funds, Government agencies were required by law to shut down operations—with exceptions for some activities—until the Congress passed a CR the President would approve. Shutdowns have lasted for periods of a day to several weeks.

The Congress also provides budget authority in laws other than appropriations acts. In fact, while annual appropriations acts fund the majority of Federal programs, they account for only about a third of the total spending in a typical year. Authorizing legislation controls the rest of the spending, which is commonly called "mandatory spending." A distinctive feature of these authorizing laws is that they provide agencies with the authority or requirement to spend money without first requiring the Appropriations Committees to enact funding. This category of spending includes interest the Government pays on the public debt and the spending of several major programs, such as Social Security, Medicare, Medicaid, unemployment insurance, and Federal employee retirement. This chapter discusses the control of budget authority and outlays in greater detail under "Budget Authority and Other Budgetary Resources, Obligations, and Outlays."

Almost all taxes and most other receipts also result from authorizing laws. Article I, Section 7, of the Constitution provides that all bills for raising revenue shall originate in the House of Representatives. In the House, the Ways and Means Committee initiates tax bills; in the Senate, the Finance Committee has jurisdiction over tax laws.

The budget resolution often includes reconciliation directives, which require authorizing committees to change laws that affect receipts or mandatory spending. It directs each designated committee to report amendments to the laws under the committee's jurisdiction that would achieve changes in the levels of receipts or reductions in mandatory spending controlled by those laws. These directives specify the dollar amount of changes that each designated committee is expected to achieve, but do not specify which laws are to be changed or the changes to be made. However, the Budget Committees' reports on the budget resolution frequently discuss assumptions about how the laws would be changed. Like other assumptions in the report, they do not bind the committees of jurisdiction but may influence their decisions. A reconciliation instruction may also specify the total amount by which the statutory limit on the public debt is to be changed.

The committees subject to reconciliation directives draft the implementing legislation. Such legislation may, for example, change the tax code, revise benefit formulas or eligibility requirements for benefit programs, or authorize Government agencies to charge fees to cover some of their costs. Reconciliation bills are typically omnibus legislation, combining the legislation submitted by each reconciled committee in a single act.

Such a large and complicated bill would be difficult to enact under normal legislative procedures because it usually involves changes to tax rates or to popular social programs, generally to reduce projected deficits. The Senate considers such omnibus reconciliation acts under expedited procedures that limit total debate on the bill. To offset the procedural advantage gained by expedited procedures, the Senate places significant restrictions on the substantive content of the reconciliation measure itself, as well as on amendments to the measure. Any material in the bill that is extraneous or that contains changes to the Federal Old-Age and Survivors Insurance and the Federal Disability Insurance programs is not in order under the Senate's expedited reconciliation procedures. Non-germane amendments are also prohibited. In addition, the Senate does not allow reconciliation bills as a whole to increase projected deficits or reduce projected surpluses. This Senate prohibition complements the Statutory Pay-As-You-Go Act of 2010, discussed below. The House does not allow reconciliation bills to increase mandatory spending in net, but does allow such bills to increase deficits by reducing revenues. See "Budget Enforcement" later in this chapter for a description of the House special order that permits the Budget Committee Chairman to certify that the costs of certain types of legislation are zero.

Reconciliation acts, together with appropriations acts for the year, are usually used to implement broad agreements between the President and the Congress on those occasions where the two branches have negotiated a comprehensive budget plan. Reconciliation acts have sometimes included other matters, such as laws providing the means for enforcing these agreements, as described under "Budget Enforcement."

Budget Enforcement

The Budget Enforcement Act (BEA), first enacted in 1990 and extended in 1993 and 1997, significantly amended the Balanced Budget and Emergency Deficit Control Act (BBEDCA) and other laws pertaining to the budget process. The BEA divided spending into two types—discretionary spending and direct or mandatory spending. Discretionary spending is controlled through annual appropriations acts. Funding for salaries and other operating expenses of government agencies, for example, is generally discretionary because it is usually provided by appropriations acts. Direct spending is more commonly called mandatory spending. Mandatory spending is controlled by permanent laws. Medicare and Medicaid payments, unemployment insurance benefits, and farm price supports are examples of mandatory spending, because permanent laws authorize payments for those purposes. The BEA applied a statutory pay-as-you-go (PAYGO) process to mandatory spending and revenue legislation and discretionary spending limits ("caps") to annual appropriations acts, but these enforcement provisions expired at the end of fiscal year 2002. Chapter 24, "Budget System and Concepts and Glossary," pages 460-461 in the *Analytical Perspectives* volume of the 2004 Budget, discusses the Budget Enforcement Act in more detail.

The Statutory Pay-As-You-Go Act of 2010, enacted on February 12, 2010, amended BBEDCA and reestablished a statutory procedure to enforce a rule of budget neutrality on new revenue and mandatory spending legislation. Unlike BBEDCA, the Statutory Pay-As-You-Go Act of 2010 applies to mandatory spending and revenue only and does not impose any enforcement regime on discretionary spending provided in appropriations acts. However, the allocations to the Appropriations Committees of discretionary amounts assumed in annual budget resolutions function as discretionary caps, which the Congressional Budget Act enforces by providing for points of order in the House of Representatives and the Senate.

The Statutory Pay-As-You-Go Act of 2010, which is a permanent law, requires that the cumulative effect of all new legislation changing governmental receipts or mandatory spending or collections must not increase projected on-budget deficits. PAYGO requires that bills reducing revenues must be fully offset by cuts in mandatory programs or by revenue increases. It also requires that any bills increasing mandatory expenditures must be fully offset by revenue increases or cuts in mandatory programs. This requirement is enforced by a process, known as "sequestration" which requires automatic across-the-board cuts in selected mandatory programs in the event that legislation taken as a whole does not meet the PAYGO standard established by the law. The law establishes special scorecards and scorekeeping rules. Under the 1990s PAYGO law, the threat of sequestration proved sufficient to ensure compliance. In that respect, sequestration can better be viewed as an incentive for compliance than a remedy for noncompliance.

The budgetary effects of revenue and direct spending provisions, including both costs and savings, are recorded

by OMB on two PAYGO scorecards in which costs or savings are averaged over rolling five-year and 10-year periods. As a general rule, the budgetary effects of PAYGO measures are determined by statements inserted into the *Congressional Record* by the chairmen of the House and Senate Budget Committees. These statements reflect the estimates of the Budget Committees, which are usually informed by cost estimates prepared by the Congressional Budget Office. If this procedure is not followed, then the budgetary effects of the legislation are determined by OMB.

After a congressional session ends, OMB determines whether a violation of the PAYGO requirement has occurred. If there are more costs than savings on the scorecard, the President is required to issue a sequestration order implementing across-the-board cuts to a select group of nonexempt mandatory programs in an amount sufficient to offset the net costs on the PAYGO scorecard.

The Statutory Pay-As-You-Go Act of 2010 exempts the costs of certain legislation from the PAYGO scorecard. Permanent extension of the middle-class provisions of the 2001 and 2003 tax cuts, as amended in 2009, do not have to be offset. In addition, extension through 2014 of the costs of providing relief from the scheduled deep reduction in Medicare physician reimbursement rates is also exempt from PAYGO, but only up to the reimbursement rates in effect in 2009. However any fixes to the scheduled reduction in reimbursement rates after December 31, 2014 are to be scored relative to current law. In three bills between June and December of 2010, the Congress enacted temporary relief to the Sustainable Growth Rate (SGR) provision of Medicare at payment rates 2.2 percent above those defined in the Statutory Pay-As-You-Go Act of 2010, so those incremental costs appear on the PAYGO scorecards. Congress chose to offset the entire costs of the relief, even though such offsets were not required.

In addition, if Congress designates a provision of mandatory spending or receipts legislation as an emergency requirement, the effect of the provision is not scored as PAYGO.

The PAYGO rules also apply to the outlays resulting from changes in outyear budget authority for mandatory programs made in appropriations acts and to all revenue changes made in appropriations acts. Provisions with zero net outlay effects over the sum of the current year and the next five fiscal years are not considered PAYGO. The PAYGO rules do not apply to increases in mandatory spending or decreases in receipts that result automatically under existing law. For example, mandatory spending for benefit programs, such as unemployment insurance, rises when the population of eligible beneficiaries rises, and many benefit payments are automatically increased for inflation under existing laws. Additional information on the Statutory Pay-As-You-Go Act of 2010 can be found on OMB's website at: *www.whitehouse.gov/omb/paygo_description.*

The Senate imposes points of order against consideration of tax or mandatory spending legislation that would violate the PAYGO principle, although the time periods covered by the Senate's rule and the treatment of previously enacted costs or savings may differ in some respects from the requirements of the Statutory Pay-As-You-Go Act of 2010.

The House, in contrast, imposes points of order on legislation increasing mandatory spending in net, whether or not those costs are offset by revenue increases, but the House rule does not constrain the size of tax cuts or require them to be offset. On January 5, 2011, the House agreed to a special order that permits the Budget Committee Chairman to certify that the costs of certain types of legislation are zero when introducing pay-as-you-go estimates into the Congressional Record:

- Repeal of the Affordable Care Act.
- Extension of EGTRRA and JGTRRA.
- Extension of AMT relief and estate tax repeal.
- Creation of a 20 percent deduction in income to small businesses.
- Enactment of legislation implementing trade agreements.

Budget Execution

The Senate imposes points of order against consideration of tax or mandatory spending legislation that would violate the PAYGO principle, although the time periods covered by the Senate's rule and the treatment of previously enacted costs or savings may differ in some respects from the requirements of the Statutory Pay-As-You-Go Act of 2010. The House, in contrast, imposes points of order on legislation increasing mandatory spending in net, whether or not those costs are offset by revenue increases, but the House rule does not constrain the size of tax cuts or require them to be offset.

Government agencies may not spend or obligate more than the Congress has appropriated, and they may use funds only for purposes specified in law. The Antideficiency Act prohibits them from spending or obligating the Government to spend in advance of an appropriation, unless specific authority to do so has been provided in law. Additionally, the Act requires the President to apportion the budgetary resources available for most executive branch agencies. The President has delegated this authority to OMB. Some apportionments are by time periods (usually by quarter of the fiscal year), some are by projects or activities, and others are by a combination of both. Agencies may request OMB to reapportion funds during the year to accommodate changing circumstances. This system helps to ensure that funds do not run out before the end of the fiscal year.

During the budget execution phase, the Government sometimes finds that it needs more funding than the Congress has appropriated for the fiscal year because of unanticipated circumstances. For example, more might be needed to respond to a severe natural disaster. Under such circumstances, the Congress may enact a supplemental appropriation.

On the other hand, the President may propose to reduce a previously enacted appropriation. The President may propose to either "cancel" or "rescind" the amount. If the President initiates the withholding of funds while

the Congress considers his request, the amounts are apportioned as "deferred" or "withheld pending rescission" on the OMB-approved apportionment form. Agencies are instructed not to withhold funds without the prior approval of OMB. When OMB approves a withholding, the Impoundment Control Act requires that the President transmit a "special message" to the Congress. The historical reason for the special message is to inform the Congress that the President has unilaterally withheld funds that were enacted in regular appropriations acts. The notification allows the Congress to consider the proposed rescission in a timely way. The last time the President initiated the withholding of funds was in fiscal year 2000.

COVERAGE OF THE BUDGET

Federal Government and Budget Totals

The budget documents provide information on all Federal agencies and programs. However, because the laws governing Social Security (the Federal Old-Age and Survivors Insurance and the Federal Disability Insurance trust funds) and the Postal Service Fund require that the receipts and outlays for those activities be excluded from the budget totals and from the calculation of the deficit or surplus, the budget presents on-budget and off-budget totals. The off-budget totals include the Federal transactions excluded by law from the budget totals. The on-budget and off-budget amounts are added together to derive the totals for the Federal Government. These are sometimes referred to as the unified or consolidated budget totals.

It is not always obvious whether a transaction or activity should be included in the budget; the dividing line between the Government and the private sector is sometimes murky. Where there is a question, OMB normally follows the recommendation of the 1967 President's Commission on Budget Concepts to be comprehensive of the full range of Federal agencies, programs, and activities. In recent years, for example, the budget has included the transactions of the Universal Service Fund, the Public Company Accounting Oversight Board, the Securities Investor Protection Corporation, Guaranty Agencies Reserves, the National Railroad Retirement Investment Trust, the United Mine Workers Combined Benefits Fund, the Telecommunications Development Fund, the Federal Financial Institutions Examination Council, and the transactions of Electric Reliability Organizations (EROs) established pursuant to the Energy Policy Act of 2005. This year, the budget includes the transactions of the Corporation for Travel Promotion, which was created pursuant to the Travel Promotion Act of 2009.

The budget also classifies as governmental the collections and spending by the Affordable Housing Program (AHP) funds created by the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) and includes them in the budget totals. FIRREA requires each of the 12 Federal Home Loan Banks (FHLBs) to contribute at least 10 percent of its previous year's net earnings to an AHP fund to be used to subsidize owner-occupied and rental housing for low-income families and individuals and to provide assistance to certain first-time homebuyers. Since 1990, the FHLBs have contributed $3.7 billion to the AHP funds, of which $2.9 billion has been spent. The unspent funds represent 2010 contributions that will be committed in 2011 and the undisbursed portion of funds already committed to specific projects. Although the funds remain in the possession of the FHLBs, the deposit of specific amounts into the AHP funds is compulsory, and the expenditures are to meet specific governmental purposes.

Table 12–1. TOTALS FOR THE BUDGET AND THE FEDERAL GOVERNMENT
(In billions of dollars)

	2010 Actual	Estimate	
		2011	2012
Budget authority			
Unified	3,485	3,651	3,685
On-budget	2,929	3,143	3,093
Off-budget	555	507	592
Receipts:			
Unified	2,163	2,174	2,627
On-budget	1,531	1,614	1,969
Off-budget	632	559	659
Outlays:			
Unified	3,456	3,819	3,729
On-budget	2,902	3,317	3,146
Off-budget	555	502	583
Deficit (-) / Surplus (+):			
Unified	–1,293	–1,645	–1,101
On-budget	–1,370	–1,703	–1,177
Off-budget	77	58	76

In contrast, the budget excludes tribal trust funds that are owned by Indian tribes and held and managed by the Government in a fiduciary capacity on the tribes' behalf. These funds are not owned by the Government, the Government is not the source of their capital, and the Government's control is limited to the exercise of fiduciary duties. Similarly, the transactions of Government-sponsored enterprises, such as the FHLBs, are not included in the on-budget or off-budget totals. Federal laws established these enterprises for public policy purposes, but they are privately owned and operated corporations. Nevertheless, because of their public charters, the budget discusses them and reports summary financial data in the budget *Appendix* and in some detailed tables.

The budget also excludes the revenues from copyright royalties and spending for subsequent payments to copyright holders where (1) the law allows copyright owners and users to voluntarily set the rate paid for the use of

protected material, and (2) the amount paid by users of copyrighted material to copyright owners is related to the frequency or quantity of the material used. This year, the budget will exclude license royalties collected and paid out by the Copyright Office for the retransmission of network broadcasts via cable collected under 17 U.S.C. 111 because these revenues meet both of these conditions. The budget will continue to include the royalties collected and paid out for license fees for digital audio recording technology under 17 U.S.C. 1004, since the amount of license fees paid is unrelated to usage of the material.

The *Appendix* includes a presentation for the Board of Governors of the Federal Reserve System for information only. The amounts are not included in either the on-budget or off-budget totals because of the independent status of the System within the Government. However, the Federal Reserve System transfers its net earnings to the Treasury, and the budget records them as receipts.

Chapter 13 of this volume, "Coverage of the Budget," provides more information on this subject.

Functional Classification

The functional classification is used to array budget authority, outlays, and other budget data according to the major purpose served—such as agriculture, transportation, income security, and national defense. There are 19 major functions, most of which are divided into subfunctions. For example, the Agriculture function comprises the subfunctions Farm Income Stabilization and Agricultural Research and Services. The functional array meets the Congressional Budget Act requirement for a presentation in the budget by national needs and agency missions and programs.

The following criteria are used in establishing functional categories and assigning activities to them:

- A function encompasses activities with similar purposes, emphasizing what the Federal Government seeks to accomplish rather than the means of accomplishment, the objects purchased, the clientele or geographic area served (except in the cases of functions 570 for Medicare, 650 for Social Security, and 700 for Veterans Benefits and Services), or the Federal agency conducting the activity (except in the case of subfunction 051 in the National Defense function, which is used only for defense activities under the Department of Defense—Military).
- A function must be of continuing national importance, and the amounts attributable to it must be significant.
- Each basic unit being classified (generally the appropriation or fund account) usually is classified according to its primary purpose and assigned to only one subfunction. However, some large accounts that serve more than one major purpose are subdivided into two or more functions or subfunctions.

Detailed functional tables, which provide information on Government activities by function and subfunction, are available on the Internet and as a CD-ROM included with the printed document.

Agencies, Accounts, Programs, Projects, and Activities

Various summary tables in the *Analytical Perspectives* volume of the Budget provide information on budget authority, outlays, and offsetting collections and receipts arrayed by Federal agency. A table that lists budget authority and outlays by budget account within each agency and the totals for each agency of budget authority, outlays, and receipts that offset the agency spending totals is available on the Internet and as a CD-ROM included with the printed document. The *Appendix* provides budgetary, financial, and descriptive information about programs, projects, and activities by account within each agency.

Types of Funds

Agency activities are financed through Federal funds and trust funds.

Federal funds comprise several types of funds. Receipt accounts of the ***general fund***, which is the greater part of the budget, record receipts not earmarked by law for a specific purpose, such as income tax receipts. The general fund also includes the proceeds of general borrowing. General fund appropriations accounts record general fund expenditures. General fund appropriations draw from general fund receipts and borrowing collectively and, therefore, are not specifically linked to receipt accounts. ***Special funds*** consist of receipt accounts for Federal fund receipts that laws have designated for specific purposes and the associated appropriation accounts for the expenditure of those receipts. ***Public enterprise funds*** are revolving funds used for programs authorized by law to conduct a cycle of business-type operations, primarily with the public, in which outlays generate collections.

Intragovernmental funds are revolving funds that conduct business-type operations primarily within and between Government agencies. The collections and the outlays of revolving funds are recorded in the same budget account. This year, the budget reclassifies as discretionary about 12 working capital and franchise funds that purchase goods and services for discretionary accounts. The majority of such funds were already classified as discretionary. As a result of this change, all of these funds will be classified in the same manner.

Trust funds account for the receipt and expenditure of monies by the Government for carrying out specific purposes and programs in accordance with the terms of a statute that designates the fund as a trust fund (such as the Highway Trust Fund) or for carrying out the stipulations of a trust where the Government itself is the beneficiary (such as any of several trust funds for gifts and donations for specific purposes). ***Trust revolving funds***

are trust funds credited with collections earmarked by law to carry out a cycle of business-type operations.

The Federal budget meaning of the term “trust,” as applied to trust fund accounts, differs significantly from its private-sector usage. In the private sector, the beneficiary of a trust usually owns the trust’s assets, which are managed by a trustee who must follow the stipulations of the trust. In contrast, the Federal Government owns the assets of most Federal trust funds, and it can raise or lower future trust fund collections and payments, or change the purposes for which the collections are used, by changing existing laws. There is no substantive difference between a trust fund and a special fund or between a trust revolving fund and a public enterprise revolving fund.

However, in some instances, the Government does act as a true trustee of assets that are owned or held for the benefit of others. For example, it maintains accounts on behalf of individual Federal employees in the Thrift Savings Fund, investing them as directed by the individual employee. The Government accounts for such funds in ***deposit funds***, which are not included in the budget. (Chapter 28 of this volume, “Trust Funds and Federal Funds,” provides more information on this subject.)

Budgeting for Full Costs

A budget is a financial plan for allocating resources—deciding how much the Federal Government should spend in total, program by program, and for the parts of each program and deciding how to finance the spending. The budgetary system provides a process for proposing policies, making decisions, implementing them, and reporting the results. The budget needs to measure costs accurately so that decision makers can compare the cost of a program with its benefits, the cost of one program with another, and the cost of one method of reaching a specified goal with another. These costs need to be fully included in the budget up front, when the spending decision is made, so that executive and congressional decision makers have the information and the incentive to take the total costs into account when setting priorities.

The budget includes all types of spending, including both current operating expenditures and capital investment, and to the extent possible, both are measured on the basis of full cost. Questions are often raised about the measure of capital investment. The present budget provides policymakers the necessary information regarding investment spending. It records investment on a cash basis, and it requires the Congress to provide budget authority before an agency can obligate the Government to make a cash outlay. By these means, it causes the total cost of capital investment to be compared up front in a rough and ready way with the total expected future net benefits. Since the budget measures only cost, the benefits with which these costs are compared, based on policy makers’ judgment, must be presented in supplementary materials. Such a comparison of total costs with benefits is consistent with the formal method of cost-benefit analysis of capital projects in government, in which the full cost of a capital asset as the cash is paid out is compared with the full stream of future benefits (all in terms of present values). (Chapter 21 of this volume, “Federal Investment,” provides more information on capital investment.)

RECEIPTS, OFFSETTING COLLECTIONS, AND OFFSETTING RECEIPTS

In General

The budget records amounts collected by Government agencies two different ways. Depending on the nature of the activity generating the collection and the law that established the collection, they are recorded as either:

- ***Governmental receipts***, which are compared in total to outlays (net of offsetting collections and offsetting receipts) in calculating the surplus or deficit; or
- ***Offsetting collections*** or ***offsetting receipts***, which are deducted from gross outlays to calculate net outlay figures.

Governmental Receipts

Governmental receipts are collections that result from the Government’s exercise of its sovereign power to tax or otherwise compel payment. Sometimes they are called receipts, Federal receipts, or Federal revenues. They consist mostly of individual and corporation income taxes and social insurance taxes, but also include excise taxes, compulsory user charges, regulatory fees, customs duties, court fines, certain license fees, and deposits of earnings by the Federal Reserve System. Total receipts for the Federal Government include both on-budget and off-budget receipts (see Table 12–1, “Totals for the Budget and the Federal Government,” which appears earlier in this chapter.) Chapter 15 of this volume, “Governmental Receipts,” provides more information on receipts.

Offsetting Collections and Offsetting Receipts

Offsetting collections and offsetting receipts are recorded as offsets to (deductions from) spending, not as additions on the receipt side of the budget. As explained below, they are recorded as offsets to outlays so that the budget totals represent governmental rather than market activity and reflect the Government’s net transactions with the public. They are recorded in one of two ways, based on interpretation of laws and longstanding budget concepts and practice. They are offsetting collections when the collections are authorized by law to be credited to expenditure accounts and are generally available for expenditure without further legislation. Otherwise, they are deposited in receipt accounts and called offsetting receipts.

Offsetting collections and offsetting receipts result from any of the following types of transactions:

- ***Business-like transactions or market-oriented activities with the public***—these include voluntary collections from the public in exchange for goods or services, such as the proceeds from the sale of postage stamps, the fees charged for admittance to recreation areas, and the proceeds from the sale of Government-owned land; and reimbursements for damages, such as recoveries by the Hazardous Substance Superfund. The budget records these amounts as *offsetting collections from non-Federal sources* (for offsetting collections) or as *proprietary receipts* (for offsetting receipts). The amounts are deducted from gross budget authority and outlays, rather than added to governmental receipts. This treatment produces budget totals for budget authority, outlays, and governmental receipts that represent governmental rather than market activity.

- ***Intragovernmental transactions***—collections from other Federal Government accounts. The budget records collections by one Government account from another as *offsetting collections from Federal sources* (for offsetting collections) or as *intragovernmental receipts* (for offsetting receipts). For example, the General Services Administration rents office space to other Government agencies and records their rental payments as offsetting collections from Federal sources in the Federal Buildings Fund. These transactions are exactly offsetting and do not affect the surplus or deficit. However, they are an important accounting mechanism for allocating costs to the programs and activities that cause the Government to incur the costs. Intragovernmental offsetting collections and receipts are deducted from gross budget authority and outlays so that the budget totals measure the transactions of the Government with the public.

- ***Voluntary gifts and donations***—gifts and donations of money to the Government, which are treated as offsets to budget authority and outlays.

- ***Offsetting governmental transactions***—collections from the public that are governmental in nature (e.g., tax receipts, regulatory fees, compulsory user charges, custom duties, license fees) but required by law to be misclassified as offsetting. The budget records amounts from non-Federal sources that are governmental in nature as *offsetting governmental collections* (for offsetting collections) or as *offsetting governmental receipts* (for offsetting receipts).

Offsetting Collections

Some laws authorize agencies to credit collections directly to the account from which they will be spent and, usually, to spend the collections for the purpose of the account without further action by the Congress. Most revolving funds operate with such authority. For example, a permanent law authorizes the Postal Service to use collections from the sale of stamps to finance its operations without a requirement for annual appropriations. The budget records these collections in the Postal Service Fund (a revolving fund) and records budget authority in an amount equal to the collections. In addition to revolving funds, some agencies are authorized to charge fees to defray a portion of costs for a program that are otherwise financed by appropriations from the general fund and usually to spend the collections without further action by the Congress. In such cases, the budget records the offsetting collections and resulting budget authority in the program's general fund expenditure account. Similarly, intragovernmental collections authorized by some laws may be recorded as offsetting collections and budget authority in revolving funds or in general fund expenditure accounts.

Sometimes appropriations acts or provisions in other laws limit the obligations that can be financed by offsetting collections. In those cases, the budget records budget authority in the amount available to incur obligations, not in the amount of the collections.

Offsetting collections credited to expenditure accounts automatically offset the outlays at the expenditure account level. Where accounts have offsetting collections, the budget shows the budget authority and outlays of the account both gross (before deducting offsetting collections) and net (after deducting offsetting collections). Totals for the agency, subfunction, and overall budget are net of offsetting collections.

Offsetting Receipts

Collections that are offset against gross outlays but are not authorized to be credited to expenditure accounts are credited to receipt accounts and are called offsetting receipts. Offsetting receipts are deducted from budget authority and outlays in arriving at total budget authority and outlays. However, unlike offsetting collections credited to expenditure accounts, offsetting receipts do not offset budget authority and outlays at the account level. In most cases, they offset budget authority and outlays at the agency and subfunction levels.

Proprietary receipts from a few sources, however, are not offset against any specific agency or function and are classified as undistributed offsetting receipts. They are deducted from the Government-wide totals for budget authority and outlays. For example, the collections of rents and royalties from outer continental shelf lands are undistributed because the amounts are large and for the most part are not related to the spending of the agency that administers the transactions and the subfunction that records the administrative expenses.

Similarly, two kinds of intragovernmental transactions—agencies' payments as employers into Federal employee retirement trust funds and interest received by trust funds—are classified as undistributed offsetting receipts. They appear instead as special deductions in computing total budget authority and outlays for the Government rather than as offsets at the agency level. This special treatment is necessary because the amounts

are so large they would distort measures of the agency's activities if they were attributed to the agency.

User Charges

User charges are fees assessed on individuals or organizations for the provision of Government services and for the sale or use of Government goods or resources. The payers of the user charge must be limited in the authorizing legislation to those receiving special benefits from, or subject to regulation by, the program or activity beyond the benefits received by the general public or broad segments of the public (such as those who pay income taxes or customs duties). Policy regarding user charges is established in OMB Circular A–25, "User Charges" (July 8, 1993). The term encompasses proceeds from the sale or use of Government goods and services, including the sale of natural resources (such as timber, oil, and minerals) and proceeds from asset sales (such as property, plant, and equipment). User charges are not necessarily dedicated to the activity they finance and may be credited to the general fund of the Treasury.

The term "user charge" does not refer to a separate budget category for collections. User charges are classified in the budget as receipts, offsetting receipts, or offsetting collections according to the principles explained previously.

See Chapter 16, "Offsetting Collections and Offsetting Receipts," for more information on the classification of user charges.

BUDGET AUTHORITY, OBLIGATIONS, AND OUTLAYS

Budget authority, obligations, and outlays are the primary benchmarks and measures of the budget control system. The Congress enacts laws that provide agencies with spending authority in the form of budget authority. Before agencies can use these resources—obligate this budget authority—OMB must approve their spending plans. After the plans are approved, agencies can enter into binding agreements to purchase items or services or to make grants or other payments. These agreements are recorded as obligations of the United States and deducted from the amount of budgetary resources available to the agency. When payments are made, the obligations are liquidated and outlays recorded. These concepts are discussed more fully below.

Budget Authority and Other Budgetary Resources

Budget authority is the authority provided in law to enter into legal obligations that will result in immediate or future outlays of the Government. In other words, it is the amount of money that agencies are allowed to commit to be spent in current or future years. Government officials may obligate the Government to make outlays only to the extent they have been granted budget authority.

The budget records new budget authority as a dollar amount in the year when it first becomes available for obligation. When permitted by law, unobligated balances of budget authority may be carried over and used in the next year. The budget does not record these balances as budget authority again. They do, however, constitute a budgetary resource that is available for obligation. In some cases, a provision of law (such as a limitation on obligations or a benefit formula) precludes the obligation of funds that would otherwise be available for obligation. In such cases, the budget records budget authority equal to the amount of obligations that can be incurred. A major exception to this rule is for the highway and mass transit programs financed by the Highway Trust Fund, where budget authority is measured as the amount of contract authority (described later in this chapter) provided in authorizing statutes, even though the obligation limitations enacted in annual appropriations acts restrict the amount of contract authority that can be obligated.

In deciding the amount of budget authority to request for a program, project, or activity, agency officials estimate the total amount of obligations they will need to incur to achieve desired goals and subtract the unobligated balances available for these purposes. The amount of budget authority requested is influenced by the nature of the programs, projects, or activities being financed. For current operating expenditures, the amount requested usually covers the needs for the fiscal year. For major procurement programs and construction projects, agencies generally must request sufficient budget authority in the first year to fully fund an economically useful segment of a procurement or project, even though it may be obligated over several years. This full funding policy is intended to ensure that the decision-makers take into account all costs and benefits fully at the time decisions are made to provide resources. It also avoids sinking money into a procurement or project without being certain if or when future funding will be available to complete the procurement or project.

Budget authority takes several forms:

- ***Appropriations***, provided in annual appropriations acts or authorizing laws, permit agencies to incur obligations and make payment;
- ***Borrowing authority***, usually provided in permanent laws, permits agencies to incur obligations but requires them to borrow funds, usually from the general fund of the Treasury, to make payment;
- ***Contract authority***, usually provided in permanent law, permits agencies to incur obligations in advance of a separate appropriation of the cash for payment or in anticipation of the collection of receipts that can be used for payment; and
- ***Spending authority from offsetting collections***, usually provided in permanent law, permits agencies to credit offsetting collections to an expenditure account, incur obligations, and make payment using the offsetting collections.

Because offsetting collections and offsetting receipts are deducted from gross budget authority, they are referred to as negative budget authority for some purposes, such as Congressional Budget Act provisions that pertain to budget authority.

Authorizing statutes usually determine the form of budget authority for a program. The authorizing statute may authorize a particular type of budget authority to be provided in annual appropriations acts, or it may provide one of the forms of budget authority directly, without the need for further appropriations.

An appropriation may make funds available from the general fund, special funds, or trust funds, or authorize the spending of offsetting collections credited to expenditure accounts, including revolving funds. Borrowing authority is usually authorized for business-like activities where the activity being financed is expected to produce income over time with which to repay the borrowing with interest. The use of contract authority is traditionally limited to transportation programs.

New budget authority for most Federal programs is normally provided in annual appropriations acts. However, new budget authority for more than half of all outlays is made available through permanent appropriations under existing laws and does not require current action by the Congress. Much of the permanent budget authority is for trust funds, interest on the public debt, and the authority to spend offsetting collections credited to appropriation or fund accounts. For most trust funds, the budget authority is appropriated automatically under existing law from the available balance of the fund and equals the estimated annual obligations of the funds. For interest on the public debt, budget authority is provided automatically under a permanent appropriation enacted in 1847 and equals interest outlays.

Annual appropriations acts generally make budget authority available for obligation only during the fiscal year to which the act applies. However, they frequently allow budget authority for a particular purpose to remain available for obligation for a longer period or indefinitely (that is, until expended or until the program objectives have been attained). Typically, budget authority for current operations is made available for only one year, and budget authority for construction and some research projects is available for a specified number of years or indefinitely. Most budget authority provided in authorizing statutes, such as for most trust funds, is available indefinitely. If budget authority is initially provided for a limited period of availability, an extension of availability would require enactment of another law (see “Reappropriation” later in this chapter).

Budget authority that is available for more than one year and not obligated in the year it becomes available is carried forward for obligation in a following year. In some cases, an account may carry forward unobligated budget authority from more than one prior year. The sum of such amounts constitutes the account’s ***unobligated balance***. Most of these balances had been provided for specific uses such as the multi-year construction of a major project and so are not available for new programs. A small part may never be obligated or spent, primarily amounts provided for contingencies that do not occur or reserves that never have to be used.

Amounts of budget authority that have been obligated but not yet paid constitute the account’s ***unpaid obligations***. For example, in the case of salaries and wages, one to three weeks elapse between the time of obligation and the time of payment. In the case of major procurement and construction, payments may occur over a period of several years after the obligation is made. Unpaid obligations (which are made up of accounts payable and undelivered orders) net of the accounts receivable and unfilled customers’ orders are defined by law as the ***obligated balances***. Obligated balances of budget authority at the end of the year are carried forward until the obligations are paid or the balances are canceled. (A general law provides that the obligated balances of budget authority that was made available for a definite period is automatically cancelled five years after the end of the period.) Due to such flows, a change in the amount of budget authority available in any one year may change the level of obligations and outlays for several years to come. Conversely, a change in the amount of obligations incurred from one year to the next does not necessarily result from an equal change in the amount of budget authority available for that year and will not necessarily result in an equal change in the level of outlays in that year.

The Congress usually makes budget authority available on the first day of the fiscal year for which the appropriations act is passed. Occasionally, the appropriations language specifies a different timing. The language may provide an ***advance appropriation***—budget authority that does not become available until one year or more beyond the fiscal year for which the appropriations act is passed. ***Forward funding*** is budget authority that is made available for obligation beginning in the last quarter of the fiscal year (beginning on July 1) for the financing of ongoing grant programs during the next fiscal year. This kind of funding is used mostly for education programs, so that obligations for education grants can be made prior to the beginning of the next school year. For certain benefit programs funded by annual appropriations, the appropriation provides for ***advance funding***—budget authority that is to be charged to the appropriation in the succeeding year, but which authorizes obligations to be incurred in the last quarter of the current fiscal year if necessary to meet benefit payments in excess of the specific amount appropriated for the year. When such authority is used, an adjustment is made to increase the budget authority for the fiscal year in which it is used and to reduce the budget authority of the succeeding fiscal year.

Provisions of law that extend into a new fiscal year the availability of unobligated amounts that have expired or would otherwise expire are called reappropriations. Reappropriations of expired balances that are newly available for obligation in the current or budget year count as new budget authority in the fiscal year in which the balances become newly available. For example, if a 2011 appropriations act extends the availability of unobligated budget authority that expired at the end of

2010, new budget authority would be recorded for 2011. This scorekeeping is used because a reappropriation has exactly the same effect as allowing the earlier appropriation to expire at the end of 2010 and enacting a new appropriation for 2011.

For purposes of the Congressional Budget Act and the Statutory Pay-As-You-Go Act of 2010 (discussed earlier under "Budget Enforcement"), the budget classifies budget authority as ***discretionary*** or ***mandatory***. This classification indicates whether an appropriations act or authorizing legislation controls the amount of budget authority that is available. Generally, budget authority is discretionary if provided in an annual appropriations act and mandatory if provided in authorizing legislation. However, the budget authority provided in annual appropriations acts for certain specifically identified programs is also classified as mandatory. This is because the authorizing legislation for these programs entitles beneficiaries—persons, households, or other levels of government—to receive payment, or otherwise legally obligates the Government to make payment and thereby effectively determines the amount of budget authority required, even though the payments are funded by a subsequent appropriation.

Sometimes, budget authority is characterized as current or permanent. Current authority requires the Congress to act on the request for new budget authority for the year involved. Permanent authority becomes available pursuant to standing provisions of law without appropriations action by the Congress for the year involved. Generally, budget authority is current if an annual appropriations act provides it and permanent if authorizing legislation provides it. By and large, the current/permanent distinction has been replaced by the discretionary/mandatory distinction, which is similar but not identical. Outlays are also classified as discretionary or mandatory according to the classification of the budget authority from which they flow (see "Outlays" later in this chapter).

The amount of budget authority recorded in the budget depends on whether the law provides a specific amount or employs a variable factor that determines the amount. It is considered ***definite*** if the law specifies a dollar amount (which may be stated as an upper limit, for example, "shall not exceed …"). It is considered ***indefinite*** if, instead of specifying an amount, the law permits the amount to be determined by subsequent circumstances. For example, indefinite budget authority is provided for interest on the public debt, payment of claims and judgments awarded by the courts against the United States, and many entitlement programs. Many of the laws that authorize collections to be credited to revolving, special, and trust funds make all of the collections available for expenditure for the authorized purposes of the fund, and such authority is considered to be indefinite budget authority because the amount of collections is not known in advance of their collection.

Obligations

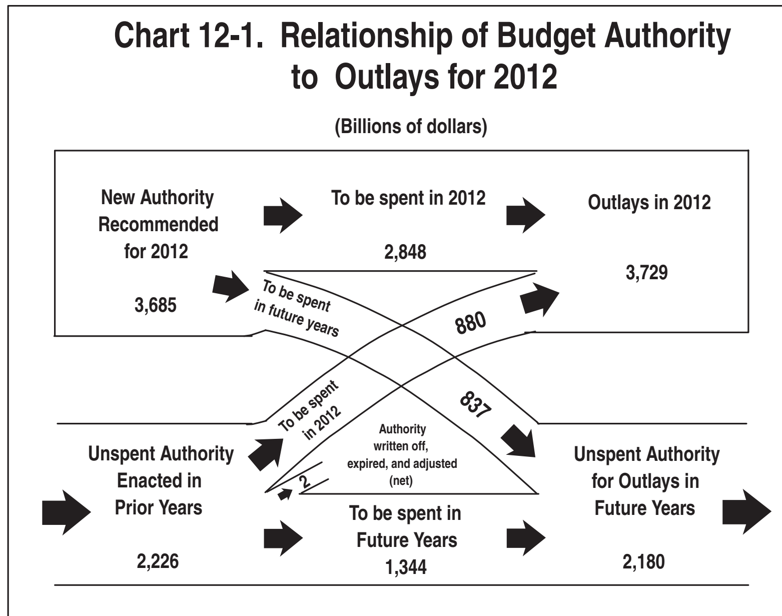
Following the enactment of budget authority and the completion of required apportionment action, Government agencies incur obligations to make payments (see earlier discussion under "Budget Execution"). Agencies must record obligations when they enter into binding agreements that will result in immediate or future outlays. Such obligations include the current liabilities for salaries, wages, and interest; and contracts for the purchase of supplies and equipment, construction, and the acquisition of office space, buildings, and land. For Federal credit programs, obligations are recorded in an amount equal to the estimated subsidy cost of direct loans and loan guarantees (see "Federal Credit" later in this chapter).

Outlays

Outlays are the measure of Government spending. They are payments that liquidate obligations (other than most exchanges of financial instruments, of which the repayment of debt is the prime example). The budget records outlays when obligations are paid, in the amount that is paid.

Agency, function and subfunction, and Government-wide outlay totals are stated net of offsetting collections and offsetting receipts for most budget presentations. (Offsetting receipts from a few sources do not offset any specific function, subfunction, or agency, as explained previously, but only offset Government-wide totals.) Outlay totals for accounts with offsetting collections are stated both gross and net of the offsetting collections credited to the account. However, the outlay totals for special and trust funds with offsetting receipts are not stated net of the offsetting receipts; like other offsetting receipts, these offset the agency, function, and subfunction totals but do not offset account-level outlays.

The Government usually makes outlays in the form of cash (currency, checks, or electronic fund transfers). However, in some cases agencies pay obligations without disbursing cash, and the budget nevertheless records outlays for the equivalent method. For example, the budget records outlays for the full amount of Federal employees' salaries, even though the cash disbursed to employees is net of Federal and State income taxes withheld, retirement contributions, life and health insurance premiums, and other deductions. (The budget also records receipts for the amounts withheld from Federal employee paychecks for Federal income taxes and other payments to the Government.) When debt instruments (bonds, debentures, notes, or monetary credits) are used in place of cash to pay obligations, the budget records outlays financed by an increase in agency debt. For example, the budget records the acquisition of physical assets through certain types of lease-purchase arrangements as though a cash disbursement were made for an outright purchase. The transaction creates a Government debt, and the cash lease payments are treated as repayments of principal and interest.



The budget records outlays for the interest on the public issues of Treasury debt securities as the interest accrues, not when the cash is paid. A small portion of Treasury debt consists of inflation-indexed securities, which feature monthly adjustments to principal for inflation and semiannual payments of interest on the inflation-adjusted principal. As with fixed-rate securities, the budget records interest outlays as the interest accrues. The monthly adjustment to principal is recorded, simultaneously, as an increase in debt outstanding and an outlay of interest.

Most Treasury debt securities held by trust funds and other Government accounts are in the Government account series. The budget normally states the interest on these securities on a cash basis. When a Government account is invested in Federal debt securities, the purchase price is usually close or identical to the par (face) value of the security. The budget generally records the investment at par value and adjusts the interest paid by Treasury and collected by the account by the difference between purchase price and par, if any.

For Federal credit programs, outlays are equal to the subsidy cost of direct loans and loan guarantees and are recorded as the underlying loans are disbursed (see “Federal Credit” later in this chapter).

The budget records refunds of receipts that result from overpayments by the public (such as income taxes withheld in excess of tax liabilities) as reductions of receipts, rather than as outlays. However, the budget records payments to taxpayers for refundable tax credits (such as earned income tax credits) that exceed the taxpayer’s tax liability as outlays. Similarly, when the Government makes overpayments that are later returned to the Government, those refunds to the Government are recorded as offsetting collections or offsetting receipts, not as governmental receipts.

Not all of the new budget authority for 2012 will be obligated or spent in 2012. Outlays during a fiscal year may liquidate obligations incurred in the same year or in prior years. Obligations, in turn, may be incurred against budget authority provided in the same year or against unobligated balances of budget authority provided in prior years. Outlays, therefore, flow in part from budget authority provided for the year in which the money is spent and in part from budget authority provided for prior years. The ratio of a given year’s outlays resulting from budget authority enacted in that or a prior year to the original amount of that budget authority is referred to as the spendout rate for that year.

As shown in the accompanying chart, $2,848 billion of outlays in 2012 (76 percent of the outlay total) will be made from that year’s $3,685 billion total of proposed new budget authority (a first-year spendout rate of 77 percent). Thus, the remaining $880 billion of outlays in 2012 (24 percent of the outlay total) will be made from budget authority enacted in previous years. At the same time, $837 billion of the new budget authority proposed for 2012 (23 percent of the total amount proposed) will not lead to outlays until future years.

As described earlier, the budget classifies budget authority and outlays as discretionary or mandatory. This classification of outlays measures the extent to which actual spending is controlled through the annual appropriations process. Almost 38 percent of total outlays in 2010 ($1,306 billion) are discretionary and the remaining 62 percent ($2,150 billion in 2010) are mandatory spending and net interest. Such a large portion of total spending is mandatory because authorizing rather than appropriations legislation determines net interest ($196 billion in 2010) and the spending for a few programs with large amounts of spending each year, such as Social Security ($701 billion in 2010) and Medicare ($446 billion in 2010).

The bulk of mandatory outlays flow from budget authority recorded in the same fiscal year. This is not necessarily the case for discretionary budget authority and outlays. For most major construction and procurement projects and long-term contracts, for example, the budget

authority covers the entire cost estimated when the projects are initiated even though the work will take place and outlays will be made over a period extending beyond the year for which the budget authority is enacted. Similarly, discretionary budget authority for most education and job training activities is appropriated for school or program years that begin in the fourth quarter of the fiscal year. Most of these funds result in outlays in the year after the appropriation.

FEDERAL CREDIT

Some Government programs make direct loans or loan guarantees. A ***direct loan*** is a disbursement of funds by the Government to a non-Federal borrower under a contract that requires repayment of such funds with or without interest. The term includes equivalent transactions such as selling a property on credit terms in lieu of receiving cash up front. A ***loan guarantee*** is any guarantee, insurance, or other pledge with respect to the payment of all or a part of the principal or interest on any debt obligation of a non-Federal borrower to a non-Federal lender. The Federal Credit Reform Act of 1990, as amended (FCRA) prescribes the budget treatment for Federal credit programs. Under this treatment, the budget records obligations and outlays up front, for the net cost to the Government (subsidy cost), rather than recording the cash flows year by year over the term of the loan. Under FCRA treatment, the costs and benefits of direct loans and loan guarantees can be compared to each other and to other methods of delivering benefits, such as grants, on an equivalent basis.

The cost of direct loans and loan guarantees, sometimes called the "subsidy cost," is estimated as the present value of expected disbursements over the term of the loan less the present value of expected collections, using appropriate Treasury interest rates to discount the cash flows.[2] Similar to most other kinds of programs, agencies can make loans or guarantee loans only if the Congress has appropriated funds sufficient to cover the subsidy costs, or provided a limitation on the amount of direct loans or loan guarantees that can be made in annual appropriations acts.

The budget records the estimated long-term cost to the Government arising from direct loans and loan guarantees—the budget authority and outlays—in ***credit program accounts***. When a Federal agency disburses a direct loan or when a non-Federal lender disburses a loan guaranteed by a Federal agency, the program account disburses or outlays an amount equal to the estimated present- value cost, or subsidy, to a non-budgetary credit ***financing account***. The financing accounts record the actual transactions with the public. For a few programs, the estimated cost is negative, because the present value of expected Government collections exceeds the present value of expected payments to the public over the term of the loan. In such cases, the financing account makes a payment to the program's negative subsidy receipt account, where it is recorded as an offsetting receipt. In a few cases, the offsetting receipts of credit accounts are dedicated to a special fund established for the program and are available for appropriation for the program.

The agencies responsible for credit programs must reestimate the cost of the outstanding portfolio of direct loans and loan guarantees each year. If the estimated cost increases, the program account makes an additional payment to the financing account. If the estimated cost decreases, the financing account makes a payment to the program's downward reestimate receipt account, where it is recorded as an offsetting receipt. The FCRA provides permanent indefinite appropriations to pay for upward reestimates.

If the Government modifies the terms of an outstanding direct loan or loan guarantee in a way that increases the cost as the result of a law or the exercise of administrative discretion under existing law, the program account records obligations for an additional amount equal to the increased cost and outlays the amount to the financing account. As with the original cost, agencies may incur modification costs only if the Congress has appropriated funds to cover them. A modification may also reduce costs, in which case the amounts are generally returned to the general fund when the financing account makes a payment to the program's receipt account.

Credit financing accounts record all cash flows arising from direct loan obligations and loan guarantee commitments. Such cashflows include all cashflows to and from the public, including direct loan disbursements and repayments, loan guarantee default payments, fees, and recoveries on defaults. Financing accounts also record intragovernmental transactions, such as the receipt of subsidy cost payments from program accounts, borrowing and repayments of Treasury debt to finance program activities, and interest paid to or received from the Treasury. The cash flows of direct loans and of loan guarantees are recorded in separate financing accounts for programs that provide both types of credit. The budget totals exclude the transactions of the financing accounts because they are not a cost to the Government. However, since financing accounts record all credit cash flows to and from the public, they affect the means of financing a budget surplus or deficit (see "Credit Financing Accounts" in the next section). The budget documents display the transactions of the financing accounts, together with the related program accounts, for information and analytical purposes.

The FCRA grandfathered the budgetary treatment of direct loan obligations and loan guarantee commitments made prior to 1992. The budget records these on a cash basis in ***credit liquidating accounts***, the same as they were recorded before FCRA was enacted. However, this exception ceases to apply if the direct loans or loan guarantees are modified as described above. In that case, the budget records the subsidy cost or savings of the modifi-

[2] Present value is a standard financial concept that allows for the time-value of money. That is, it accounts for the fact that a given sum of money is worth more today than the same sum would be worth in the future because interest can be earned on money held today.

cation, as appropriate, and begins to account for the associated transactions as the FCRA prescribes for direct loan obligations and loan guarantee commitments made in 1992 or later.

Under the authority provided in various acts, certain activities are reflected pursuant to FCRA. For example, the Emergency Economic Stabilization Act of 2008 (EESA) created the Troubled Asset Relief Program (TARP) under the Department of the Treasury, and authorized Treasury to purchase or guarantee troubled assets until October 3, 2010. Under the TARP, Treasury has purchased equity interests in financial institutions. Section 123 of the EESA provides the Administration the authority to treat these equity investments on a FCRA-basis, recording outlays for the subsidy as is done for direct loans and loan guarantees. The budget reflects the cost to the Government of TARP direct loans, loan guarantees, and equity investments consistent with the FCRA and Section 123 of EESA, which requires adjustments to the discount rate otherwise prescribed by FCRA to account for market risk for transactions recorded on a present-value basis. Increases to the International Monetary Fund Quota and New Arrangement to Borrow enacted in the 2009 Supplemental Appropriations Act are treated on a FCRA basis with a risk adjustment to the discount rate, under the authority provided in that Act. In addition, Treasury equity purchases under the Small Business Lending Fund (SBLF) are treated pursuant to the FCRA, as provided by the Small Business Jobs Act of 2010.

BUDGET DEFICIT OR SURPLUS AND MEANS OF FINANCING

When outlays exceed receipts, the difference is a deficit, which the Government finances primarily by borrowing. When receipts exceed outlays, the difference is a surplus, and the Government automatically uses the surplus primarily to reduce debt. The Government's debt (debt held by the public) is approximately the cumulative amount of borrowing to finance deficits, less repayments from surpluses, over the Nation's history.

Borrowing is not exactly equal to the deficit, and debt repayment is not exactly equal to the surplus, because of the other means of financing such as those discussed in this section. The factors included in the other means of financing can either increase or decrease the Government's borrowing needs (or decrease or increase its ability to repay debt). For example, the change in the Treasury operating cash balance is a factor included in other means of financing. Holding receipts and outlays constant, increases in the cash balance increase the Government's need to borrow or reduce the Government's ability to repay debt, and decreases in the cash balance decrease the need to borrow or increase the ability to repay debt. In some years, the net effect of the other means of financing is minor relative to the borrowing or debt repayment; in other years, such as 2009, the net effect may be significant, as explained later in this chapter.

Borrowing and Debt Repayment

The budget treats borrowing and debt repayment as a means of financing, not as receipts and outlays. If borrowing were defined as receipts and debt repayment as outlays, the budget would always be virtually balanced by definition. This rule applies both to borrowing in the form of Treasury securities and to specialized borrowing in the form of agency securities. The rule reflects the commonsense understanding that lending or borrowing is just an exchange of financial assets of equal value—cash for Treasury securities—and so is fundamentally different from, say, paying taxes.

In 2010, the Government borrowed $1,474 billion from the public, bringing debt held by the public to $9,019 billion. This borrowing financed the $1,293 billion deficit in that year as well as the net effect of the other means of financing, such as changes in cash balances and other accounts discussed below.

In addition to selling debt to the public, the Treasury Department issues debt to Government accounts, primarily trust funds that are required by law to invest in Treasury securities. Issuing and redeeming this debt does not affect the means of financing, because these transactions occur between one Government account and another and thus do not raise or use any cash for the Government as a whole.

(See Chapter 6 of this volume, "Federal Borrowing and Debt," for a fuller discussion of this topic.)

Exercise of Monetary Power

Seigniorage is the profit from coining money. It is the difference between the value of coins as money and their cost of production. Seigniorage reduces the Government's need to borrow. Unlike the payment of taxes or other receipts, it does not involve a transfer of financial assets from the public. Instead, it arises from the exercise of the Government's power to create money and the public's desire to hold financial assets in the form of coins. Therefore, the budget excludes seigniorage from receipts and treats it as a means of financing other than borrowing from the public. The budget also treats proceeds from the sale of gold as a means of financing, since the value of gold is determined by its value as a monetary asset rather than as a commodity.

Credit Financing Accounts

The budget records the net cash flows of credit programs in credit financing accounts. These accounts include the transactions for direct loan and loan guarantee programs, as well as the equity purchase programs under TARP that are recorded on a credit basis consistent with Section 123 of EESA. Financing accounts also record the 2009 increase in the U.S. quota in the International Monetary Fund that are recorded on a credit basis consistent with the Supplemental Appropriations Act, 2009, and equity purchases under the Small Business Lending Fund (SBLF) consistent with the Small Business Jobs

Act of 2010. Credit financing accounts are excluded from the budget because they are not allocations of resources by the Government (see "Federal Credit" earlier in this chapter). However, even though they do not affect the surplus or deficit, they can either increase or decrease the Government's need to borrow. Therefore, they are recorded as a means of financing.

Financing account disbursements to the public increase the requirement for Treasury borrowing in the same way as an increase in budget outlays. Financing account receipts from the public can be used to finance the payment of the Government's obligations and therefore reduce the requirement for Treasury borrowing from the public in the same way as an increase in budget receipts.

Deposit Fund Account Balances

The Treasury uses non-budgetary accounts, called deposit funds, to record cash held temporarily until ownership is determined (for example, earnest money paid by bidders for mineral leases) or cash held by the Government as agent for others (for example, State and local income taxes withheld from Federal employees' salaries and not yet paid to the State or local government or the Thrift Savings Fund, a defined contribution pension fund held and managed in a fiduciary capacity by the Government). Deposit fund balances may be held in the form of either invested or uninvested balances. To the extent that they are not invested, changes in the balances are available to finance expenditures and are recorded as a means of financing other than borrowing from the public. To the extent that they are invested in Federal debt, changes in the balances are reflected as borrowing from the public (in lieu of borrowing from other parts of the public) and are not reflected as a separate means of financing.

United States Quota Subscriptions to the International Monetary Fund (IMF)

The United States participates in the IMF through a quota subscription. Financial transactions with the IMF are exchanges of monetary assets. When the IMF draws dollars from the U.S. quota, the United States simultaneously receives an equal, offsetting, Special Drawing Right (SDR)-denominated claim in the form of an increase in the U.S. reserve position in the IMF. The U.S. reserve position in the IMF increases when the United States transfers dollars to the IMF and decreases when the United States is repaid and the cash flows return to the Treasury.

The budgetary treatment of appropriations for IMF quotas has changed over time. Prior to 1981, the transactions were not included in the budget because they were viewed as exchanges of cash for a monetary asset (SDRs) of the same value. This was consistent with the scoring of other exchanges of monetary assets, such as deposits of cash in Treasury accounts at commercial banks. As a result of an agreement reached with the Congress in 1980, the budget began to record budget authority for the quotas, but did not record outlays because of the continuing view that the transactions were exchanges of monetary assets of equal value. This scoring convention continued to be applied through 2008. The 2010 Budget proposed to change the scoring back to the pre-1981 practice of showing zero budget authority and outlays for proposed increases in the U.S. quota subscriptions to the IMF.

In 2009, Congress enacted an increase in the Supplemental Appropriations Act of 2009 (Public Law 111–2, Title XIV, International Monetary Programs) and directed that the increase be scored as credit under the Federal Credit Reform Act of 1990, with an adjustment to the discount rate for market risk. The 2012 Budget reflects obligations and outlays for the quota increase provided by the Supplemental Appropriations Act of 2009 under the terms of that Act. The cash transactions between the U.S. Treasury and the IMF are treated as a means of financing (see "Credit Financing Accounts" earlier in this chapter), which do not affect the deficit.

In contrast, for increases to the U.S. quota subscriptions made prior to the 2009 Supplemental Appropriations Act, the 2012 Budget records interest received from the IMF on U.S. deposits as an offsetting receipt in the general fund of the Treasury. Treasury records outlays in the prior year for financial transactions with the IMF to the extent there is an unrealized loss in dollar terms and offsetting receipts to the extent there is an unrealized gain in dollar terms on the value of the interest-bearing portion of the U.S. quota actually held at the IMF in SDRs. Changes in the value of the portion of the U.S. quota held at Treasury rather than in the U.S. reserve position held at the IMF are recorded as a change in obligations.

Investments of the National Railroad Retirement Investment Trust

Under longstanding rules, the budget has generally treated investments in non-Federal equities and debt securities as a purchase of an asset, recording an obligation and an outlay in an amount equal to the purchase price in the year of the purchase. Since investments in non-Federal equities or debt securities consume cash, fund balances (of funds available for obligation) are normally reduced by the amounts paid for these purchases. However, as previously noted, the purchase of equity securities through TARP is recorded on a credit basis, with an outlay recorded in the amount of the estimated subsidy cost. In addition, the Railroad Retirement and Survivors' Improvement Act of 2001 (Public Law 107–90) requires purchases or sales of non-Federal assets by the National Railroad Retirement Investment Trust to be treated as a means of financing in the budget, rather than as an outlay.

Earnings on investments by the National Railroad Retirement Investment Trust (NRRIT) in private assets pose special challenges for budget projections. Over long periods, equities and private bonds are expected to earn a higher return on average than the Treasury rate, but that return is subject to greater uncertainty. Sound budgeting principles require that estimates of future trust fund balances reflect both the average return on investments, and the cost of risk associated with the uncertainty of that

return. (The latter is particularly true in cases where individual beneficiaries have not made a voluntary choice to assume additional risk.) Estimating both of these separately is quite difficult. While the gains and losses that these assets have experienced in the past are known, it is quite possible that such premiums will differ in the future. Furthermore, there is no existing procedure for the budget to record separately the cost of risk from such an investment, even if it could be estimated accurately. Economic theory suggests, however, that the difference between the expected return of a risky liquid asset and the Treasury rate is equal to the cost of the asset's additional risk as priced by the market net of administrative and transaction costs. Following through on this insight, the best way to project the rate of return on the Fund's balances is probably to use a Treasury rate. As a result, the Budget treats equivalently NRRIT investments with equal economic value as measured by market prices, avoiding the appearance that the budget would be expected to benefit if the Government bought private sector assets.

The actual and estimated returns to private (debt and equity) securities are recorded in subfunction 909, other investment income. The actual-year returns include interest, dividends, and capital gains and losses on private equities and other securities. The Fund's portfolio of these assets is revalued at market prices at the end of each month to determine capital gains or losses. As a result, the Fund's balance at any given point reflects the current market value of resources available to the Government to finance benefits. Earnings for the remainder of the current year and for future years are estimated using the 10-year Treasury rate and the value of the Fund's portfolio at the end of the actual year. No estimates are made of gains and losses for the remainder of the current year or for subsequent years.

FEDERAL EMPLOYMENT

The budget includes information on civilian and military employment. It also includes information on related personnel compensation and benefits and on staffing requirements at overseas missions. Chapter 11 of this volume, "Improving the Federal Workforce," provides employment levels measured in full-time equivalents (FTE). Agency FTEs are the measure of total hours worked by an agency's Federal employees divided by the total number of one person's compensable work hours in a fiscal year.

BASIS FOR BUDGET FIGURES

Data for the Past Year

The past year column (2010) generally presents the actual transactions and balances as recorded in agency accounts and as summarized in the central financial reports prepared by the Treasury Department for the most recently completed fiscal year. Occasionally, the budget reports corrections to data reported erroneously to Treasury but not discovered in time to be reflected in Treasury's published data. In addition, in certain cases the Budget has a broader scope and includes financial transactions that are not reported to Treasury (see Chapter 30 of this volume, "Comparison of Actual to Estimated Totals," for a summary of these differences).

Data for the Current Year

The current year column (2011) includes estimates of transactions and balances based on the amounts of budgetary resources that were available when the budget was transmitted. In cases where the budget proposes policy changes effective in the current year, the data will also reflect the budgetary effect of those proposed changes. This year, many programs and activities are operating under a continuing resolution (P.L. 111-242, as amended), which will expire March 4, 2011, so information on the final appropriations amounts is not available. Data for the current year column in the budget *Appendix,* and in tables that show details on discretionary spending amounts in the *Analytical Perspectives* volume, reflect the annualized level provided by the continuing resolution. In the main *Budget* volume, the *Historical Tables* volume, and in tables that include total discretionary spending in the *Analytical Perspectives* volume, current year totals by agency and for the total Government will match the President's 2011 Budget request.

Data for the Budget Year

The budget year column (2012) includes estimates of transactions and balances based on the amounts of budgetary resources that are estimated to be available, including new budget authority requested under current authorizing legislation, and amounts estimated to result from changes in authorizing legislation and tax laws.

The budget *Appendix* generally includes the appropriations language for the amounts proposed to be appropriated under current authorizing legislation. In a few cases, this language is transmitted later because the exact requirements are unknown when the budget is transmitted. The *Appendix* generally does not include appropriations language for the amounts that will be requested under proposed legislation; that language is usually transmitted later, after the legislation is enacted. Some tables in the budget identify the items for later transmittal and the related outlays separately. Estimates of the total requirements for the budget year include both the amounts requested with the transmittal of the budget and the amounts planned for later transmittal.

Data for the Outyears

The budget presents estimates for each of the nine years beyond the budget year (2013 through 2021) in order to reflect the effect of budget decisions on objectives and plans over a longer period.

Allowances

The budget may include lump-sum allowances to cover certain transactions that are expected to increase or decrease budget authority, outlays, or receipts but are not, for various reasons, reflected in the program details. For example, the budget might include an allowance to show the effect on the budget totals of a proposal that would actually affect many accounts by relatively small amounts, in order to avoid unnecessary detail in the presentations for the individual accounts.

This year's Budget, like last year's, includes an allowance for the costs of possible future natural disasters.

Baseline

The budget baseline is an estimate of the receipts, outlays, and deficits or surpluses that would occur if no changes were made to current laws and policies during the period covered by the budget. The baseline assumes that receipts and mandatory spending, which generally are authorized on a permanent basis, will continue in the future as required by current law and policy. The baseline assumes that the future funding for most discretionary programs, which generally are funded annually, will equal the most recently enacted appropriation, adjusted for inflation.

Baseline outlays represent the amount of resources that would be used by the Government over the period covered by the budget on the basis of laws currently enacted.

The baseline serves several useful purposes:

- It may warn of future problems, either for Government fiscal policy as a whole or for individual tax and spending programs.
- It may provide a starting point for formulating the President's Budget.
- It may provide a "policy-neutral" benchmark against which the President's Budget and alternative proposals can be compared to assess the magnitude of proposed changes.

As it happens, a number of significant changes in policies are embedded in current law. For example, the tax cuts enacted in 2001 and 2003 and extended in 2010 are assumed to expire at the end of 2012. Because the expiration of this law would create significant differences between the baseline as specified in the Budget Enforcement Act (BEA) of 1990 and policies in effect this year, the Administration also issues an adjusted baseline that, unlike the BEA baseline, assumes such scheduled changes in current law will not occur. (Chapter 27 of this volume, "Current Services Estimates," provides more information on the baseline, including the differences between the baseline as calculated under the rules of the BEA and the adjusted baseline used in this Budget.)

PRINCIPAL BUDGET LAWS

The following basic laws govern the Federal budget process:

Article 1, section 8, clause 1 of the Constitution, which empowers the Congress to collect taxes.

Article 1, section 9, clause 7 of the Constitution, which requires appropriations in law before money may be spent from the Treasury and the publication of a regular statement of the receipts and expenditures of all public money.

Antideficiency Act (codified in Chapters 13 and 15 of Title 31, United States Code), which prescribes rules and procedures for budget execution.

Chapter 11 of Title 31, United States Code, which prescribes procedures for submission of the President's budget and information to be contained in it.

Congressional Budget and Impoundment Control Act of 1974 (Public Law 93–344), as amended. This Act comprises the:

Congressional Budget Act of 1974, as amended, which prescribes the congressional budget process; and

Impoundment Control Act of 1974, which controls certain aspects of budget execution.

Federal Credit Reform Act of 1990, as amended (2 USC 661–661f), which the Budget Enforcement Act of 1990 included as an amendment to the Congressional Budget Act to prescribe the budget treatment for Federal credit programs.

Government Performance and Results Act of 1993 (Public Law 103–62, as amended) which emphasizes managing for results. It requires agencies to prepare strategic plans, annual performance plans, and annual performance reports.

Statutory-Pay-As-You-Go Act of 2010, which establishes a budget enforcement mechanism generally requiring that direct spending and revenue legislation enacted into law not increase the deficit.

GLOSSARY OF BUDGET TERMS

Account refers to a separate financial reporting unit used by the Federal government to record budget authority, outlays and income for budgeting or management information purposes as well as for accounting purposes. All budget (and off-budget) accounts are classified as being either expenditure or receipt accounts and by fund group. Budget (and off-budget) transactions fall within either of two fund group: (1) Federal funds and (2) trust funds. (Cf. Federal funds group and trust funds group.)

Accrual method of measuring cost means an accounting method that records cost when the liability is incurred. As applied to Federal employee retirement benefits, accrual costs are recorded when the benefits are earned rather than when they are paid at some time in the future. The accrual method is used in part to provide data that assists in agency policymaking, but not used in presenting the overall budget of the United States Government.

Advance appropriation means appropriations of new budget authority that become available one or more fiscal years beyond the fiscal year for which the appropriation act was passed.

Advance funding means appropriations of budget authority provided in an appropriations act to be used, if necessary, to cover obligations incurred late in the fiscal year for benefit payments in excess of the amount specifically appropriated in the act for that year, where the budget authority is charged to the appropriation for the program for the fiscal year following the fiscal year for which the appropriations act is passed.

Agency means a department or other establishment of the Government.

Allowance means a lump-sum included in the budget to represent certain transactions that are expected to increase or decrease budget authority, outlays, or receipts but that are not, for various reasons, reflected in the program details.

Balances of budget authority means the amounts of budget authority provided in previous years that have not been outlayed.

Baseline means a projection of the estimated receipts, outlays, and deficit or surplus that would result from continuing current law or current policies through the period covered by the budget.

Budget means the Budget of the United States Government, which sets forth the President's comprehensive financial plan for allocating resources and indicates the President's priorities for the Federal Government.

Budget authority (BA) means the authority provided by law to incur financial obligations that will result in outlays. (For a description of the several forms of budget authority, see "Budget Authority and Other Budgetary Resources" earlier in this chapter.)

Budget Enforcement Act of 1990 (BEA) refers to legislation that altered the budget process, primarily by replacing the earlier fixed targets for annual deficits with a Pay-As-You-Go requirement for new tax or mandatory spending legislation, and with caps on annual discretionary funding. Most aspects of the BEA expired in 2002 but the Statutory Pay-As-You-Go Act of 2010 reinstates a statutory pay-as-you-go rule for revenues and mandatory spending legislation.

Budget resolution—see concurrent resolution on the budget.

Budget totals mean the totals included in the budget for budget authority, outlays, receipts, and the surplus or deficit. Some presentations in the budget distinguish on-budget totals from off-budget totals. On-budget totals reflect the transactions of all Federal Government entities except those excluded from the budget totals by law. The off-budget totals reflect the transactions of Government entities that are excluded from the on-budget totals by law. Under current law, the off-budget totals include the Social Security trust funds (Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds) and the Postal Service Fund. The budget combines the on- and off-budget totals to derive unified or consolidated totals for Federal activity.

Budgetary resources mean amounts available to incur obligations in a given year. The term comprises new budget authority and unobligated balances of budget authority provided in previous years.

Cap means the legal limits for each fiscal year under the Budget Enforcement Act on the budget authority and outlays provided by discretionary appropriations.

Cash equivalent transaction means a transaction in which the Government makes outlays or receives collections in a form other than cash or the cash does not accurately measure the cost of the transaction. (For examples, see the section on "Outlays" earlier in this chapter.)

Collections mean money collected by the Government that the budget records as a governmental receipt, an offsetting collection, or an offsetting receipt.

Concurrent resolution on the budget refers to the concurrent resolution adopted by the Congress to set budgetary targets for appropriations, mandatory spending legislation, and tax legislation. These concurrent reso-

lutions are required by the Congressional Budget Act of 1974, and are generally adopted annually.

Continuing resolution means an appropriations act that provides for the ongoing operation of the Government in the absence of enacted appropriations.

Cost refers to legislation or administrative actions that increase outlays or decrease receipts. (Cf savings.)

Credit program account means a budget account that receives and obligates appropriations to cover the subsidy cost of a direct loan or loan guarantee and disburses the subsidy cost to a financing account.

Current services estimate—see Baseline.

Debt held by the public means the cumulative amount of money the Federal Government has borrowed from the public and not repaid.

Debt held by the public net of financial assets means the cumulative amount of money the Federal Government has borrowed from the public and not repaid, minus the current value of financial assets such as loan assets, bank deposits, or private-sector securities or equities held by the Government and plus the current value of financial liabilities other than debt.

Debt held by Government accounts means the debt the Treasury Department owes to accounts within the Federal Government. Most of it results from the surpluses of the Social Security and other trust funds, which are required by law to be invested in Federal securities.

Debt limit means the maximum amount of Federal debt that may legally be outstanding at any time. It includes both the debt held by the public and the debt held by Government accounts, but without accounting for offsetting financial assets. When the debt limit is reached, the Government cannot borrow more money until the Congress has enacted a law to increase the limit.

Deficit means the amount by which outlays exceed receipts in a fiscal year. It may refer to the on-budget, off-budget, or unified budget deficit.

Direct loan means a disbursement of funds by the Government to a non-Federal borrower under a contract that requires the repayment of such funds with or without interest. The term includes the purchase of, or participation in, a loan made by another lender. The term also includes the sale of a Government asset on credit terms of more than 90 days duration as well as financing arrangements for other transactions that defer payment for more than 90 days. It also includes loans financed by the Federal Financing Bank (FFB) pursuant to agency loan guarantee authority. The term does not include the acquisition of a federally guaranteed loan in satisfaction of default or other guarantee claims or the price support "loans" of the Commodity Credit Corporation. (Cf. loan guarantee.)

Direct spending—see mandatory spending.

Discretionary spending means budgetary resources (except those provided to fund mandatory spending programs) provided in appropriations acts. (Cf. mandatory spending.)

Emergency requirement means an amount that the Congress has designated as an emergency requirement. Such amounts are not included in the estimated budgetary effects of PAYGO legislation under the requirements of the Statutory Pay-As-You-Go Act of 2010, if they are mandatory or receipts, or to congressional limits on discretionary spending under the terms of most recent budget resolutions, if they are discretionary.

Entitlement refers to a program in which the Federal Government is legally obligated to make payments or provide aid to any person who, or State or local government that, meets the legal criteria for eligibility. Examples include Social Security, Medicare, Medicaid, and Food Stamps.

Federal funds group refers to the moneys collected and spent by the Government through accounts other than those designated as trust funds. Federal funds include general, special, public enterprise, and intragovernmental funds. (Cf. trust funds group.)

Financing account means a non-budgetary account (an account whose transactions are excluded from the budget totals) that records all of the cash flows resulting from post-1991 direct loan obligations or loan guarantee commitments. At least one financing account is associated with each credit program account. For programs that make both direct loans and loan guarantees, there are separate financing accounts for the direct loans and the loan guarantees. (Cf. liquidating account.)

Fiscal year means the Government's accounting period. It begins on October 1st and ends on September 30th, and is designated by the calendar year in which it ends.

Forward funding means appropriations of budget authority that are made for obligation starting in the last quarter of the fiscal year for the financing of ongoing grant programs during the next fiscal year.

General fund means the accounts in which are recorded governmental receipts not earmarked by law for a specific purpose, the proceeds of general borrowing, and the expenditure of these moneys.

Government sponsored enterprises mean private enterprises that were established and sponsored by the Federal Government for public policy purposes. They are not included in the budget totals because they are pri-

vate companies, and their securities are not backed by the full faith and credit of the Federal Government. However, the budget presents statements of financial condition for certain Government sponsored enterprises such as the Federal National Mortgage Association. (Cf. off-budget.)

Intragovernmental fund —see Revolving fund.

Liquidating account means a budget account that records all cash flows to and from the Government resulting from pre-1992 direct loan obligations or loan guarantee commitments. (Cf. financing account.)

Loan guarantee means any guarantee, insurance, or other pledge with respect to the payment of all or a part of the principal or interest on any debt obligation of a non-Federal borrower to a non-Federal lender. The term does not include the insurance of deposits, shares, or other withdrawable accounts in financial institutions. (Cf. direct loan.)

Mandatory spending means spending controlled by laws other than appropriations acts (including spending for entitlement programs) and spending for the food stamp program. Although the Statutory Pay-As-You-Go Act of 2010 uses the term direct spending to mean this, mandatory spending is commonly used instead. (Cf. discretionary spending.)

Means of financing refers to borrowing, the change in cash balances, and certain other transactions involved in financing a deficit. The term is also used to refer to the debt repayment, the change in cash balances, and certain other transactions involved in using a surplus. By definition, the means of financing are not treated as receipts or outlays and so are non-budgetary.

Obligated balance means the cumulative amount of budget authority that has been obligated but not yet outlayed. (Cf. unobligated balance.)

Obligation means a binding agreement that will result in outlays, immediately or in the future. Budgetary resources must be available before obligations can be incurred legally.

Off-budget refers to transactions of the Federal Government that would be treated as budgetary had the Congress not designated them by statute as “off-budget.” Currently, transactions of the Social Security trust fund and the Postal Service fund are the only sets of transactions that are so designated. The term is sometimes used more broadly to refer to the transactions of private enterprises that were established and sponsored by the Government, most especially “Government sponsored enterprises” such as the Federal Home Loan Banks. (Cf. budget totals.)

Offsetting collections mean collections that, by law, are credited directly to expenditure accounts and deducted from gross budget authority and outlays of the expenditure account, rather than added to receipts. Usually, they are authorized to be spent for the purposes of the account without further action by the Congress. They result from business-like transactions with the public, including payments from the public in exchange for goods and services, reimbursements for damages, and gifts or donations of money to the Government and from intragovernmental transactions with other Government accounts. The authority to spend offsetting collections is a form of budget authority. (Cf. receipts and offsetting receipts.)

Offsetting receipts mean collections that are credited to offsetting receipt accounts and deducted from gross budget authority and outlays, rather than added to receipts. They are not authorized to be credited to expenditure accounts. The legislation that authorizes the offsetting receipts may earmark them for a specific purpose and either appropriate them for expenditure for that purpose or require them to be appropriated in annual appropriation acts before they can be spent. Like offsetting collections, they result from business-like transactions or market-oriented activities with the public, including payments from the public in exchange for goods and services, reimbursements for damages, and gifts or donations of money to the Government and from intragovernmental transactions with other Government accounts. (Cf. receipts, undistributed offsetting receipts, and offsetting collections.)

On-budget refers to all budgetary transactions other than those designated by statute as off-budget (Cf. budget totals.)

Outlay means a payment to liquidate an obligation (other than the repayment of debt principal or other disbursements that are “means of financing” transactions). Outlays generally are equal to cash disbursements, but also are recorded for cash-equivalent transactions, such as the issuance of debentures to pay insurance claims, and in a few cases are recorded on an accrual basis such as interest on public issues of the public debt. Outlays are the measure of Government spending.

Outyear estimates mean estimates presented in the budget for the years beyond the budget year of budget authority, outlays, receipts, and other items (such as debt).

Pay-as-you-go (PAYGO) refers to requirements of the Statutory Pay-As-You-Go Act of 2010 that result in a sequestration if the estimated combined result of new legislation affecting direct spending or revenue increases the on-budget deficit relative to the baseline, as of the end of a congressional session.

Public enterprise fund —see Revolving fund.

Reappropriation means a provision of law that extends into a new fiscal year the availability of unobligated amounts that have expired or would otherwise expire.

Receipts mean collections that result from the Government's exercise of its sovereign power to tax or otherwise compel payment. They are compared to outlays in calculating a surplus or deficit. (Cf. offsetting collections and offsetting receipts.)

Revolving fund means a fund that conducts continuing cycles of business-like activity, in which the fund charges for the sale of products or services and uses the proceeds to finance its spending, usually without requirement for annual appropriations. There are two types of revolving funds: Public enterprise funds, which conduct business-like operations mainly with the public, and intragovernmental revolving funds, which conduct business-like operations mainly within and between Government agencies. (Cf. special fund and revolving fund.)

Savings refers to legislation or administrative actions that decrease outlays or increase receipts. (Cf. cost.)

Scorekeeping means measuring the budget effects of legislation, generally in terms of budget authority, receipts, and outlays, for purposes of measuring adherence to the Budget or to budget targets established by the Congress, as through agreement to a Budget Resolution.

Sequestration means the cancellation of budgetary resources. The Statutory Pay-As-You-Go Act of 2010 requires such cancellations if revenue or direct spending legislation is enacted that, in total, increase projected deficits or reduces projected surpluses relative to the baseline. Under the law, selected mandatory programs would be subject to across-the-board cancellations.

Special fund means a Federal fund account for receipts or offsetting receipts earmarked for specific purposes and the expenditure of these receipts. (Cf. revolving fund and trust fund.)

Subsidy means the estimated long-term cost to the Government of a direct loan or loan guarantee, calculated on a net present value basis, excluding administrative costs and any incidental effects on governmental receipts or outlays.

Surplus means the amount by which receipts exceed outlays in a fiscal year. It may refer to the on-budget, off-budget, or unified budget surplus.

Supplemental appropriation means an appropriation enacted subsequent to a regular annual appropriations act, when the need for additional funds is too urgent to be postponed until the next regular annual appropriations act.

Trust fund refers to a type of account, designated by law as a trust fund, for receipts or offsetting receipts dedicated to specific purposes and the expenditure of these receipts. Some revolving funds are designated as trust funds, and these are called trust revolving funds. (Cf. special fund and revolving fund.)

Trust funds group refers to the moneys collected and spent by the Government through trust fund accounts. (Cf. Federal funds group.)

Undistributed offsetting receipts mean offsetting receipts that are deducted from the Government-wide totals for budget authority and outlays instead of being offset against a specific agency and function. (Cf. offsetting receipts.)

Unified budget includes receipts from all sources and outlays for all programs of the Federal Government, including both on- and off-budget programs. It is the most comprehensive measure of the Government's annual finances.

Unobligated balance means the cumulative amount of budget authority within a budget account that is not obligated and that remains available for obligation under law.

User charges are charges assessed for the provision of Government services and for the sale or use of Government goods or resources. The payers of the user charge must be limited in the authorizing legislation to those receiving special benefits from, or subject to regulation by, the program or activity beyond the benefits received by the general public or broad segments of the public (such as those who pay income taxes or custom duties).

13. COVERAGE OF THE BUDGET

The Federal Government's activities have far-reaching impacts, affecting the economy and society of the Nation and the world. One of the primary activities of the Government is to allocate resources in order to provide public goods and achieve public policy objectives. The budget is the Government's financial plan for proposing, deciding, and controlling the allocation of resources. Those financial activities that constitute the direct allocation of resources are included in the budget's measures of receipts and expenditures, and are therefore characterized as "budgetary."

Federal Government activities that do not involve the direct allocation of resources in a measurable way are characterized as "non-budgetary" and classified outside of the budget. For example, the budget does not include funds that are privately owned but held and managed by the Government in a fiduciary capacity, such as the deposit funds owned by Native American Indians. In addition, the budget does not include costs that are borne by the private sector even when those costs result from Federal regulatory activity. Also, although the budget includes the subsidy costs[1] of Federal credit programs, it does not include the cash flows of these programs that do not involve a direct allocation of resources by the Government and that are a means of financing these programs. Non-budgetary activities can be important instruments of Federal policy and are discussed briefly in this chapter and in more detail in other parts of the budget documents.

The term "off-budget" may appear to be synonymous with non-budgetary. However, it has a meaning distinct from non-budgetary and, as discussed below, refers to Federal Government activities that are required by law to be excluded from the budget totals. The term is also used colloquially to refer to emergency funding or supplemental appropriations for war costs because these items have often been passed by the Congress without regard to the normal budget enforcement procedures. Despite the colloquial usage of the term off-budget, emergency aid and war costs are budgetary and specifically "on-budget," as that term is defined below; budgetary outlays and receipts reflect the costs of these provisions.

Budgetary Activities

The Federal Government has used the unified budget concept as the foundation for its budgetary analysis and presentation since the 1969 Budget, implementing a recommendation made by the President's Commission on Budget Concepts in 1967. The Commission called for the budget to include the financial transactions of all of the Federal Government's programs and agencies. For this reason, the budget includes the financial transactions of all 15 Executive departments, all independent agencies (from all three branches of Government), and all Government corporations.[2] Government corporations are distinct from Government-sponsored enterprises, which, as discussed below, are private entities and classified as non-budgetary.

All accounts in Table 33-1, "Federal Programs by Agency and Account," in the Supplemental Materials to this volume, are budgetary.[3] The vast majority of budgetary accounts are associated with the departments and other entities that are clearly Federal agencies. Some budgetary accounts reflect Government payments to non-budgetary entities, such as the Corporation for Public Broadcasting and the Legal Services Corporation. Other budgetary accounts reflect Government activity at entities that have both budgetary and non-budgetary components, such as the Smithsonian Institution. As noted below, some entities are classified as non-budgetary because they receive the majority of their funding from non-Federal sources and because they are not controlled entirely by the Government. The President's 1967 Commission on Budget Concepts recommended that the budget be comprehensive, but it also recognized that proper budgetary classification would require weighing all relevant factors regarding ownership and control of an entity. Generally, entities that are primarily owned and controlled by the Government are classified as budgetary. The budgetary classification of entities is made jointly by the Office of Management and Budget (OMB), the Congressional Budget Office (CBO), and the Budget Committees of the Congress.[4]

Off-budget Federal entities.—Despite the 1967 Commission's recommendation that the budget be com-

[1] Subsidy costs are explained in the section below on "Federal credit programs."

[2] Government corporations are Government entities that are defined as corporations under 31 U.S.C. 9101. Many Government corporations engage in a cycle of business activity with the public, selling services to the public at prices that enable the entities to be self-sustaining. Examples of Government corporations include the Commodity Credit Corporation, the Federal Deposit Insurance Corporation, the Export-Import Bank of the United States, the Federal Crop Insurance Corporation, the Overseas Private Investment Corporation, the Pension Benefit Guaranty Corporation, the Tennessee Valley Authority, and the Millennium Challenge Corporation.

[3] Table 33-1 can be found at *www.whitehouse.gov/sites/default/files/omb/budget/fy2012/assets/33_1.pdf*.

[4] Until the 2011 Budget, the Securities Investor Protection Corporation (SIPC) was classified as non-budgetary. In the fall of 2009, OMB, CBO, and the Budget Committees of the Congress reviewed the non-budgetary status of SIPC and decided to reclassify it as budgetary. The 2012 Budget includes as budgetary the Corporation for Travel Promotion created by the Travel Promotion Act of 2009, Public Law 111-145, enacted on March 4, 2010. The 2012 Budget also classifies as budgetary the State programs of reinsurance and risk adjustments mandated by the Patient Protection and Affordable Care Act, Public Law 111-148, enacted on March 23, 2010.

Table 13–1. COMPARISON OF TOTAL, ON-BUDGET, AND OFF-BUDGET TRANSACTIONS [1]

(In billions of dollars)

Fiscal Year	Receipts			Outlays			Surplus or deficit (–)		
	Total	On-budget	Off-budget	Total	On-budget	Off-budget	Total	On-budget	Off-budget
1980	517.1	403.9	113.2	590.9	477.0	113.9	–73.8	–73.1	–0.7
1981	599.3	469.1	130.2	678.2	543.0	135.3	–79.0	–73.9	–5.1
1982	617.8	474.3	143.5	745.7	594.9	150.9	–128.0	–120.6	–7.4
1983	600.6	453.2	147.3	808.4	660.9	147.4	–207.8	–207.7	–0.1
1984	666.4	500.4	166.1	851.8	685.6	166.2	–185.4	–185.3	–0.1
1985	734.0	547.9	186.2	946.3	769.4	176.9	–212.3	–221.5	9.2
1986	769.2	568.9	200.2	990.4	806.8	183.5	–221.2	–237.9	16.7
1987	854.3	640.9	213.4	1,004.0	809.2	194.8	–149.7	–168.4	18.6
1988	909.2	667.7	241.5	1,064.4	860.0	204.4	–155.2	–192.3	37.1
1989	991.1	727.4	263.7	1,143.7	932.8	210.9	–152.6	–205.4	52.8
1990	1,032.0	750.3	281.7	1,253.0	1,027.9	225.1	–221.0	–277.6	56.6
1991	1,055.0	761.1	293.9	1,324.2	1,082.5	241.7	–269.2	–321.4	52.2
1992	1,091.2	788.8	302.4	1,381.5	1,129.2	252.3	–290.3	–340.4	50.1
1993	1,154.3	842.4	311.9	1,409.4	1,142.8	266.6	–255.1	–300.4	45.3
1994	1,258.6	923.5	335.0	1,461.8	1,182.4	279.4	–203.2	–258.8	55.7
1995	1,351.8	1,000.7	351.1	1,515.7	1,227.1	288.7	–164.0	–226.4	62.4
1996	1,453.1	1,085.6	367.5	1,560.5	1,259.6	300.9	–107.4	–174.0	66.6
1997	1,579.2	1,187.2	392.0	1,601.1	1,290.5	310.6	–21.9	–103.2	81.4
1998	1,721.7	1,305.9	415.8	1,652.5	1,335.9	316.6	69.3	–29.9	99.2
1999	1,827.5	1,383.0	444.5	1,701.8	1,381.1	320.8	125.6	1.9	123.7
2000	2,025.2	1,544.6	480.6	1,789.0	1,458.2	330.8	236.2	86.4	149.8
2001	1,991.1	1,483.6	507.5	1,862.8	1,516.0	346.8	128.2	–32.4	160.7
2002	1,853.1	1,337.8	515.3	2,010.9	1,655.2	355.7	–157.8	–317.4	159.7
2003	1,782.3	1,258.5	523.8	2,159.9	1,796.9	363.0	–377.6	–538.4	160.8
2004	1,880.1	1,345.4	534.7	2,292.8	1,913.3	379.5	–412.7	–568.0	155.2
2005	2,153.6	1,576.1	577.5	2,472.0	2,069.7	402.2	–318.3	–493.6	175.3
2006	2,406.9	1,798.5	608.4	2,655.0	2,233.0	422.1	–248.2	–434.5	186.3
2007	2,568.0	1,932.9	635.1	2,728.7	2,275.0	453.6	–160.7	–342.2	181.5
2008	2,524.0	1,865.9	658.0	2,982.5	2,507.8	474.8	–458.6	–641.8	183.3
2009	2,105.0	1,451.0	654.0	3,517.7	3,000.7	517.0	–1,412.7	–1,549.7	137.0
2010	2,162.7	1,531.0	631.7	3,456.2	2,901.5	554.7	–1,293.5	–1,370.5	77.0
2011 estimate	2,173.7	1,614.3	559.4	3,818.8	3,317.3	501.5	–1,645.1	–1,703.0	57.9
2012 estimate	2,627.4	1,968.7	658.7	3,728.7	3,145.9	582.8	–1,101.2	–1,177.2	75.9
2013 estimate	3,003.3	2,273.3	730.0	3,770.9	3,121.5	649.4	–767.5	–848.2	80.6
2014 estimate	3,332.6	2,561.1	771.5	3,977.1	3,291.3	685.8	–644.6	–730.3	85.7
2015 estimate	3,583.0	2,768.1	814.9	4,189.8	3,465.0	724.7	–606.7	–696.9	90.2
2016 estimate	3,819.1	2,949.2	869.9	4,467.8	3,701.9	765.9	–648.7	–752.7	104.0

[1] Off-budget transactions consist of the Social Security trust funds and the Postal Service fund.

prehensive, every year since 1971, at least one Federal entity that would otherwise be included in the budget has been presented as off-budget because of a requirement in the law. Such off-budget Federal entities are federally owned and controlled, but their transactions are excluded, by law, from the rest of the budget totals, which are also known as "on-budget" totals. The budget reflects the legal distinction between on-budget entities and off-budget entities by showing outlays and receipts for both types of entities separately.

Although there is a legal distinction between on-budget and off-budget entities, there is no conceptual difference between the two. The off-budget Federal entities engage in the same kinds of governmental activities as the on-budget entities, and the programs of off-budget entities result in the same kind of outlays and receipts as on-budget entities. Like on-budget entities, off-budget entities are owned and controlled by the Government. The "unified budget" reflects the conceptual similarity between

on-budget and off-budget entities by showing combined totals of outlays and receipts for both types of entities.

The off-budget Federal entities currently consist of the Postal Service Fund and the two Social Security Trust Funds: Old-Age and Survivors Insurance and Disability Insurance. Social Security has been classified as off-budget since 1986 and the Postal Service Fund has been classified as off-budget since 1990.[5] Other entities that had been declared off-budget by law at different times before 1986 have been classified as on-budget by law since at least 1985.

Table 13–1 divides total Federal Government receipts, outlays, and the surplus or deficit between on-budget and off-budget amounts. Within this table, the Social Security and Postal Service transactions are classified as off-budget for all years in order to provide a consistent comparison over time. Entities that were off-budget at one time but are now on-budget are classified as on-budget for all years.

Because Social Security is the largest single program in the unified budget and is classified by law as off-budget, the off-budget accounts constitute a significant part of total Federal spending and receipts. In 2012, off-budget receipts are an estimated 25.1 percent of total receipts, and off-budget outlays are a smaller, but still significant, percentage of total outlays at 15.6 percent. The estimated unified budget deficit in 2011 is $1,645 billion—a $1,703 billion on-budget deficit partly offset by a $58 billion off-budget surplus. The off-budget surplus for 2010 and 2011 consists entirely of the Social Security surplus.[6] Social Security had small deficits or surpluses from its inception through the early 1980s and large and growing surpluses from the mid-1980s until 2008. Because of the economic downturn, the Social Security surplus has been declining for several years, but it is expected to begin growing again during the budget horizon. However, under present law, the surplus is eventually estimated to decline, turn into a deficit, and never reach balance again.

Non-Budgetary Activities

Some important Government activities are characterized as non-budgetary because they do not involve the direct allocation of resources by the Government.[7] Some of the Government's major non-budgetary activities are discussed below and, as noted below, some of these activities affect budget outlays or receipts even though they have components that are non-budgetary.

Federal credit programs: budgetary and non-budgetary transactions.—Federal credit programs make direct loans or guarantee private loans to non-Federal borrowers. The Federal Credit Reform Act of 1990 (FCRA) established the current budgetary treatment for credit programs.

Under FCRA, the budgetary cost of a credit program is known as the "subsidy cost," and outlays equal to the subsidy cost are recorded in the budget when a loan is made or guaranteed. The subsidy cost is the estimated long-term cost to the Government of a loan or a loan guarantee and it is calculated on a net present value basis, not including the Government's administrative costs of providing or guaranteeing the loan. All other credit program cash flows to and from the public are treated as non-budgetary.

To illustrate the budgetary and non-budgetary components of a credit program, consider a portfolio of new direct loans made to a cohort of college students. To encourage higher education, the Government offers loans at a lower cost than private lenders. Students agree to repay the loans according to the terms of their promissory notes. The loan terms may include lower interest rates or longer repayment periods than would be available from private lenders. Some of the students are likely to become delinquent or default on their loans, leading to Government losses to the extent the Government is unable to recover the full amount owed by the students. Under credit reform, the subsidy cost equals the net estimated lifetime cash flows to and from the Government (excluding administrative costs) discounted to the point of the loan disbursement. If the repayments of principal and interest are not sufficient to offset the expected losses from delinquencies, defaults, or costs associated with favorable loan terms, the present value of the expected future cash flows will be less than the Government disburses in loans and the Government will incur a cost (known as the subsidy cost). In other words, the subsidy cost is the difference in present value between the amount disbursed by the Government and the estimated value of the loan assets the Government receives in return. Because the loan assets have value, the remainder of the transaction (beyond the amount recorded as a subsidy) is simply an exchange of financial assets of equal value and does not result in a cost to the Government

Since credit reform first took effect in 1992, the budget outlays for credit programs have reflected only the subsidy costs of Government credit and have shown the cost when the credit assistance was or is expected to be provided. Credit reform allows the budget to reflect more accurately the cost of credit decisions.[8] This enables the

[5] See 42 U.S.C. 911 and 39 U.S.C. 2009a.

[6] The 2010 off-budget surplus reflects an $81.7 billion surplus for Social Security and a $4.7 billion deficit for the Postal Service. The estimated 2011 off-budget surplus reflects a $59.4 billion surplus for Social Security and a $1.5 billion deficit for the Postal Service, and the projected 2012 off-budget surplus reflects a $75.6 billion surplus for Social Security and a $0.3 billion surplus for the Postal Service.

[7] Tax expenditures, which are discussed in Chapter 17 of this volume, are an example of Government activities that could be characterized as either budgetary or non-budgetary. Tax expenditures refer to the reduction in tax receipts resulting from the special tax treatment accorded certain private activities. Because tax expenditures reduce tax receipts and receipts are budgetary, tax expenditures clearly have budgetary effects. However, the size and composition of tax expenditures are not explicitly recorded in the budget as outlays or as negative receipts and, for this reason, tax expenditures might be considered a special case of non-budgetary transactions.

[8] Both credit reform accounting and the earlier cash accounting of Federal credit programs would ultimately show the same costs for credit transactions. For example, cash accounting for direct loans would show the full disbursement of the loan as an outlay when it was made, and then later show the repayments of principal and interest as an offset to outlays. Over the life of the loan, only the net cost of the loan would ultimately be reflected in the budget. Credit accounting shows that same net cost, but shows that cost at the time the loan is made (adjusting

budget to fulfill its purpose of serving as a financial plan for allocating resources among alternative uses by comparing the expected cost of credit programs with their benefits, comparing the cost of credit programs with the cost of other spending programs, and comparing the cost of one type of credit assistance with the cost of another type.[9] Credit programs are discussed in more detail in Chapter 23 of this volume, "Credit and Insurance."

Deposit funds.—Deposit funds are non-budgetary accounts that record amounts held by the Government temporarily until ownership is determined (such as earnest money paid by bidders for mineral leases) or held by the Government as an agent for others (such as State income taxes withheld from Federal employees' salaries and not yet paid to the States). The largest deposit fund is the Government Securities Investment Fund, which is also known as the G Fund. It is one of several investment funds managed by the Federal Retirement Thrift Investment Board, as an agent, for Federal employees who participate in the Government's defined contribution retirement plan, the Thrift Savings Plan (which is similar to private-sector 401(k) plans). Because the G Fund assets, which are held by the Department of the Treasury, are the property of Federal employees and are held by the Government only in a fiduciary capacity, the transactions of the Fund are not resource allocations by the Government for public purposes and are therefore non-budgetary.[10] For similar reasons, the budget excludes funds that are owned by Native American Indians, but held and managed by the Government in a fiduciary capacity.

Government-sponsored enterprises.—The Federal Government has chartered Government-sponsored enterprises (GSEs) such as the Federal National Mortgage Association (Fannie Mae), the Federal Home Loan Mortgage Corporation (Freddie Mac), the Federal Home Loan Banks, the Farm Credit System, and the Federal Agricultural Mortgage Corporation to provide financial intermediation for specified public purposes. Although federally chartered to serve public-policy purposes, the GSEs are classified as non-budgetary and excluded from the Budget. This is because they are intended to be privately owned and controlled, with any public benefits accruing indirectly, resulting from the GSEs' business transactions. Estimates of the GSEs' activities are reported in a separate chapter of the *Budget Appendix,* and their activities are discussed in Chapter 23 of this volume, "Credit and Insurance."

In September 2008, in response to the financial market crisis, the director of the Federal Housing Finance Agency (FHFA)[11] placed Fannie Mae and Freddie Mac into conservatorship for the purpose of preserving the assets and restoring the solvency of these two GSEs. As conservator, FHFA has broad authority to direct the operations of these GSEs. However, these GSEs remain private companies with Boards of Directors and management responsible for their day-to-day operations.

This Budget continues to treat these two GSEs as non-budgetary private entities in conservatorship rather than as Government agencies. By contrast, the CBO treats these GSEs as budgetary Federal agencies. Both treatments include budgetary and non-budgetary amounts.

Under the approach in the Budget, all of the GSEs' transactions with the public are non-budgetary because the GSEs are not considered to be Government agencies. However, the payments from the U.S. Treasury to the GSEs are recorded as budgetary outlays. Under CBO's approach, the subsidy costs, or expected losses over time, of the GSEs' past credit activities have already been recorded in the budget estimates and the subsidy costs of future credit activities will be recorded when the activities occur. Lending and borrowing activities between the GSEs and the public apart from the subsidy costs are treated as non-budgetary by CBO, and Treasury payments to the GSEs are intragovernmental transfers (from Treasury to the GSEs) that net to zero in CBO's budget estimates.

Overall, both the Budget's accounting and CBO's accounting present the GSEs' losses as Government outlays, which increase Government deficits. The two approaches, however, reflect the losses as budgetary costs at different times.[12]

Other Federally Created Non-Budgetary Entities.—In addition to chartering the GSEs, the Federal Government has created a number of other entities that are classified as non-budgetary. These include federally funded research and development centers (FFRDCs), non-appropriated fund instrumentalities (NAFIs), and

the cash flows for the time-value of money). Under cash accounting, the outlays recorded when a loan was made overstated the lifetime costs of the loan and the outlays recorded when a guarantee was made understated the lifetime cost of the guarantee. Credit reform makes it possible to consider the full cost of a credit program at the time the program decisions are made and in a way that enables the cost of credit programs to be compared to other forms of Government assistance, such as grants.

[9] For more explanation of the budget concepts for direct loans and loan guarantees, see the sections on Federal credit and credit financing accounts in Chapter 12 of this volume, "Budget Concepts." The structure of credit reform is further explained in Chapter VIII.A of the *Budget of the United States Government*, Fiscal Year 1992, Part Two, pp. 223–226. The implementation of credit reform through 1995 is reviewed in Chapter 8, "Underwriting Federal Credit and Insurance," *Analytical Perspectives, Budget of the United States Government*, Fiscal Year 1997, pp. 142–144. Refinements and simplifications enacted by the Balanced Budget Act of 1997 or provided by later OMB guidance are explained in Chapter 8, "Underwriting Federal Credit and Insurance," *Analytical Perspectives, Budget of the United States Government,* Fiscal Year 1999, p. 170.

[10] The administrative functions of the Federal Retirement Thrift Investment Board are carried out by Government employees, and are, therefore, included in the budget.

[11] The Housing and Economic Recovery Act of 2008, enacted on July 30, 2008, created the FHFA as the new regulator for Fannie Mae, Freddie Mac, and the Federal Home Loan Banks. FHFA reflects the merger of the Office of Federal Housing Enterprise Oversight, the Federal Housing Finance Board, and the Department of Housing and Urban Development's Government-sponsored enterprise mission team.

[12] The two approaches would be the same over the long run under the assumption that the Government maintains its current relationship with the two GSEs indefinitely.

other entities, some of which are incorporated as non-profit entities.

FFRDCs are entities that conduct agency-specific research under contract or cooperative agreement. Most FFRDCs were created by and conduct research for the Departments of Defense and Energy, and most are administered by colleges, universities, or other non-profit entities. Examples of federally funded research and development centers are the Center for Naval Analysis, Los Alamos National Laboratory, and the Jet Propulsion Laboratory.[13] FFRDCs are non-budgetary, but the Federal agency's payments to the FFRDC are recorded as budget outlays. In addition to Federal funding, FFRDCs may receive funding from non-Federal sources.

Non-appropriated fund instrumentalities (NAFIs) are entities that support an agency's personnel. Virtually all NAFIs are associated with the Departments of Defense, Homeland Security (Coast Guard), and Veterans Affairs. Most NAFIs are located on military bases and include the armed forces exchanges (which sell goods to military personnel and their families), recreational facilities, and child care centers. NAFIs do not receive direct appropriations; they are financed by the proceeds from the sale of goods or services. Because NAFIs are non-budgetary, any agency payments to the NAFIs are recorded as budget outlays.

A number of entities created by the Government receive a significant amount of non-Federal funding and are primarily or wholly controlled by non-Federal individuals or organizations. Although not exhaustive, this list of entities includes Amtrak, the Corporation for Public Broadcasting, Gallaudet University, Howard University, the Legal Services Corporation, the National Academy of Sciences, the Neighborhood Reinvestment Corporation, the Smithsonian Institution, the United States Enrichment Corporation, and the United States Institute of Peace. Most of these entities receive direct appropriations or other recurring payments from the Government, which are budgetary and included in Table 33-1, mentioned above. However, many of these entities are non-budgetary. Generally, entities that receive a significant portion of funding from non-Federal sources and that are not controlled by the Government are treated as non-budgetary. As noted above, classifications for budgetary and non-budgetary status are made jointly by OMB, CBO, and the Budget Committees of the Congress.[14]

Regulation.—Federal Government regulation often requires the private sector or other levels of government to make expenditures for specified purposes that are intended to have public benefits, such as safety and pollution control. Although the budget reflects the Government's cost of conducting regulatory activities, the costs imposed on the private sector as a result of regulation are treated as non-budgetary and not included in the budget. The Government's regulatory priorities and plans are described in the annual Regulatory Plan and the semi-annual Unified Agenda of Federal Regulatory and Deregulatory Actions.[15]

The estimated costs and benefits of Federal regulation have been published annually by OMB since 1997. The latest report was released in July 2010.[16] In this report, OMB indicates that the estimated annual benefits of Federal regulations it reviewed from October 1, 1999, to September 30, 2009, range from $128 billion to $616 billion, while the estimated annual costs range from $43 to $55 billion. In its report, OMB discusses the impact of Federal regulation on State, local, and tribal governments, and agency compliance with the Unfunded Mandates Reform Act of 1995. The costs and benefits of Federal regulation are also discussed in Chapter 9 of this volume, "Benefit-Cost Analysis."

Monetary policy.—As noted above, the budget is a financial plan for allocating resources by raising revenues and spending those revenues. As a fiscal policy tool, the budget is used by elected Government officials to promote economic growth and achieve other public policy objectives. Monetary policy is another tool that governments use to promote public policy objectives. In the United States, monetary policy is conducted by the Federal Reserve System, which is composed of a Board of Governors and 12 regional Federal Reserve Banks. The Federal Reserve Act provides that the goal of monetary policy is to "maintain long run growth of the monetary and credit aggregates commensurate with the economy's long run potential to increase production, so as to promote effectively the goals of maximum employment, stable prices, and moderate long-term interest rates."[17] The dual goals of full employment and price stability were reaffirmed by the Full Employment and Balanced Growth Act of 1978, also known as the Humphrey-Hawkins Act.[18]

By law, the Federal Reserve System is a self-financing entity that is independent of the Executive Branch and subject to only broad oversight by the Congress. Consistent with the recommendations of the 1967 President's Commission on Budget Concepts, the effects of monetary policy and the actions of the Federal Reserve

[13] The National Science Foundation maintains a list of FFRDCs at *www.nsf.gov/statistics/ffrdc*.

[14] In the spring of 2010, OMB, CBO, and the Budget Committees of Congress agreed to reclassify as non-budgetary those copyright royalties received and subsequently paid out by the Copyright Office where (1) the amount paid by users of copyrighted material to copyright owners is directly related to the frequency or quantity of the material used, and (2) the law allows copyright owners and users to voluntarily set the rate paid for the use of protected material. Because they do not satisfy these two conditions, the copyright fees collected and paid out by the Copyright Office under 17 U.S.C. 1004 remain classified as budgetary.

[15] The most recent Regulatory Plan and introduction to the Unified Agenda were issued by the General Services Administration's Regulatory Information Service Center and were printed in the Federal Register of April 26, 2010. Both the Regulatory Plan and Unified Agenda are available on-line at *www.reginfo.gov and at www.gpoaccess.gov*.

[16] Office of Information and Regulatory Affairs, OMB, 2010 Report to Congress on the Benefits and Costs of Federal Regulations and Unfunded Mandates on State, Local, and Tribal Entities (July 2010). The Report is available at *www.whitehouse.gov/omb/inforeg_regpol_reports_congress/*.

[17] See 12 U.S.C. 225a.

[18] See 15 U.S.C. 3101 et seq.

System are, with two exceptions, non-budgetary. Although the relatively recent increase in the Federal Reserve's balance sheet in response to the financial crisis has had important macroeconomic consequences, it does not directly affect the Federal deficit.

The exceptions to the treatment of Federal Reserve transactions as non-budgetary involve excess earnings of the Federal Reserve System. The Federal Reserve System earns income from a variety of sources including interest on U.S. Government securities, foreign currency investments and loans to depository institutions, and fees for services (e.g., check clearing services) provided to depository institutions. After paying its expenses, the Federal Reserve System remits to the U.S. Treasury any excess income. This income, which is classified in the budget as a governmental receipt, was equal to $75.9 billion in 2010. The recent expansion of the Federal Reserve's balance sheet has increased its sources of income (and potential loss), which in turn has affected the Federal Reserve's excess income payment to the Treasury. In addition to remitting excess income to the Treasury, the Dodd-Frank Wall Street Reform and Consumer Protection Act requires the Federal Reserve to transfer a portion of its excess earnings to the Consumer Financial Protection Bureau, an independent bureau of the Federal Reserve, which was created by the Act.[19]

The Board of Governors is a Federal Government agency, but because of its independent status, its budget is not subject to Executive Branch review and is included in the *Budget Appendix* for informational purposes only. The Federal Reserve Banks are subject to Board oversight and managed by boards of directors chosen by the Board of Governors and member banks, which include all national banks and state banks that choose to become members. The budgets of the regional Banks, although subject to approval by the Board of Governors, are not included in the *Budget Appendix*.

Indirect macroeconomic effects of Federal activity.—Government activity has many effects on the Nation's economy that extend beyond the amounts recorded in the budget. Government expenditures, taxation, tax expenditures, regulation, and trade policy can all affect the allocation of resources among private uses and income distribution among individuals. These effects, resulting indirectly from Federal activity, are generally not part of the budget, but the most important of them are discussed in this volume. For example, the effects of the American Recovery and Reinvestment Act of 2009 (ARRA), among other things, are discussed in Chapter 2 of this volume, "Economic Assumptions."

Financial Stabilization Activity

Since late 2007, the Federal Reserve System, Executive Branch agencies, and the GSEs Fannie Mae and Freddie Mac have been engaged in a variety of activities designed to stabilize the financial markets and restore economic growth. The actions taken by the Federal Reserve System[20] are non-budgetary for reasons discussed above in the section on "Monetary policy." However, as also noted above, Federal Reserve actions may affect the System's earnings, which ultimately affect governmental receipts. The placement of Fannie Mae and Freddie Mac into conservatorship, discussed above in the section on "Government-sponsored enterprises," is not treated as affecting their non-budgetary status, so the GSEs' transactions with the public are not included in the 2012 Budget. However, as with other transactions between non-budgetary entities and the Government, the transactions of the GSEs with the Government, including all cash payments from the Treasury to the GSEs, are included in the budget.

Executive Branch activities in support of financial market stabilization include actions taken by the Department of the Treasury, the Federal Deposit Insurance Corporation (FDIC), the National Credit Union Administration (NCUA), and the Federal Housing Finance Agency (FHFA). The Treasury activities include the Public-Private Investment Partnership program, the Term Asset-Backed Securities Loan Facility (administered jointly with the Federal Reserve), the Small Business Lending Fund, the State Small Business Credit Initiative, the Homeowner Affordability and Stability Plan, the GSE Credit Facility, and the GSE mortgage-backed securities purchases. Actions by the FDIC include the Temporary Liquidity Guarantee Program and actions by the NCUA include the Temporary Corporate Credit Union Liquidity Guarantee Program. Actions by the FHFA include the placement of the GSEs into conservatorship in 2008 and the subsequent and ongoing management of the GSEs. Chapter 4 of this volume, "Financial Stabilization Efforts and Their Budgetary Effects," discusses all Government efforts to stabilize the financial markets and restore economic growth.

As distinct from the activities of the Federal Reserve and the GSEs, the activities of the Department of the Treasury, the FDIC, and the NCUA are budgetary. Financial asset acquisitions, loans, and loan guarantees under the Troubled Asset Relief Program (TARP), are reported in the budget on a credit basis.[21] As discussed above in the section on "Federal credit programs," this

[19] See section 1011 of Public Law 111-203, enacted on July 21, 2010. OMB determined that the Consumer Financial Protection Bureau is a budgetary entity.

[20] The following Federal Reserve liquidity facilities that were created during the financial market crisis have been allowed to expire: the Asset-Backed Commercial Paper Money Market Mutual Fund Liquidity Facility, the Commercial Paper Funding Facility, the Money Market Investor Funding Facility, the Primary Dealer Credit Facility, the Term Auction Facility, and the Term Securities Lending Facility. The Federal Reserve Bank of New York continues to lend under the Term Asset-Backed Securities Loan Facility, a program administered jointly with the Department of the Treasury.

[21] The Emergency Economic Stabilization Act (EESA) (section 123(a)) provides the authority to record the costs of all troubled assets purchased (or guaranteed) under TARP in accordance with the Federal Credit Reform Act (FCRA). EESA further requires (in section 123(b)) that the discount rate used for recording these costs reflect market risk, which is in contrast to the risk-free discount rate required under FCRA for calculating the costs of loans and loan guarantees not authorized by EESA.

means that outlays equal to the net present value of all future cash flows with the public are recorded when the transaction occurs. The rationale for recording financial asset purchases under TARP on a credit basis rather than on a cash basis is the same as the rationale, discussed above, for loans and loan guarantees generally: the Government's cost of purchasing a financial asset that is intended to be sold at some point in the future is not equal to the cash used to acquire the asset at the time of acquisition. Rather, the cost is equal to the present value of the cash outflows for acquiring the asset less the present value of cash inflows from holding and ultimately selling the asset.

The total budget impact of all of the credit market stabilization efforts undertaken by the Treasury, other Executive Branch agencies, the GSEs, and the Federal Reserve may not be known with certainty for several years. Nevertheless, actual and estimated outlays and receipts are included in the 2012 Budget. In addition, the actual and estimated impacts of credit market stabilization efforts on the Federal debt held by the public are included in the 2012 Budget.

14. BUDGET PROCESS

Since taking office, the Administration has strived to present budget figures that accurately reflect the present and future course of the Nation's finances, and continues to strive to make improvements in budget process and enforcement. An honest and transparent accounting of our Nation's finances is critical to making decisions about key fiscal policies. This chapter begins with an overview of the Administration's significant accomplishments in promoting budget discipline and improved transparency, particularly the restoration of the statutory Pay-As-You-Go rule, which was a key component of balancing the budget in the late 1990s.

The chapter then describes two broad categories of budget reform proposals. First, the chapter describes proposals to strengthen budgeting and fiscal sustainability of individual programs as well as across Government, such as critical transportation and education programs, and a proposal for a fast-track procedure for Congress to consider certain rescission requests. Together these will help to impose greater discipline on revenue and spending policies.

Second, the chapter presents a revised baseline, which includes a projection of the costs of certain major tax and spending policies currently in effect, such as relief from the growing scope of the Alternative Minimum Tax, even though those policies are scheduled to expire within the budget window. In addition, the Budget includes an allowance for the costs of possible future natural disasters. This revised baseline better captures the likely future costs of operating the Federal Government.

Taken together, these reforms generate a Budget that is more transparent, comprehensive, accurate, and realistic, and is thus a better guidepost for citizens and their representatives in making decisions about the key fiscal policy issues we confront as a Nation.

I. CHANGES IN THE BUDGET PROCESS AND BUDGET DISPLAY

The Administration supports the following reforms that would supplement the budget process laid out in the Congressional Budget Act of 1974: 1) implementing the renewed statutory Pay-As-You-Go (PAYGO) rule, 2) conducting PAYGO reviews of potential administrative actions by Executive Branch agencies affecting mandatory programs, 3) treating spending from the proposed Transportation Trust Fund as mandatory, 4) offsetting some of the cost increases in the Pell Grant program with mandatory savings, 5) treating Postal Service reform on a unified budget basis for purposes of PAYGO enforcement, 6) proposing an option for the expedited consideration of certain rescission proposals, 7) proposing program integrity funding, including appropriations "allocation adjustments," to support the cost-efficient administration of mandatory programs and tax collection, 8) protecting appropriated funding in the Disaster Relief Fund for major disasters and emergencies, 9) limiting the use of advance appropriations for discretionary programs, 10) supporting a display of debt net of offsetting financial assets, and 11) continuing the current display of Fannie Mae and Freddie Mac while transitioning to a new housing finance system.

Statutory PAYGO

The Statutory Pay-As-You-Go Act of 2010 (PAYGO, or "the Act") is part of Public Law 111-139, enacted on February 12, 2010. A key priority for this Administration, the Act significantly strengthens the rules of budget discipline.

Drawing upon the version of the law enacted as part of the 1990 Budget Enforcement Act, the Act requires that all new legislation changing taxes or mandatory expenditures and collections, taken together, must not increase projected deficits. This requirement is enforced by an accompanying requirement of automatic across-the-board cuts in selected mandatory programs if legislation taken as a whole does not meet that standard. PAYGO also established special scorecards and scorekeeping rules.

The PAYGO Principle.—The principle underlying PAYGO is a rule of budget neutrality—that is, the government must not enact new laws that, when added together, would increase projected deficits. In general, adherence to PAYGO does not by itself reduce projected deficits, but during the 1990s, when the first statutory PAYGO law was in effect, adherence to the principle reinforced—and effectively locked into place—the substantive deficit-reduction measures enacted in 1990, 1993, and 1997, which contributed to the surpluses in the last four years of the Clinton Administration.

Moreover, adherence to PAYGO will reduce projected deficits relative to the Administration's adjusted baseline in two cases. Specifically, the adjusted baseline, discussed at the end of this chapter, assumes that AMT relief and estate tax relief will be continued after 2011 while PAYGO requires those two forms of tax relief to be offset. In this case, adherence to PAYGO will reduce baseline deficits by $1,718 billion through 2021, including interest.

Legislation Covered by PAYGO.—PAYGO applies to laws enacted after February 12, 2010, that would alter revenues or mandatory spending or collections. Mandatory spending encompasses any spending except that controlled by the annual appropriations process. [1]

PAYGO requires that bills reducing revenues must be fully offset by cuts in mandatory programs or by revenue increases. It also requires that any bills increasing mandatory expenditures must be fully offset by revenue increases or cuts in mandatory programs. The requirement applies to bills enacted during a congressional session, not to any individual bill. For purposes of PAYGO, there is no fundamental distinction between mandatory and tax legislation. Although the PAYGO principle is mostcommonly described as barring legislation that would increase projected deficits, the Act, which is permanent, would continue to apply even if the budget were in surplus.

Enforcement.—If Congress enacts PAYGO bills cutting taxes or increasing mandatory expenditures without fully offsetting the costs, the Act requires a process called "sequestration." If Congress adjourns at the end of a session with net costs—that is, more costs than savings—on the scorecard, the Office of Management and Budget (OMB) is required to calculate, and the President is required to issue, a sequestration order implementing, across-the-board cuts to a select group of mandatory programs in an amount sufficient to offset the net costs on the PAYGO scorecard.

Exemptions from a sequestration order include Social Security; most unemployment benefits; veterans' benefits; interest on the debt; Federal retirement; and the low-income entitlements such as Medicaid, the Supplemental Nutrition Assistance Program (SNAP, formerly known as food stamps), and Supplemental Security Income (SSI).[2] The major remaining mandatory programs, which are subject to sequestration, include most Medicare payments, farm price supports, vocational rehabilitation basic state grants, mineral leasing payments to States, the Social Services Block Grant, and many smaller programs.

If a sequestration is ordered, each non-exempt mandatory program is reduced for one year by the same percentage, with one exception: Medicare payments subject to sequestration cannot be reduced more than 4 percent.[3] Consequently, if an overall 4 percent sequestration would not suffice to offset net costs on the PAYGO scorecard, sequestrable Medicare payments would be cut 4 percent and all other non-exempt programs would be cut by a higher uniform percentage. In effect, if a large sequestration is needed, the bar to cutting sequestrable Medicare payments by more than 4 percent means that other non-exempt programs must make up the difference.

Even though sequestration is calculated to fully offset any net costs on the PAYGO scorecard, it historically has acted as a successful deterrent, and so has not been implemented. During the 1990s, under the first statutory PAYGO law, the sequestration rules and exemptions were almost identical to those in the current Act. Congress complied with PAYGO throughout that decade. As a result, no PAYGO sequestration ever occurred.

The PAYGO Scorecards.—Under PAYGO, OMB must maintain a 5-year and a 10-year scorecard that record the cost or savings of every PAYGO bill enacted in each session of Congress. The 5-year scorecard displays columns for the budget year and each of the next four years, while the 10-year scorecard displays columns for the budget year and each of the next nine years. OMB maintains running totals for all PAYGO bills. The total costs and savings are then averaged over 5 and 10 years, respectively, before being entered on the scorecards.[4] At the end of each session of Congress (usually in December), OMB looks to the scorecards to determine whether a sequestration is necessary. The key question for purposes of sequestration is whether the sum for the budget year on either the 5-year scorecard or the 10-year scorecard is positive—that is, costs exceed savings—when Congress adjourns at the end of a session. If either sum is positive, the sequestration described above will go into effect automatically to offset the net costs. If both the 5- and 10-year scorecards show net costs, the sequestration must offset the higher amount.

The first annual report under the PAYGO Act was issued on January 13, 2011, and is available at www.omb.gov. It shows that savings exceeded costs by $11.0 billion per year on the 5-year scorecard and by $6.4 billion per year in the 10-year scorecard. Since both amounts are negative, sequestration was not necessary.

When Congress starts a new session, the budget year will shift forward by one year and the two scorecards will each extend one year into the future. The net sum of all prior entries—the PAYGO balances from prior sessions of Congress—will remain on the scorecard and be part of the calculations. For example, the current session of Congress starts with a credit (a negative balance) of $11.0 billion on the five-year scorecard for each year 2012 through 2015,

[1] Mandatory spending is termed *direct spending* in the PAYGO Act. The term *mandatory* encompasses entitlement programs, e.g., Medicare and Medicaid, and *any* funding not controlled by annual appropriations bills, such as the automatic availability of immigration examination fees to the Department of Homeland Security.

[2] Although many programs are exempt from sequestration, those programs are rarely exempt from PAYGO. For example, a bill to increase veterans' disability benefits or Medicaid benefits must be offset, even though a sequestration, if it is required, will not reduce those benefits.

[3] Medicare payments for services, devices, or insurance plans are subject to sequestration within the 4 percent limit described above; other payments—such as the low-income subsidy that is part of the prescription drug benefit—are not subject to sequestration.

[4] Costs or savings that occur in the current year are treated as though they occur in the budget year. The terms *budget year* and *current year* are defined with respect to a session of Congress; the budget year means the fiscal year that will start or has started on the October 1 that falls within that session of Congress, and the current year is the fiscal year before the budget year.

the result of the net PAYGO savings enacted by the prior Congress. However, the five-year scorecard rolls over by one year, and now covers the years through 2016, with no credits in the 2016 column of the five-year scorecard. Therefore, if Congress enacts legislation that costs $5 billion per year without paying for those costs, the existing balances on the five-year scorecard would more than cover those costs in each year through 2015, but the 2016 column of the scorecard would show a debit of $5 billion. If no other PAYGO legislation were subsequently enacted, no sequestration would occur until the end of calendar year 2015, but at that time a $5 billion sequestration would be ordered to eliminate the $5 billion debit for 2016, the fiscal year that would have just started.

***Special Rules for Certain PAYGO Estimates*.—** There are a number of special rules that affect whether all estimated budgetary effects of PAYGO bills are entered on the scorecard.

- Off-budget costs or savings are excluded. The Social Security trust funds and the Postal Service fund are the only two Federal programs designated as off-budget by law. If legislation affects Social Security, for example, those effects, though shown in the unified budget, will not be entered on the PAYGO scorecards. As described later in this chapter, the Administration proposes that the unified budget effects of Postal Service reform legislation be recorded on the PAYGO scorecards.
- Emergency costs are excluded. If Congress statutorily designates specified costs as emergency requirements under the Act, the costs are not entered on the PAYGO scorecard but instead are shown separately. As noted in the first annual PAYGO report, the prior Congress enacted a net of $529 billion in emergency costs over the ten-year period through 2020. Those costs, all of which are temporary, are listed on the scorecards but excluded from the official totals.
- Certain timing shifts are excluded. Congress cannot use timing shifts to avoid violating PAYGO on the 10-year scorecard. If a PAYGO bill contains provisions that would move costs from year ten of the scorecard to year 11, or would move savings from year 11 onto the last year of the scorecard, the effects of those timing shifts are ignored.
- CLASS Act savings of almost $79 billion over ten years are excluded. The CLASS Act, enacted as part of health care reform, established a voluntary, fully prefunded long-term care benefit, with the value of the benefit linked directly to the value of the advance funding. Because it is fully prefunded, the program reduces deficits in the early years but has a long-term present value of zero. A special provision of the PAYGO Act provides that the up-front savings from the CLASS Act are not entered on the PAYGO scorecards.
- Current-policy scorekeeping adjustments can reduce scored costs. PAYGO is described as requiring that legislation not increase projected deficits, relative to current law (baseline). This raises the question of how existing tax and mandatory laws are projected. In most cases, baseline projections are assumed to reflect scheduled changes built into those existing laws. For example, future benefits under the SSI program are indexed to inflation under current law, as are tax brackets. This indexing is assumed to occur on schedule, so a PAYGO law is viewed as changing future deficits only if it changes some aspect of law that is already scheduled to occur.

  However, under the Act there are five exceptions to this general rule. Each exception exists because the scheduled future changes in the law are considered so unlikely, based on past history, that they do not provide a reasonable benchmark for judging the effect of new legislation.

1. Some longstanding programs require periodic reauthorization, such as farm price supports, SNAP, the Children's Health Insurance Program (CHIP), and Temporary Assistance to Needy Families (TANF). These programs are treated as though they are ongoing, which has been the rule since baselines were first developed in the 1970s.[5]

2. At the time PAYGO was enacted, a temporary increase in the exemption from the Alternative Minimum Tax (AMT) had not yet been enacted for tax year 2010. In the past, Congress had consistently granted "temporary" relief from the scheduled AMT change. Anticipating a continuation of this practice, PAYGO provided that the cost of AMT relief, relative to scheduled law, would be adjusted downward, but not below zero, by an amount equal to the costs of granting relief equivalent to that in effect in 2008. The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 extended AMT relief through tax year 2011, the period of the downward current policy adjustment provided for in the Act.

3. Reimbursement rates for Medicare physicians are scheduled to decrease dramatically under the "Sustainable Growth Rate" (SGR) provision of Medicare. Since 2003, Congress has granted "temporary" relief from the SGR cuts. In this case, the Act does not change the baseline, which continues to reflect scheduled SGR law. Rather, it provides that legislation extending relief from the scheduled

[5] One consequence of this rule is that a five-year reauthorization of SNAP that, for example, increases benefits is scored as though it increases benefits permanently, since the underlying program is treated as permanent. Therefore, that increase would be scored as producing costs in all ten columns of the ten-year scorecard, and so would require ten years of offsets.

SGR cuts is not scored as producing PAYGO costs except to the extent that the relief is more generous than the relief in effect in 2009. More precisely, if a SGR provision is enacted, the cost of that provision, relative to scheduled law, is adjusted downward, but not below zero, by an amount equal to the costs of granting relief equivalent to that in effect in 2009. The maximum current policy adjustment is equal to the costs of relief up to the 2009 payment levels, through December 31, 2014. Any fixes that extend past that point are scored relative to current law. Finally, SGR relief that is less generous than the relief in effect in 2009 would be available to offset costs of SGR relief after 2014, but only for that purpose; such savings could not offset other PAYGO costs. In three bills between June and December of 2010, Congress enacted temporary SGR relief through December 2011 at payment rates 2.2 percent above those defined in the PAYGO Act, so those incremental costs appear on the PAYGO scorecards.[6]

4. At the time PAYGO was enacted, the phased reduction and ultimate repeal of the estate tax was scheduled to sunset at the end of 2010, at which point the 2001 version of the estate tax would spring back to life. The PAYGO Act provided for a current policy adjustment for granting estate tax relief based on 2009 parameters, but only through tax year 2011. In December 2010, Congress enacted a more expensive version of estate tax relief through 2012 as part of the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010, so a portion of those costs were excluded from the PAYGO scorecards through a downward adjustment. (The remaining costs were declared an emergency.)

5. A wide variety of cuts to the individual income tax were enacted in the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA) and the Jobs and Growth Tax Relief Reconciliation Act of 2003 (JGTRRA), and some of those tax cuts have been amended. At the time PAYGO was enacted, all of these tax cuts were scheduled to expire on December 31, 2010. The PAYGO Act set the benchmark for the current policy adjustment equal to the relevant provisions of the tax code as in effect for 2010 and allowed the relief from the scheduled expiration of those tax cuts to be permanent. Note that this relief does not apply to all the provisions of EGTRRA and JGTRRA—only those referred to as the "middle-class" tax cuts. Under the PAYGO Act, permanent current policy adjustments are allowed for the following provisions of EGTRRA and JGTRRA:

   - The 10-percent income tax bracket;
   - The child tax credit;
   - Tax benefits for married couples;
   - The adoption tax credit;
   - The dependent care tax credit;
   - The employer-provided child care tax credit;
   - The education tax benefits;
   - The 25-percent and 28-percent tax brackets;
   - The 33-percent tax bracket, but only for taxpayers with Adjusted Gross Income (AGI) of $200,000 or less for single filers or $250,000 or less for married filers;
   - The tax rates on capital gains and dividends, but only for taxpayers with AGI of $200,000 or less for single filers or $250,000 or less for married filers;
   - The phase-out of personal exemptions (PEP) and the limitation on itemized deductions (Pease), but only for taxpayers with AGI of $200,000 or less for single filers or $250,000 or less for married filers; and
   - The increased limits on "expensing" small business assets under §179(b) of the internal revenue code.

   In December 2010, as part of the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010, Congress extended all of EGTRRA and JGTRRA through 2012. The extension of the middle-class provisions described above generated an offsetting downward adjustment on the PAYGO scorecard, while the extension of the upper-income portions of EGTRRA and JGTRRA was declared an emergency.

As described in items two through five above, current policy adjustments allow the enactment without offsets of relief from certain scheduled changes in laws. Whether the relief is allowed through 2011 (AMT, estate tax), through 2014 (Medicare physician reimbursement rates), or permanently (middle-class tax cuts), the legislation providing that relief must be enacted by December 31, 2011, to be eligible for the current policy adjustments. The previous session of Congress enacted legislation generating offsetting downward adjustments to the PAYGO scorecard of almost $434 billion through 2020.

Responsibility for PAYGO Estimates.—The Act specifies two mechanisms for providing PAYGO cost estimates. The first uses an estimate included in the Congressional Record by the Chairmen of the Budget

[6] Congress chose to offset the entire cost of the relief, even though the PAYGO Act did not require such offsets.

Committees. The second relies on OMB to produce the PAYGO estimate.

Under the first mechanism, Congress can determine the costs or savings of PAYGO bills by enacting those estimates into law. Under the Act, Congress includes within the text of a PAYGO bill a cross-reference to an estimate that will have been included in the Congressional Record by the Chairmen of the Budget Committees. That estimate must be submitted to the Record before the House of Representatives or the Senate has voted on final passage of that PAYGO bill but after they have voted on the last amendment (if any) to that bill. Under this mechanism, OMB's role is limited to entering the congressionally determined estimates on the 5-year and 10-year PAYGO scorecards, averaging and cumulating the entries, and calculating any sequestration that might be needed.

If Congress does not determine the costs or savings of PAYGO legislation as described above, the Act requires OMB to estimate the budgetary effects for the scorecards using the economic and technical assumptions underlying the President's Budget. Cost and savings estimates are entered on the scorecard after PAYGO bills are enacted. Entries on the scorecard are not later changed, even if new estimates could be developed based on more recent information.

If Congress determines the costs of legislation, as the PAYGO Act envisions, it is significant that on January 5, 2011, the House of Representatives agreed to a special order that permits the Budget Committee Chairman to certify that the costs of certain types of legislation are zero when PAYGO estimates are introduced into the Congressional Record:

- Repeal of the Affordable Care Act.
- Extension of EGTRRA and JGTRRA. (This would have the effect of expanding the current adjustment in PAYGO to include the upper-income provisions of EGTRRA and JGTRRA.)
- Extension of AMT relief and estate tax repeal. (This provision would have the effect of making the PAYGO adjustments, which are available only through 2011, permanent. Moreover, this provision would increase the size of the adjustment for the estate tax, allowing its complete repeal without offsets, whereas the PAYGO Act allowed the estate tax to be scaled back without offsets from the $1 million exemption and maximum 55 percent rate under 2001 law only to a $3.5 million exemption and maximum 45 percent rate).
- Creation of a 20 percent deduction in income to small businesses.
- Enactment of legislation implementing trade agreements.

Legislation described in the first three bullets would add approximately $2.9 trillion in ten-year costs to the PAYGO scorecards under the definitions and current policy adjustments in that Act, but would add no costs, and therefore would not have to be offset, under the terms of the House's new special order. For example, CBO estimates that repealing the Affordable Care Act would cost $230 billion over the next decade. Under the House's new special order, however, this cost would not have to be offset. Thus, after counting interest, the new House rules could have the effect of increasing deficits over the 10-year scorecard window by $3.4 trillion.

Administrative PAYGO

The Administration will continue to review potential administrative actions by Executive Branch agencies affecting entitlement programs, as stated in a memorandum issued on May 23, 2005, by the Director of the Office of Management and Budget. This effectively establishes a PAYGO requirement for administrative actions involving mandatory spending programs. Exceptions to this requirement are only provided in extraordinary or compelling circumstances.

Budgetary Treatment of Surface Transportation Infrastructure Funding

Overview.—Currently, surface transportation programs financed from the Highway Trust Fund (HTF) are treated as hybrids: contract authority[7] is classified as mandatory, while outlays are classified as discretionary. Broadly speaking, this framework evolved as a mechanism to ensure that collections into the HTF (e.g., motor fuel taxes) were used to pay only for programs that benefit surface transportation users, and that funding for those programs would generally be commensurate with collections. However, the framework no longer functions as it was intended, because collections are no longer adequate to support current law spending levels. Absent that central part of the bargain—enough revenue to support spending—the system does not give policy-makers appropriate incentives to make fiscally sound choices and bring revenue and spending in line.

The National Commission on Fiscal Responsibility and Reform (the "Fiscal Commission") recognized this problem and recommended changing the scorekeeping treatment of surface transportation programs:

> This hybrid treatment results in less accountability and discipline for transportation spending and allows for budget gimmicks to circumvent budget limits to increase spending. The Commission plan reclassifies spending from the Transportation Trust Fund to make both contract authority and outlays mandatory, and then limits spending to actual revenues collected by the trust fund.

[7] Contract authority is a form of budget authority that permits obligations to be incurred in advance of liquidating appropriations.

Specifically, rather than skirting the two mechanisms intended to control spending, discretionary funding allocations and PAYGO, the Fiscal Commission's recommendation would establish surface transportation programs as subject to PAYGO.

The 2012 Budget reflects the recommendation of the Fiscal Commission. The 2012 Budget also includes a surface transportation reauthorization proposal that would broaden the scope of programs included under the Trust Fund umbrella: the HTF is renamed the Transportation Trust Fund (TTF), and supports additional highway safety and transit programs, as well as passenger rail programs and a new National Infrastructure Bank. The mechanics of how the 2012 Budget conforms to the Fiscal Commission recommendation are described in greater detail below. Generally speaking:

- Hybrid treatment is ended; all TTF accounts have mandatory contract authority and mandatory outlays.
- For the sake of comparability, the Budget reclassifies current law spending for all TTF activities as mandatory. This is intended to allow policy makers to: 1) transparently calculate the difference between baseline levels and the President's proposal, and 2) account for that difference under a unified, existing scorekeeping regime, PAYGO.
- Rescissions of contract authority in appropriations acts would be scored as CHIMPS (discretionary changes that would be rebased as mandatory subsequent to enactment, following long-standing scorekeeping conventions).

The Budget also assumes bipartisan agreement on new revenues sufficient to keep the Transportation Trust Fund solvent in every year, not only for the six-year reauthorization period (2012-2017) but for the ten-year Budget window. The estimates in the Budget fill projected Highway Trust Fund shortfalls that exist under current law and cover proposed spending with dedicated trust fund resources, thus requiring no transfers from the General Fund. These estimates are a placeholder and do not assume an increase in gas taxes or any specific proposal to offset surface transportation spending. Rather, they are intended to initiate a discussion about how the Administration and Congress could work together on a bipartisan basis to pass a surface transportation reauthorization that is both financially sustainable and meets critical national needs.

As proposed by the Administration, this unified scoring framework does not radically alter traditional roles and jurisdictional relationships as they are conceived of under current law and scorekeeping practice. Authorizing committees would be scored with the full cost of contract authority and outlays associated with their proposal; discretionary outlays would no longer be a central feature of the scorekeeping system. However, under the proposal, the Appropriations Committees would continue to set obligation limitations that would remain legally binding. In addition, the Appropriations Committees would liquidate contract authority. As under current law, multi-year authorizing bills would set initial expectations for spending. The new scorekeeping regime would recognize that fact by fully reflecting the cost of that legislation in terms of both budget authority and outlays.

While the Administration envisions both types of committees playing important roles, the central innovation of the proposed scorekeeping regime is that it would require all stakeholders to reconcile revenue and spending during the authorization process. That is the chief concern highlighted by the Fiscal Commission. By taking action to make all surface transportation programs subject to PAYGO, the Administration and the Congress would create a framework whereby any policy option must be fiscally sustainable. The Administration believes that current spending must be increased to keep the Nation competitive. We also recognize that a scorekeeping regime that closes loopholes in current practice and forecloses options that are not fiscally responsible is necessary for budget discipline and to drive policy makers towards consensus. Further delay in addressing our inadequate surface transportation infrastructure, and our inadequate system for financing that infrastructure, is not an acceptable outcome for the American people.

Note that this budget process is only one element of the Administration's comprehensive plan to rebuild the Nation's transportation infrastructure and put the financing of those expenditures on a more sustainable path. The *Budget* and *Appendix* discuss the broader policy in more detail.

Account-by-Account Budgetary Treatment.—As under current law, the Budget proposes the enactment of no-year contract authority for the Transportation Trust Fund for each year, 2012-2017, totaling $551 billion over six years. The contract authority is to be enacted by the reauthorization bill and, as under current law, will be classified as mandatory.

Under the budget, outlays flowing from that contract authority—which is already mandatory—will be treated as mandatory. The same treatment is applied to outlays flowing from prior obligations of the Highway Trust Fund, which will now be attributed to the Transportation Trust Fund. This is a departure from current law; as discussed earlier, this mandatory treatment of both contract authority and outlays follows the recommendation of the Fiscal Commission. As is the case for all other programs, this aligns outlays with budget authority, and by placing trust fund revenue and outlays on the PAYGO scorecard, it gives scoring effect to the linkage between dedicated re-

ceipts in a trust fund and the spending of those receipts for trust fund purposes.

For virtually all of the resources in the surface transportation reauthorization proposal, the Budget proposes that the reauthorization contain annual obligation limits at the same level as the contract authority, and also that annual appropriations bills include obligation limits at those levels. The obligation limits enacted by the appropriators enable the Administration and Congress to review TTF policies and resource levels on an annual basis, but under a framework that will continue to give external stakeholders a high level of certainty regarding the multi-year resource trajectory for highways, transit, passenger rail, and Infrastructure Bank activities.

The Budget modifies individual accounts to conform to the proposed budgetary treatment in all years. Specifically:

- For accounts that are presently classified as generating discretionary budget authority and outlays, but that the Administration proposes to incorporate into the TTF (for example the Federal Transit Administration's Capital Investment Grants account), the Budget includes separate schedules that:
  - Show baseline budget authority and outlays as discretionary, consistent with current classifications.
  - Reclassify baseline budget authority and outlays as mandatory in all years, including 2010 and 2011, for comparability purposes (i.e., to enable a comparison of funding levels across years in an account).
  - Show mandatory changes (subject to PAYGO) to the baseline level of budget authority and outlays that are requested in the Budget.
- For accounts that are presently funded from the HTF and that the Administration proposes to incorporate into the TTF (for example, Federal-Aid Highways), the Budget includes separate schedules that:
  - Show baseline levels of mandatory contract authority and discretionary outlays resulting from obligation limitations contained in appropriations acts. Since SAFETEA-LU is only currently extended through March 4, 2011, the contract authority is frozen in all years subsequent to that extension, consistent with current scorekeeping conventions.
  - Reclassify discretionary outlays from obligation limitations as mandatory outlays from mandatory contract authority for the 2011 estimate and create a new baseline of contract authority that is equal to the previous inflated discretionary baseline for obligation limitations.
  - Reclassify 2010 enacted budget authority and outlays as mandatory for comparability purposes (i.e., to enable a comparison of funding levels across years in an account).
  - Show proposed mandatory spending above or below the baseline as PAYGO costs or savings.
- For proposed new accounts supported by the TTF (for example, the Federal Railroad Administration's Network Development account), the Budget includes a schedule that includes new mandatory contract authority and outlays requested to support those programs.

Table 14–1. FUNDING, SPENDING, AND REVENUES ASSOCIATED WITH THE TRANSPORTATION TRUST FUND

(Dollars in billions)

	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	6-year	10-year
1. Funding for the Transportation Trust Fund (Contract Authority)	107	77	82	89	95	101	97	98	99	100	551	944
2. Estimated outlays	60	69	75	78	83	91	97	101	102	103	457	861
3. Baseline funding (Contract Authority and Budget Authority)	59	60	61	62	63	65	66	67	68	69	371	641
4. Estimated baseline outlays	53	50	59	60	61	64	67	69	70	71	348	624
5. Proposed funding increase	48	16	21	26	31	36	31	31	31	31	179	303
6. Estimated outlay increase	7	19	16	18	22	27	31	32	32	32	110	237
7. Dedicated revenues of the Transportation Trust Fund	64	76	80	82	85	87	90	92	94	97	475	848
8. Highway Trust Fund revenues (at current rates)	38	39	41	41	42	42	42	42	42	43	244	413
9. Placeholder revenue increase	26	37	39	41	43	45	48	50	52	54	231	435
10. Transportation Trust Fund annual cash flow	4	7	4	4	1	–4	–7	–8	–8	–7	17	–13
11. Transportation Trust Fund end-of-year balances	26	34	38	42	43	39	32	23	15	9		
Effect of proposal on overall budget:												
12. Estimated outlay increase (above)	7	19	16	18	22	27	31	32	32	32	110	237
13. Revenue increase, *net of assumed 25 percent offset*	20	28	29	31	32	34	36	38	39	41	174	328
14. Reduction in baseline deficits	13	9	13	13	10	7	5	6	7	9	64	91

Note: Amounts may not add due to rounding. This table includes $1.9 billion in BA and $1.5 billion in outlays in years 2013-2021 that were inadvertently omitted from account-level data in the Budget.

The discretionary accounts that are incorporated into the TTF construct are:

- Office of the Secretary, National Infrastructure Investments.
- Federal Railroad Administration (FRA): Operating Subsidy Grants to the National Railroad Passenger Corporation; Capital and Debt Service Grants to the National Railroad Passenger Corporation; Capital Assistance for High-Speed Rail Corridors.
- National Highway Traffic Safety Administration (NHTSA): Operations and Research.
- Federal Transit Administration (FTA): Administrative Expenses; Capital Investment Grants; Research and University Research Centers; Grants for Energy Efficiency and Greenhouse Gas Reductions.

Amounts in these accounts currently total $7.1 billion. Note that in a number of cases, activities captured in these accounts are requested under a new account in the Administration's reauthorization proposal. For example, activities under the two existing Amtrak accounts are requested as part of the Federal Railroad Administration's new System Preservation account. In those instances, the PAYGO impact of the Administration's reauthorization proposal must be calculated at the aggregate level rather than the individual account level (i.e., the change between the reclassified baseline amounts in the existing General Fund accounts and the proposed levels in the successor account).

Outyear Assumptions.—Beyond the reauthorization proposal, the Budget assumes that contract authority will increase at one percent per year after 2017, although the requested legislation will only extend through 2017. As an exception, funding for the National Infrastructure Bank is assumed to end after 2017; resources of the Infrastructure Bank are assumed to support activity beyond the six-year time frame of the reauthorization proposal, and their level can be revisited when appropriate.

Transportation Trust Fund Mechanics.—As discussed earlier, the Budget proposes a successor to the Highway Trust Fund, the Transportation Trust Fund, containing four accounts:

- The Highway Account subsumes the highway and highway safety activities currently in the Highway Trust Fund plus the NHTSA Operations and Research account, currently a General Fund account.
- The Mass Transit Account subsumes the transit activities currently in the Highway Trust Fund plus four FTA accounts currently financed by the General Fund: Capital Investment Grants; Research and University Research Centers; Grants for Energy Efficiency and Greenhouse Gas Reductions; and Administrative Expenses.
- The Rail Account focuses on developing high-speed rail and also subsumes activities currently financed from the General Fund: Capital Assistance for High-Speed Rail Corridors; Capital and Debt service grants to AMTRAK; and Operating Grants to AMTRAK.
- The final account covers the Infrastructure Bank (I-Bank) included in the Administration's reauthorization proposal.

The goal of a broader Trust Fund is to allow policy-makers to review surface transportation policy and spending in a more comprehensive way.

Financing.—The President is committed to working with Congress on a bipartisan basis to bring solvency to the Transportation Trust Fund and to ensure that funding increases for surface transportation do not increase the deficit. As a placeholder, the Budget assumes bipartisan agreement on new revenues sufficient to ensure the solvency of the Transportation Trust Fund through 2021. The placeholder does not make any specific assumptions about the composition of these new revenues, including whether they are composed of modifications to charges under current law, like the existing charges to motor fuels or truck tires, or new revenues. The Budget assumes that these revenues would be dedicated to the Transportation Trust Fund, as would all gross proceeds from existing excise taxes dedicated to the Highway Trust Fund and any unexpended balances of the Highway Trust Fund available at the beginning of 2012. In no year do the unexpended balances of the Transportation Trust Fund fall below $8 billion; these resources are estimated to cover all the Trust Fund's outlays through 2021 with a cushion of $8 billion or more in each year.

As a matter of policy, the Administration believes that the proceeds from existing Highway Trust Fund excise taxes should be dedicated solely to the highway and transit accounts; no existing excise taxes would be diverted to rail, I-Bank activities, or other activities. Rather, under the Administration's proposal, the new revenues would eliminate the projected shortfall in the Highway and Mass Transit accounts, cover increased funding for highways and mass transit, and finance passenger rail and Infrastructure Bank activities.

The Administration intends to work with Congress on a bipartisan basis to develop the specific revenues to be included in the reauthorization and the date on which they would become effective. The revenue stream displayed in the Budget is a placeholder that assumes that additional revenues become effective on January 1, 2012. This approach is intended to preclude the need for transfers from the General Fund to the Transportation Trust Fund. Note, however, that if the new revenues are not

effective until some year after 2012, transfers from the General Fund may still be necessary in 2012 and perhaps subsequent years. If that is the case, Administration policy is that the new revenues be sufficient to fully repay the General Fund by 2021 for any further transfers. A later effective date for the new revenues would therefore imply initially lower but ultimately higher annual revenues than shown in the Budget. Repaying the General Fund for any new transfers is also consistent with a budgetary treatment in which transfers from the General Fund to the Transportation Trust fund are treated as costs. Note that under Statutory PAYGO, such up-front costs are permissible if they are fully offset over the PAYGO window. Because the Administration's proposal does not require any future General Fund transfers, however, such a budgetary treatment of transfers is not a necessary component of the proposal.

Because some sources of revenue generate partially offsetting revenue reductions, the Budget makes the most conservative assumption, which is that a bipartisan agreement on financing produces new revenues that have the general characteristics of an excise tax, for which net proceeds are 75 percent of gross proceeds. This assumption is a conservative placeholder and is not intended to limit the choice of revenue type. The gross proceeds of the new revenues are to be deposited into the Transportation Trust Fund.

Explanation of the Administration's Proposal and PAYGO Treatment.—Table 14-1 details the Administration's surface transportation reauthorization proposal.

- Line one illustrates the proposed contract authority levels for accounts under the TTF, including accounts presently reflected as General Fund budget authority, HTF-funded accounts (hybrid treatment), and new activities. Note that the Administration proposes to front-load the reauthorization proposal to accelerate its economic impact. Line two illustrates outlay estimates associated with that contract authority, as well as prior-year outlays from the HTF.
- Line three illustrates the baseline level of budgetary resources for all activities proposed under the TTF. For comparability, those budgetary resources that were previously classified as discretionary are here displayed as mandatory. Line four illustrates the outlay estimates associated with those budgetary resources, including prior year outlays from the HTF.
- Lines five and six calculate the mandatory budget authority and outlay changes—the increases over the baseline levels. Line six is the amount that would be subject to PAYGO.
- Line seven indicates the assumed income of the Transportation Trust Fund available to liquidate outlays. That figure is made up of two components: estimates associated with current law receipts (line eight) to the Highway Trust Fund and the placeholder revenue stream needed to maintain Trust Fund solvency (line nine). Note that the placeholder revenue stream is not intended to match solvency needs year by year; rather, it is a smoothed estimate of revenue required to keep the TTF solvent over the ten-year window. The smoothed estimate, however, produces somewhat more than the minimum needed amount of revenues in the earlier years.
- Line ten illustrates the net cash flow to the TTF assumed in each year (revenues minus outlays).
- Line eleven illustrates the notional cash balances of the TTF over the ten-year period. As mentioned above, in each year the balances exceed the $8 billion minimally needed to ensure solvency.
- Lines twelve through fourteen illustrate the net impact of the proposal on the Budget.

In order to ensure the successful transition of these programs to a fiscally responsible framework, the Administration's proposal—or any proposal to make surface transportation programs subject to PAYGO—must consider two initial adjustments.

First, congressional scorekeeping must accommodate the initial shift from discretionary to mandatory outlays. As illustrated by line four, the activities that the administration proposes to incorporate in the TTF as mandatory outlays would generate discretionary outlays under current law totaling an estimated $348 billion over six years and $624 billion over ten years. If those outlays are reclassified, they should not be added to the PAYGO cost of any legislation by virtue of the fact that they are new to the mandatory side of the budget. Rather, the mandatory baseline should be adjusted to include those outlays that would occur under current law—as the 2012 Budget does—and calculate any changes from that baseline. Without this initial accommodation, the same archaic scorekeeping rules that frustrate budget discipline would prevent implementation of the Fiscal Commission's recommendation by overstating the cost of legislation intended to reform the hybrid system.

Second, to adhere to the Fiscal Commission's recommendation that the Transportation Trust Fund be fully financed by its own resources, additional revenue would be needed. Illustratively, over six years it would have to cover: 1) the difference between current law revenues and baseline HTF outlays ($66.2 billion) to restore solvency to the existing HTF, 2) any reclassification of baseline activities currently financed by the General Fund ($23.7 billion in the Administration's proposal), and 3) all program increases relative to the baseline ($109.7 billion, shown in Table 14-1). The Administration suggests that, for revenue increases that fill the gap between current law spending (under a BEA baseline) and current law revenue, that

Table 14–2. EFFECT OF STUDENT AID PROPOSALS ON DISCRETIONARY PELL FUNDING NEEDS
(Dollars in billions)

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	11-year
Current law (discretionary) before administrative actions	17.5	23.2	44.2	35.7	36.3	36.8	37.3	37.8	38.4	38.9	39.4	40.0	
IRS Verification (Administrative action)			–0.3	–0.3	–0.3	–0.4	–0.4	–0.4	–0.4	–0.4	–0.4	–0.4	–3.7
Current law (discretionary)	17.5	23.2	43.9	35.4	36.0	36.4	36.9	37.5	38.0	38.5	39.0	39.6	
Pell reforms (discretionary): end year-round Pell, reform FAFSA			–7.6	–4.3	–4.4	–4.5	–4.6	–4.7	–4.8	–4.9	–4.9	–5.0	–49.6
Proposed total discretionary funding before mandatory legislation	17.5	23.2	36.3	31.1	31.6	31.9	32.4	32.8	33.2	33.6	34.1	34.6	
Mandatory savings (non-add):													
Student loan acquisition/debt consolidation			–2.1										–2.1
Sudent loan subsidies			–1.0	–3.2	–3.0	–3.0	–3.0	–3.0	–3.1	–3.2	–3.3	–3.3	–29.3
Savings in mandatory Pell		–0.5	–0.6	–0.7	–0.8	–1.0	–1.1	–1.3	–1.3	–1.4	–1.4	–1.4	–11.4
Other mandatory savings			–0.4	–1.1	–0.7	–0.5	–0.3	–0.6	–0.6	–0.6	–0.6	–0.5	–5.7
Total mandatory savings (non-add)		–0.5	–4.0	–5.0	–4.5	–4.4	–4.4	–4.9	–5.0	–5.2	–5.3	–5.3	–48.6
Mandatory funding for discretionary Pell			–7.7	–2.8	–3.3	–3.7	–4.1	–4.5	–5.0	–5.4	–5.9	–6.4	–48.6
Total reduction in Pell discretionary funding			–15.6	–7.4	–8.0	–8.5	–9.0	–9.6	–10.1	–10.6	–11.2	–11.8	–101.8
Remaining needed discretionary funding	17.5	23.2	28.6	28.3	28.3	28.3	28.3	28.3	28.3	28.3	28.3	28.3	

Note: Amounts may not add due to rounding

increment of revenue not be recorded as a credit to the PAYGO scorecard. That "excess" revenue should be reserved for filling that gap, whereas under current PAYGO rules it could be used to offset other direct spending.[8]

Finally, the transportation initiative includes $5.350 billion of one-time, 2012 budget authority increases for TIGER grants and aviation, proposed as direct spending, that are not part of the TTF and so are not included in the table. These amounts are separate from the calculation of the amount of "excess revenue" that is kept off the PAYGO scorecard.

Pell Grants

The Pell Grant program includes features that make it unlike other discretionary programs. In recent years, the program's costs have risen significantly. This section provides some background on the unique nature of the Pell Grant program and explains how the Budget accommodates these rising discretionary costs. A later section of this chapter discusses the treatment of Pell in the adjusted baseline.

Under current law, the Pell program has several notable features:

- The costs of each Pell grant are funded with both mandatory budget authority provided by the College Cost Reduction and Access Act (CCRAA) as amended, and discretionary budget authority provided in annual appropriations acts. There is no programmatic difference between the mandatory and discretionary funding.
- The Pell program acts like an entitlement program, such as the Supplemental Nutrition Assistance Program or Supplemental Security Income, where the size of the individual award and the number of eligible applicants together determine the cost in any given year. Specifically, Pell Grant costs depend on the maximum award set in statute, the number of eligible applicants, and the award for which those applicants are eligible based on their needs and costs of attendance. The current maximum Pell award for an academic year is $5,550, of which $4,860 is established in appropriations acts and the remaining $690 is provided automatically by the CCRAA as amended.
- If valid applicants are more numerous than expected, or if these applicants are eligible for higher awards, the Pell program will cost more than the appropriations provided, and vice versa. If the costs during one academic year are higher than expected, the Department of Education funds the extra costs with the subsequent year's appropriation. The Department can do this because the annual appropriations act both sets the maximum Pell award and provides funding for the subsequent academic year. The 2012 appropriation, for instance, will support the 2012-2013 academic year beginning in July 2012.[9]
- To prevent deliberate underfunding of Pell costs, in 2006 the congressional and Executive Branch scorekeepers agreed to a special scorekeeping rule for

[8] As explained above, the new revenues used to fill the existing shortfall in the HTF constitute deficit reduction, as do the new revenues used to cover the baseline amount of programs that are currently general fund programs but would become part of the TTF and so need dedicated financing. These two sources of deficit reduction are described in the text. However, they are partially offset by the fact that gross revenues increases having the general characteristics of excise taxes – as the placeholder revenues in this Budget are assumed to have – produce net revenues for the Budget as a whole that are 25 percent smaller. This 25 percent offset also reduces the amount by which the notional revenue increase exceeds the estimated increase in outlays.

[9] This ability to "borrow" from a subsequent appropriation is unique to the Pell program. It comes about for two reasons. First, like many education programs, Pell is "forward-funded"—the budget authority enacted in the fall of one year is intended for the subsequent academic year, which begins in the following July. Second, even though the amount of funding is predicated on the expected cost of Pell during one academic year, the money is made legally available for the full 24-month period covering the current fiscal year and the subsequent fiscal year. This means that, if the funding for an academic year proves inadequate, the following year's appropriation will legally be available to cover the funding shortage for the first academic year. The 2012 appropriation, for instance, will support the 2012-2013 academic year beginning in July 2012 but will become available in October 2011 and can therefore help cover any shortages that may arise in funding for the 2011-2012 academic year.

Pell. Under this rule, the annual appropriations bill would be charged with the full estimated cost of the Pell program for the budget year, plus or minus any cumulative shortfalls or surpluses from prior years. This scorekeeping rule was adopted by Congress as §406(b) of the Concurrent Resolution on the Budget for Fiscal Year 2006 (H. Con. Res. 95, 109th Congress).

Given the nature of the program, it is reasonable to consider Pell Grants an individual entitlement for purposes of budget analysis and enforcement, and in the past two Budgets, the Administration requested that Pell Grants be converted into a mandatory program. Congress has chosen to continue treating the portion funded in annual appropriations acts as discretionary, counting that budget authority for Pell Grants against the appropriations allocations established annually under §302 of the Congressional Budget Act. This year the Budget maintains this treatment.

The total cost of Pell Grants can fluctuate from year to year, even with no change in the maximum Pell Grant award. One drawback of treating Pell Grants as discretionary is that aggregate targets for discretionary funding may be set with reference to some previous year's funding level without accounting for substantial fluctuations in Pell Grant funding. This problem has grown as the Pell program has grown. In this Budget, for example, the 2012 current-law funding level for the discretionary portion of Pell would be $44 billion—$21 billion higher than the 2011 level and almost $27 billion higher than the 2010 level.

This Budget reflects an Administration policy to maintain the current $5,550 maximum award. In order to fund the base of the program with discretionary appropriations, and in order to fit Pell funding within an aggregate budget authority target for 2012 that does not exceed the 2010 funding level, the Budget takes three basic steps, shown in Table 14-2. The Administration proposes to implement these steps as a package of changes to the Higher Education Act in the Pell Grant Protection Act.

- First, the Budget makes the Pell program less expensive through three policies:
  - Verifying income data between the Treasury and the Department of Education to reduce net overpayments, which can be done administratively and without the need for new legislation;
  - Immediately repealing the new year-round Pell program, which has cost much more than anticipated, beginning in the 2011-2012 school year; and
  - Simplifying the Free Application for Federal Student Aid (FAFSA).

These three policies are discussed at greater length in the *Appendix* to the 2012 President's Budget. Note especially that the repeal of year-round Pell will save money for the current year, 2011, and for the budget year, therefore requiring congressional action before July 1, 2011. Because Pell shortfalls are rolled forward, the 2011 savings will decrease the sizable shortfall otherwise rolled forward into 2012. This is shown in Table 14-2.

The administrative savings from income verification total $3.7 billion over ten years, and are built into the baseline shown above. The two legislative proposals together reduce the costs of the discretionary portion of Pell by another $49.6 billion in budget authority and reduce the costs of the mandatory portion of Pell by $11.4 billion in budget authority, both through 2021.

- Second, the Budget includes new student aid reforms that realize mandatory savings, which the Budget dedicates to Pell Grants. The additional reforms in mandatory education programs are discussed in the *Appendix* to the 2012 President's Budget. The total mandatory savings amount to a $48.6 billion, ten-year reduction in mandatory budget authority. That $48.6 billion in saved budget authority is then appropriated, as part of the authorizing reform legislation, toward paying for the discretionary portion of Pell. This is analogous to SAFRA's one-time $13.5 billion appropriation for discretionary Pell enacted last spring, which was financed by mandatory savings in student loan programs. This current proposal spreads the $48.6 billion in new funding over ten years in a way designed to make the needed amount of discretionary Pell constant in each year after 2012. The $300 million decrease in the discretionary appropriation between 2012 and 2013 means that the Budget can accommodate up to $3 billion over 10 years in additional needs, whether created by increased Pell costs or decreased mandatory savings, without requiring discretionary funding increases after 2012. This can be seen in the last three rows of Table 14-2.
- Finally, the Budget provides $28.6 billion in discretionary budget authority in 2012. This is $5.4 billion more than the $23.2 billion provided in 2011, but $15.3 billion less than the $44.2 billion that would be needed to maintain the current maximum award without the policies outlined above. Even with these policies, the growth in Pell has prompted difficult choices in other discretionary programs.

These important student aid reforms will address the growing costs of the Pell Grant program while still ensuring that aid is available to the neediest college students. However, even with these reforms, it remains likely that future Pell costs will vary significantly from current estimates. Cost increases could reflect the success of the Pell Grant program in helping more low-income students pay for college, and helping more workers return to school to upgrade their skills. While the Budget shows the Administration's commitment to controlling these costs and making the Federal student aid programs more ef-

ficient, it would be unwise for the budgetary treatment of Pell Grants to force continual cuts in need-based postsecondary education aid that would undermine the Nation's long-term success. For this reason, the Administration will work with Congress to consider other scorekeeping or enforcement approaches for the Pell Grant program.

Budgetary Treatment of the Postal Service Fund

The Administration proposes reform of the Postal Service, necessitated by the serious financial condition of the Postal Service fund. The policy proposals are discussed in the Postal Service and Office of Personnel Management sections of the *Appendix*.

As a matter of law, the Postal Service is designated as an off-budget federal agency. This designation and budgetary treatment was most recently mandated in 1989, in part to reflect the policy agreement that the Postal Service should pay for its own costs through its own revenues and should operate more like an independent business entity. The current deep recession and the ongoing evolution to paperless written communications have made this goal increasingly difficult to achieve. To address its current financial and structural challenges, the Administration proposes specific short-term financial relief measures and to work with Congress and stakeholders to secure necessary Postal Service reforms. The Administration also proposes that the PAYGO scoring of Postal legislation be done on a unified budget basis to better reflect how and when such legislation will affect overall deficits and debt. That is, for the purposes of entering amounts on the statutory PAYGO scorecards, the applicable estimates should include both the off-budget and the on-budget costs and savings produced by the legislation. This scorekeeping change would be accomplished by a directive contained within Postal reform legislation.

Expedited Rescission

Since taking office, the Administration has made a priority of identifying and cutting unnecessary spending, proposing approximately $20 billion of terminations, reductions, and savings in the last two Budgets, increasing to more than $30 billion in the 2012 Budget. While recent administrations have seen between 15 and 20 percent of their proposed discretionary cuts approved by Congress, this Administration succeeded in enacting 60 percent of proposed discretionary cuts for 2010.

While significant progress has been made on cutting unnecessary funding, more can be done. The Administration requests that Congress enact the President's proposal for expedited rescission, transmitted last May 24. That legislation would create an important tool for reducing such funding. In short, the bill would provide the President with additional authority to propose a package of rescissions that would then receive expedited consideration in Congress and a guaranteed up-or-down vote.

The proposal includes several components:

- *Scope.*—Under this new authority, the President can propose fast-track consideration of rescissions of discretionary and non-entitlement mandatory spending.[10] The President is limited to proposing changes that reduce funding levels and cannot use this authority to propose other changes in law, including new transfer authority, supplemental funding, or changes in authorizing legislation. The fast-track process is thus limited only to simple funding reductions, for which a straight up-or-down vote is desirable.
- *Proposing a rescission package.*—After enactment of funding, the President has 45 days during which Congress is in session (excluding weekends and national holidays) to decide whether to submit a rescission package using this expedited procedure. The President is also limited to a single package of rescissions per bill under this procedure, and the requested rescissions must be limited to provisions in that bill.[11]
- *Congressional procedure.*—A rescission package submitted under this authority receives fast-track consideration in Congress. Debate is limited in both houses and the package is guaranteed an up-or-down vote without amendment. The package is first introduced and considered in the House and, if approved there, is taken up in the Senate. From the package's introduction to its final vote in the Senate, the process will take no more than 25 days. Note that, while Congress cannot amend the package, the proposal enables Congress to omit from the bill any proposed rescission that it believes goes beyond the scope allowed.
- *Withholding funding.*—Following submission of a rescission request using this expedited procedure, the President may withhold funding for up to 25 days, after which the funding must be released. This ensures that agencies do not obligate funds before Congress has had an opportunity to consider the rescission package.

In sum, the proposal provides the President with important, but limited, powers that will allow the President and Congress to work together more effectively to eliminate unnecessary funding. Knowing this procedure exists may also discourage policymakers from enacting such funding in the first place.

[10] In almost every case, "non-entitlement mandatory funding" exists where an agency has the authority to spend the proceeds of fees or other offsetting collections to run the agency. The spending in question is generally indistinguishable from other funding for administering the government that is typically provided through discretionary appropriations.

[11] There is one exception to the packaging rule: when a single appropriations bill includes funding that is in the jurisdiction of more than one appropriations subcommittee such as in an omnibus appropriations bill. In that case, the President may submit up to two packages.

The proposal is crafted to preserve the constitutional balance of power between the President and Congress. In 1996, Congress granted the President "line item veto" power over certain spending and tax bills, allowing the President to use his veto authority to strip out select provisions of legislation while signing the rest into law. The Supreme Court found this to violate the Constitutional procedure for presenting a bill to the President for approval or veto of the entire bill. The Administration's proposal is, however, fundamentally different. Under the proposal, Congress, which is empowered to set its own rules, changes those rules under which it considers rescission packages proposed by the President—using well-established fast-track procedures. Most importantly, rescissions only occur if Congress affirmatively enacts them into law. In other words, the proposal does not expand the Presidential veto authority in any way.

The proposal also preserves the President's two existing authorities for proposing rescissions. First, the President retains the Constitutional authority to recommend legislation such as cancellation packages to be considered under regular order in Congress. Second, the President retains the power to recommend rescissions under the procedure already established under the Impoundment Control Act of 1974. This existing authority provides more limited fast-track protections to a Presidential rescission package than what the Administration has proposed and, specifically, allows committee and floor amendments and so does not guarantee a clean up-or-down vote on a package submitted by the President.

The proposal lifts procedural barriers; however, the President and Congress will still have to make the difficult choices to cut back unnecessary funding. Furthermore, restoring fiscal sustainability in the medium and long term will require not only targeting unnecessary funding in specific programs, which the proposal aids, but also making larger choices about overall budget priorities and revenue levels.

Program Integrity Funding

With hundreds of billions of dollars being spent in programs such as Social Security, Medicare, and Medicaid, upon which so many Americans rely, it is important that they are run efficiently and effectively. Most notably, the Government made an estimated $125 billion in improper payments last year over all its programs. Although this amount actually reflects a decline in the payment error rate, this level of error and waste in Government programs is unaffordable, nor should such a figure be acceptable regardless of the size of the deficit. The Administration, therefore, will make significant investments in activities to ensure that taxpayer dollars be spent correctly, expanding oversight activities in the largest benefit programs and increasing investments in tax compliance and enforcement activities. In addition, the Administration supports a number of legislative and administrative reforms on improper payments and debt collection. Many of these proposals will provide savings for the Government and taxpayers, and will support government-wide efforts to improve the management and oversight of Federal resources. If all of the legislative program integrity proposals are enacted, they are estimated to save at least $162.7 billion over 10 years.

The Administration supports initiatives to ensure that Federal agencies are responsible stewards of taxpayer resources, and will work with Congress to that end. Specifically, the Administration is focused on the reduction of improper payments while continuing to ensure access to important benefit programs. The Administration supports efforts to provide Federal agencies with the necessary resources and incentives to prevent, reduce, or recover improper payments, including fraudulent payments. With the enactment of the Improper Payments Elimination and Recovery Act of 2010 (Public Law 111-204), and the release of three Presidential directives on improper payments, agencies are well positioned to utilize these new tools and techniques to prevent, reduce, and recover improper payments, and the Administration will continue to identify areas where it can work with Congress to further improve agency efforts.

Discretionary Program Integrity Initiatives.—The Administration proposes significant increases in discretionary administrative program integrity activities at the Social Security Administration (SSA), the Department of Health and Human Services (HHS), the Department of Labor (DOL), and the Internal Revenue Service (IRS). The Administration proposes a multi-year strategy, which will permit the agencies to pay closer attention to the risk of improper payments, commensurate with the large and growing costs of the programs administered by these agencies, including Social Security, Medicare, Medicaid, and Unemployment Insurance (UI).

There is solid and rigorously evaluated evidence that these investments in administrative resources can significantly decrease the rate of improper payments and recoup many times their initial investment. For every $1 spent by SSA on a disability review, $10 is saved in erroneous payments. Similarly, for every additional $1 spent by HHS on program integrity efforts, approximately $1.50 is saved or averted, and the IRS enforcement activities recoup roughly $6 or $7 for every $1 spent. As shown in Table 14-3, the initial five-year investment of $18.9 billion for 2012 through 2016, if sustained in real terms thereafter, is estimated to result in more than $125 billion in lower spending and additional tax revenue over the next 10 years, with further savings after the 10-year period.

The Administration proposes to protect the dollars requested for these activities in the appropriations process through allocation adjustments, a mechanism that has been used by administrations and Congresses over the

Table 14–3. MANDATORY AND RECEIPT SAVINGS FROM DISCRETIONARY PROGRAM INTEGRITY BASE FUNDING AND ALLOCATION ADJUSTMENTS

(Budget authority in millions of dollars)

	2012–2016 Allocation Adjustments	Savings Achieved from Allocation Adjustments and Inflation Thereafter										10-Year Total
		2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	
SSA Program Integrity [1]												
Enforcement Base	1,701	620	–86	–655	–1,069	–1,566	–1,886	–2,134	–2,625	–2,997	–3,358	–15,756
Allocation Adjustment	4,587	–379	–2,280	–3,549	–4,496	–5,651	–6,392	–7,034	–8,076	–8,865	–9,646	–56,368
IRS Tax Enforcement [2]												
Enforcement Base [3]	38,814	–50,000	–50,000	–50,000	–50,000	–50,000	–50,000	–50,000	–50,000	–50,000	–50,000	–500,000
Allocation Adjustment [4]	10,729	–276	–804	–1,970	–3,721	–5,646	–7,227	–8,184	–8,773	–9,274	–9,778	–55,653
Health Care Fraud and Abuse Control Program												
Allocation Adjustment [5]	3,208	–750	–890	–930	–990	–1,040	–1,070	–1,100	–1,130	–1,170	–1,200	–10,270
Unemployment Insurance Improper Payments [6]												
Enforcement Base	54	–35	–37	–39	–41	–41	–43	–45	–49	–49	–53	–432
Allocation Adjustment	350	–92	–213	–235	–258	–283	–301	–314	–326	–338	–352	–2,712

[1] This is based on SSA's Office of the Actuary estimates of savings. In the first year, the enforcement base shows a positive outlay. This is due to the fact that redeterminations of eligibility can uncover underpayment errors as well as overpayment errors. SSI recipients are more likely to initiate a redetermination if they believe there is an underpayment, and SSA completes these beneficiary-initiated redeterminations in the enforcement base. In addition, corrections for underpayments are realized more quickly than corrections for overpayment. The allocation adjustment does not show an outlay in the first year because SSA would target their allocation adjustment redetermination dollars to cases where an overpayment is suspected.

[2] Savings for IRS are revenue increases rather than spending reductions. They are shown as negatives for consistency in presentation.

[3] No official estimate for FY 2012 enforcement revenue has been produced at the time of publishing, so this figure is an approximation and included only for illustrative purposes.

[4] The Internal Revenue Service (IRS) allocation adjustment funds cost increases for existing enforcement initiatives and activities and new initiatives. The IRS enforcement program helps maintain the more than $2 trillion in taxes voluntarily paid each year. The cost increases will help maintain the base revenue while generating additional revenue through targeted program investments. The activities and new initiatives funded out of the allocation adjustment will yield almost $56 billion over 10 years. Aside from direct enforcement revenue, the deterrence impact of these activities suggests the potential for even greater savings.

[5] These savings are based on estimates from the HHS Office of the Actuary for return on investment (ROI) from program integrity activities. The ROI is based on the discretionary allocation amount less the administrative costs for implementing the legislative program integrity proposals included in the Budget.

[6] The maximum UI benefit period is typically 26 weeks. As a result, preventing an ineligible individual from collecting UI benefits would save at most a half year of benefits.The two years of savings reflect the fact that reemployment and eligibility assessments conducted late in the year affect individuals whose benefits would have continued into the subsequent fiscal year.

past two decades. Allocation adjustments are increases in the congressional allocation for annual appropriations, with these increases granted only if appropriations bills increase funding for the specified program integrity purposes above specified base levels. This budget mechanism will ensure that this funding will not supplant other Federal spending on these activities or be diverted to other purposes. The base level of funding assumed in each appropriations request and the allocation adjustment for each agency is listed in Table 14-4. The Administration's proposal assumes baseline inflation increases for the base level of funding for all ten years of the budget window and assumes funding for five years of allocation adjustments, with inflation adjustments for that funding after the fifth year.

For the Social Security Administration, the $623 million allocation adjustment (and base funding of $315 million) will allow SSA to conduct at least 592,000 Continuing Disability Reviews (CDRs) and at least 2.6 million Supplemental Security Income (SSI) redeterminations of eligibility in 2012. CDRs determine whether an individual continues to qualify for Disability Insurance or Supplemental Security Income. The funding provided for the Social Security Administration will enable the agency to work down a backlog of CDRs. As a result of increased funding provided by the allocation adjustment, SSA would recoup almost $56.4 billion in savings in the Disability Insurance and Supplemental Security Income programs, with additional savings after the ten-year period, according to estimates of SSA's Office of the Actuary.

SSA is required by law to conduct CDRs for all beneficiaries who are receiving Disability Insurance benefits, as well as all children under age 18 who are receiving Supplemental Security Income. SSI redeterminations are also required by law, but the frequency is not specified in statute. The baseline assumes the likely frequency of program integrity activities, given the baseline funding levels. The President's Budget shows the savings that would result from the increase in CDRs and redeterminations made possible by the program integrity allocation adjustment.

As stated above, the return on investment (ROI) for CDRs is approximately 10 to 1 in lifetime program savings. The ROI for redeterminations is approximately 7 to 1. The savings from one year of program integrity activities are realized over multiple years because some CDRs identify that beneficiaries have medically improved and are capable of working, which may mean that they

Table 14–4. DISCRETIONARY PROGRAM INTEGRITY BASE FUNDING AND ALLOCATION ADJUSTMENTS
(Budget authority in millions of dollars)

	2010 Actual	2011 CR	2012 Proposed	2013 Proposed	2014 Proposed	2015 Proposed	2016 Proposed
SSA Program Integrity:							
Enforcement Base[1]	273	273	315	327	340	353	366
Allocation Adjustments:							
BA	485	485	623	751	924	1,123	1,166
Outlays	485	485	623	751	924	1,123	1,166
IRS Tax Enforcement:							
Enforcement Base:	7,100	7,100	7,233	7,663	7,815	7,972	8,131
Enforcement Account	4,904	4,904	5,031	5,132	5,234	5,339	5,446
Operations Support Account	2,196	2,196	2,202	2,531	2,581	2,633	2,685
Allocation Adjustments:							
BA	890	890	1,257	1,674	2,105	2,568	3,125
Outlays	850	890	1,347	1,632	2,062	2,522	3,069
Health Care Fraud and Abuse Control Program:							
Enforcement Base (Mandatory)	1,173	1,398	1,272	1,267	1,291	1,306	1,331
Allocation Adjustments:							
BA	311	311	581	610	640	672	706
Outlays	311	311	581	610	640	672	706
Unemployment Insurance Improper Payments:							
Enforcement Base	10	10	10	11	11	11	11
Allocation Adjustments:							
BA	50	50	60	65	70	75	80
Outlays	49	50	59	64	69	74	79
Partnership Fund for Program Integrity Innovation:							
Allocation Adjustments:							
BA	38	38	20				
Outlays	1	20	26	10	1		
TOTAL:							
Enforcement Base	8,556	8,781	8,830	9,268	9,457	9,642	9,839
Allocation Adjustments:							
BA	1,774	1,774	2,541	3,100	3,739	4,438	5,077
Outlays	1,696	1,756	2,635	3,067	3,696	4,391	5,020

[1] For 2010 through 2016, numbers reflect spending on CDRs and SSI redeterminations. Limited funding in the 2010 allocation adjustment may also be available for asset verification processes, provided the activity is as cost-effective as SSI redeterminations.

are no longer eligible to receive Disability Insurance (DI) or Supplemental Security Income (SSI) benefits. Redeterminations focus on an individual's eligibility for the means-tested SSI program and generally result in a revision of the individual's benefit level. However, the schedule of savings resulting from redeterminations will be different for the base funding and the allocation adjustment. This is because redeterminations of eligibility can uncover underpayment errors as well as overpayment errors. SSI recipients are more likely to initiate a redetermination of eligibility if they believe there are underpayments, and these recipient-initiated redeterminations are included in the base.

For the IRS, the $1,257 million allocation adjustment covers cost increases for the base IRS tax enforcement program plus new and continuing investments in expanding and improving the effectiveness and efficiency of the IRS' overall tax enforcement program. As a result, the IRS will collect an estimated $50 to $60 billion in 2012 in direct enforcement revenue. The IRS estimates that the proposed new 2012 enforcement initiatives will yield an additional $650 million in revenue in 2012. Further, once the initiatives' new staff are trained and become fully operational in 2014, the extra revenue brought in each year will rise to at least $1.3 billion, or roughly $6 in additional revenue for every $1 in IRS expenses. Moreover, this ROI estimate is likely understated because a portion of the new investment is directed towards efforts to improve the performance of existing staff and resources (such as new computers and better research) which are not reflected in the IRS' ROI calculation. More importantly, the ROI is understated because it only includes amounts received; it does not reflect the effect enhanced enforcement has on deterring non-compliance. This indirect deterrence effect

Table 14–5. MANDATORY AND RECEIPT SAVINGS FROM OTHER PROGRAM INTEGRITY INITIATIVES
(Receipts and outlays in millions of dollars)

	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	10-year total
Department of Health and Human Services:											
Expand CMS Program Integrity Authority [1]	–655	–885	–1,155	–2,805	–3,560	–4,310	–4,475	–4,670	–4,815	–5,005	–32,335
Department of Labor:											
Implement Unemployment Insurance Integrity Legislation:											
Outlay impact:											
PAYGO	....	–4	18	22	26	28	29	28	26	27	200
Non-PAYGO	....	–84	–171	–174	–176	–182	–189	–197	–205	–213	–1,591
Receipt impact:											
PAYGO [2]	....	–20	–40	–40	–40	–41	–43	–45	–47	–49	–365
Non-PAYGO [2]	....	–34	–68	–30	628	–121	398	433	89	–95	1,200
Department of the Treasury:											
Increase levy authority for payments to Medicare providers with delinquent tax debt (receipt effect)	–64	–68	–71	–74	–76	–76	–78	–80	–80	–81	–748
Increase levy authority for vendor payments to Federal contractors with delinquent tax debt (receipt effect)	–59	–61	–64	–67	–69	–73	–76	–80	–83	–87	–719
Social Security Administration:											
Windfall Elimination Provision/Government Pension Offset Enforcement Provision (non-PAYGO)	13	20	18	–202	–439	–574	–609	–555	–522	–479	–3,329
Total, Mandatory and Receipt Savings	**–765**	**–1,136**	**–1,533**	**–3,370**	**–3,706**	**–5,349**	**–5,043**	**–5,166**	**–5,637**	**–5,982**	**–37,687**
PAYGO Savings	–778	–1,038	–1,312	–2,964	–3,719	–4,472	–4,643	–4,847	–4,999	–5,195	–33,967
Non-PAYGO Savings	13	–98	–221	–406	13	–877	–400	–319	–638	–787	–3,720

[1] Savings estimates may not include all interactions.
[2] Net of income offsets.

helps to ensure the continued payment of well over $2 trillion in taxes voluntarily paid each year. Though this indirect effect is not explicitly measured, research suggests it is at least three times as large as the direct effect on revenue, and possibly much greater.

The discretionary allocation adjustment of $581 million for Health Care Fraud and Abuse Control (HCFAC) activities is designed to support efforts to reduce the Medicare improper payment rate by 50 percent, expand the Health Care Fraud Prevention & Enforcement Action Team (HEAT) initiative, and provide resources to implement a robust set of legislative program integrity proposals. The increased funding will also allow the Centers for Medicare and Medicaid Services (CMS) to deploy innovative efforts that focus on improving the analysis and application of data, including state-of-the-art predictive modeling capabilities, in order to prevent potentially wasteful, abusive, or fraudulent payments before they occur. The funding is to be allocated among CMS, the Health and Human Services Office of Inspector General, the Federal Bureau of Investigation, and Department of Justice. This $581 million will generate approximately $750 million in savings in 2012, which reflect both prevention and recoupment of improper payments made to providers, as well as recoveries related to civil and criminal penalties.

The 2012 Budget proposes an allocation adjustment of $60 million for the Department of Labor's (DOL) Unemployment Insurance (UI) State administrative grants program to reduce UI improper payments, a top management challenge identified by GAO and DOL's Inspector General. The proposal would expand a $10 million Reemployment and Eligibility Assessment initiative, begun in 2005 to finance in-person interviews at One-Stop Career Centers, to assess UI beneficiaries' need for job finding services and their continued eligibility for benefits. The current $10 million effort results in a savings in UI benefit payments of an estimated $35 million. The request for additional funding for in-person reemployment and eligibility assessments of claimants of unemployment compensation builds upon the success of a number of States in reducing improper payments and speeding reemployment by using these assessments. Because most unemployment claims are now filed by telephone or online, in-person assessments conducted in the One-Stop Career Centers can help determine the continued eligibility for benefits and the adequacy of work search, verify the identity of beneficiaries where there is suspicion of possible identity theft, and provide a referral to reemployment assistance for those who need additional help. The maximum UI benefit period is typically 26 weeks, although it is currently longer in response to the elevated unemployment rate. As a result, preventing an ineligible individual from collecting UI benefits would generally save at most a half year of benefits. The two years of savings from the additional $60 million, totaling $202 million, reflect the fact that reemployment and eligibility assessments conducted

late in the year affect individuals whose benefits would have continued into the subsequent fiscal year.

In addition to the initiatives described above, the 2012 Budget includes $20 million to continue piloting the pipeline of innovations generated through the Partnership Fund for Program Integrity Innovation (Partnership Fund) to improve service delivery, payment accuracy, and administrative efficiency across Federal assistance programs administered by States—while protecting qualified beneficiaries. The Partnership Fund allows Federal, State, and local agencies to pilot and evaluate new ideas that break down the silos among programs and levels of government, boosting efficiency and preventing improper payments. The results of these pilots will be a positive return on investment for taxpayers. In addition, the Partnership Fund allows for pilot projects that simulate the effects of more efficient, accurate methods of service delivery that might require changes to existing regulatory or statutory authorities. These simulations can inform both the Administration and the Congress about whether changes in authority may be warranted. As pilots are selected, funding is transferred to the applicable Federal agencies to administer the pilots in conjunction with States or localities. For example, a recently funded pilot simulation to reduce error in the Earned Income Tax Credit (EITC) program, if successful, offers potential annual savings of up to $100 million or more for a pilot investment of $2 million. This pilot, managed by the Department of the Treasury, will identify both current and new authorities required to take the pilot to scale. By law, Partnership Fund pilots must save at least as much as they cost, in aggregate. Based on projections in early pilots and pilots under development, the Partnership Fund will be able to use the additional funding of $20 million to prioritize new projects that, like the EITC pilot, promise a significant return on investment. The 2010 Consolidated Appropriations Act (P.L. 111-117) included $37.5 million authorized through 2012 for the Partnership Fund.

Mandatory Program Integrity Initiatives.—Table 14-5 lays out the mandatory and receipt savings from other program integrity initiatives that are included in the 2012 Budget, beyond the expansion in resources resulting from the increases in discretionary funding discussed above. These savings total more than $37.7 billion over ten years. More than 90 percent of these savings would be scored as PAYGO offsets because the legislation would authorize agencies to use new methods to crack down on overpayments and combat fraud. These mandatory proposals to reduce improper payments and ensure agencies recover debt owed to the Federal Government reflect the importance of these issues to the Administration. Through these and other initiatives outlined in the Budget, the Administration can improve management efforts across the Federal Government.

Expand CMS Program Integrity Authority.—The 2012 Budget includes new Medicare and Medicaid program integrity proposals to help prevent fraud and abuse before they occur; detect fraud and abuse as early as possible; more comprehensively enforce penalties and other sanctions when fraud and abuse occur; provide greater flexibility to the Secretary of Health and Human Services to implement program integrity activities that allow for efficient use of resources and achieve high returns-on-investment; and promote integrity in Federal-State financing. Examples for the Medicare program include a proposal to require enhanced recoupment of overpayments made to Medicare Advantage plans based on sample error rates, and a proposal to create a Medicare claims ordering system that would validate physician and practitioner orders before payments are made for certain high-risk services. In Medicaid, the Budget proposes limiting State financing practices that increase Federal Medicaid spending, as recommended by the National Commission on Fiscal Responsibility and Reform, and requiring States to monitor prescription drug patterns that could indicate fraud or abuse. Together, the CMS program integrity proposals are projected to save more than $32 billion over 10 years.

Unemployment Insurance Integrity Legislation—Since 2006, the President's Budget has included a multi-part proposal to give States additional tools and resources to recover and prevent UI improper payments. The current proposal would:

- Strengthen States' incentives to recover UI benefit overpayments and employer contributions by permitting States to use a portion of recovered funds for the reduction of fraud and errors and detection of nonpayment of required contributions;
- Impose a penalty for UI fraud;
- Charge employers when their actions lead to overpayments; and
- Require employers to provide information to the National Directory of New Hires on laid-off workers who have been rehired.

The combined revenue loss and the outlay savings associated with this proposal would reduce the deficit by $556 million over 10 years. Of the nearly $1.4 billion outlay impact, $200 million would be PAYGO savings. The net revenue reduction of $835 million represents $1.2 billion in non-PAYGO revenue losses as increased recoveries of improper payments permit States to reduce their UI taxes and $365 million in PAYGO savings from penalty collections by the States.

Improve Treasury Debt Collection by Increasing Levy Authority.—The 2012 Budget includes two proposals to increase receipts from debt collection activities:

- *Increase levy authority for payments to Medicare providers with delinquent tax debt.*—The Budget

proposes a change to the Department of the Treasury's debt collection procedures that will increase the amount of delinquent taxes collected from Medicare providers. Through the Federal Payment Levy Program, Treasury deducts (levies) a portion of a Government payment to an individual or business in order to collect unpaid taxes. Pursuant to the Medicare Improvements for Patients and Providers Act of 2008, Medicare provider and supplier payments are included in the Federal Payment Levy Program, whereby Treasury is authorized to continuously levy up to 15 percent of a payment to a Medicare provider in order to collect delinquent tax debt. The Budget proposal will allow Treasury to levy up to 100 percent of a payment to a Medicare provider to collect unpaid taxes. This proposal would result in PAYGO savings of $748 million over ten years.

- *Increase levy authority for payments to Federal contractors with delinquent tax debt*.—The Budget proposes a change to the Department of the Treasury's debt collection procedures that will increase the amount of delinquent taxes collected from Federal contractors. Through the Federal Payment Levy Program, the Treasury deducts (levies) a portion of a Government payment to an individual or business in order to collect unpaid taxes. Pursuant to the American Jobs Creation Act of 2004, Treasury is authorized to continuously levy up to 100 percent of payments to a Federal vendor for goods or services sold or leased to the Federal government if the vendor has an unpaid tax liability. However, the language contains a technical imperfection that has the unintended effect of limiting the levy to 15 percent for vendor payments made for the sale or lease of real estate or other types of property. The Budget proposal will allow Treasury to levy up to 100 percent of any payment due to a Federal vendor with unpaid tax liabilities. This proposal would result in PAYGO savings of $719 million over ten years.

Social Security Windfall Elimination Provision/ Government Pension Offset Enforcement Provision.—The Budget re-proposes legislation that would improve reporting for non-covered pensions by including up to $50 million for administrative expenses to develop a mechanism so that the Social Security Administration could enforce the offsets for non-covered employment, Windfall Elimination Provision (WEP), and Government Pension Offset (GPO). The proposal would require State and local governments to provide information on their non-covered pension payments to SSA so that the agency can apply the WEP and GPO adjustments. Under current law, the WEP and GPO adjustments are dependent on self-reported pension data and cannot be independently verified. This proposal would result in savings in the Old-Age, Survivors, and Disability Insurance program of almost $3.4 billion over 10 years, which would be scored as non-PAYGO because the program is off-budget.

Other Program Integrity Initiatives.*—Executive Order (EO) on Reducing Improper Payments.*—Executive Order 13520 on Reducing Improper Payments and Eliminating Waste in Federal Programs intensifies agency efforts to eliminate errors (including waste, fraud, and abuse) in the major programs (i.e., those programs with the highest dollar value or majority of improper payments) administered by the Federal Government. There are three overarching Executive Order requirements:

1. Increase transparency and public participation;

2. Intensify agency accountability and coordination; and

3. Use incentives to improve contractor and state and local efforts in eliminating payment errors.

The provisions of the Executive Order align with the President's program integrity initiatives by (1) ensuring that performance measures exist to assess (either annually or more frequently) whether these actions are reducing errors; (2) requiring agencies to submit a remediation plan when reduction targets for those programs with the high dollar value of improper payments are missed two consecutive years; and (3) initiating studies to recommend incentives for reducing error. Agencies are continuing to make progress in implementing EO 13520, and agency results can be found on the Federal Government's improper payments dashboard at http://www.paymentaccuracy.gov/.

"Do Not Pay" List and Fraud Detection Technology.—The Budget requests $10 million for the Department of the Treasury to support expansion of the "Do Not Pay" list—created by a Presidential memorandum issued June 18, 2010—and to add forensic fraud detection capabilities to the basic "Do Not Pay" portal. Specifically, the funding will help procure the detection technology and hire staff to support an operations center to analyze fraud patterns and refer potential issues to agency management and the relevant Inspector General. This operations center will link public and private-sector information, and enable trained analysts to review the results and help identify and prevent fraud and improper payments. In addition, funding will also help expand the number of databases linked to the "Do Not Pay" list and support the underlying platform. It is expected that supporting the operations center and the "Do Not Pay" list will have a significant return on investment and will help reduce the amount of improper payments that agencies annually report.

Expanding Data Matching Authority to Reduce Improper Payments.—Based on Federal agencies' 2010 improper payment reporting, approximately 35 percent (or $40 billion) of all payment errors were due to the inability to verify applicant information such as earnings,

income, assets, or work status. This type of information is frequently available in data sources maintained by Federal agencies and third parties, but access to these sources is often limited due to legal, regulatory, or cost impediments. Recognizing the importance of data matching in reducing improper payments, Executive Order 13520 emphasized exploring solutions to improve data sharing between agencies. In addition, in June 2010, the President issued a memorandum that directed that a single portal, the “Do Not Pay” portal referred to above, be established through which agencies could check multiple eligibility databases before making an award or payment. In November 2010, OMB released a memorandum that encouraged agencies to share high-value data between agencies that can be used to support important Administration initiatives, including preventing improper payments. The Administration is continuing to pursue opportunities to improve information sharing by developing or enhancing policy and guidance and developing legislative proposals to leverage available information in determining benefit eligibility.

Social Security Workers' Compensation Enforcement Provision.—The Budget has a new proposal to improve the collection of data on the receipt of Workers' Compensation benefits. Similar to WEP/GPO (see description in the mandatory program integrity initiatives section above), this information is self-reported to SSA and is used to offset benefit amounts in the Social Security Disability Insurance and Supplemental Security Income programs. This proposal would develop a process to collect this information in a timely manner from States and private insurers to correctly offset Disability Insurance benefits and reduce SSI payments. The proposal includes $10 million to help fund States' systems implementation costs, with a savings estimate still under development.

Other Program Integrity Proposals.—The Budget also supports Treasury's legislative debt collection proposals highlighted earlier by including several administrative debt collection reforms that could help improve the Federal Government's collection of debts from individuals and businesses that are owed to Federal agencies. In addition, the Budget recognizes Administration efforts to improve program integrity by highlighting several administrative actions that could prevent and reduce agency improper payments if implemented. The administrative proposals would help reduce improper payments in programs like the Department of Education's Pell Grants program and the Department of Health and Human Services' Low Income Home Energy Assistance Program.

For more information on the specific program integrity funding proposals described in this section, see the *Terminations, Reductions, and Savings* volume.

Disaster Relief Fund

The Administration requests discretionary budget authority of $1.8 billion for FEMA in 2012 to provide Federal assistance in response to presidentially declared major disasters and emergencies. The Budget uses the five-year historical obligations for non-catastrophic events (those less than $500 million in estimated obligations) minus the estimated annual recoveries to calculate this level. The rationale for this methodology is that large or catastrophic events are rare and would likely involve a supplemental or emergency appropriation. As a result of this assumption, obligations in response to large or catastrophic events are not included in the level of disaster relief. The Administration seeks to protect the Disaster Relief Fund (DRF) and prevent redirection of these funds for non-disaster purposes by proposing that the full DRF request be allocated to the Appropriations Committees in a separate category, available only for the specified purposes. Specifically, the Administration requests that the Budget Committees include in the 2012 budget resolution a provision that allows for an adjustment to their 302(a) allocations for the full DRF request. The terms of this adjustment would stipulate that the 302(a) allocations would not be increased unless the Appropriations bill provided for full funding for the DRF and the language included a provision preventing transfers.

Limit on Discretionary Advance Appropriations

An advance appropriation first becomes available for obligation one or more fiscal years beyond the year for which the appropriations act is passed. Budget authority is recorded in the year the funds become available for obligation, not in the year the appropriation is enacted.

There are legitimate policy reasons to use advance appropriations to fund programs. For example, funding for the Corporation for Public Broadcasting is customarily appropriated two years in advance. This gives the beneficiaries of this funding time to plan their broadcasting budgets before the broadcast season starts.

However, advance appropriations can also be used in situations that lack a programmatic justification, as a gimmick to make room for expanded funding within the funding allocations set under a congressional budget resolution. For example, some education grants are forward funded (available beginning July 1 of the fiscal year) to provide certainty of funding for an entire school year, since school years straddle Federal fiscal years. This funding is recorded in the budget year because the funding is first legally available in that fiscal year. However, more than $21.9 billion of this funding is advance appropriated (available beginning three months later, on October 1) rather than forward funded. Prior Congresses increased advance appropriations and decreased the amounts of forward funding as a gimmick to free up room in the bud-

get year without affecting the total amount available for a coming school year. This gimmick works because the advance appropriation is not recorded in the budget year but rather the following fiscal year. But it works only in the year in which funds are switched from forward funding to advance appropriations; that is, it works only in years in which the amounts of advance appropriations for such "straddle" programs are increased.

To curtail this gimmick, which allows over-budget funding in the budget year and exerts pressure for increased funding in future years, congressional budget resolutions since the 2001 resolution have set limits on the amount of advance appropriations. When the congressional limit equals the amount that had been advance appropriated in the most recent appropriations bill, there is no additional room to switch forward funding to advance appropriations, and so no room for this particular gimmick to operate in that year's budget.

The 2012 Budget includes $28,821 million in advance appropriations for 2013 and freezes them at this level in subsequent years. In this way, the Budget does not employ this potential gimmick. Moreover, the Administration supports limiting advance appropriations to the proposed level through the congressional budget resolution for 2012, similar to the limits included as section 402 and 424 of S. Con. Res. 13, the concurrent resolution on the budget for 2010. Those limits applied only to the accounts explicitly specified in the joint explanatory statement of managers accompanying the budget resolution.

In order to account for the Administration's Elementary and Secondary Education Act reauthorization proposal, the 2012 Budget eliminates the $1,681 million advance appropriation that was previously in the School Improvement account (renamed the Education Improvement account) and replaces it with corresponding increases to advance appropriations in the accounts for Education for the Disadvantaged ($840 million, renamed Accelerating Achievement and Ensuring Equity) and Special Education ($841 million). Total advance appropriations in the Department of Education remain unchanged at $21,905 million.

In addition, the Administration would allow advance appropriations for the Corporation for Public Broadcasting, which is typically enacted two years in advance, and for Veterans Medical Care, as is now required by the Veterans Health Care Budget Reform and Transparency Act (P.L. 111-81). The advance appropriations funding level for the veterans medical care accounts (comprising Medical Services, Medical Support and Compliance, and Medical Facilities) is largely determined by the Health Care and Enrollment Projection model of the Department of Veterans Affairs. This model covers approximately 80 percent of the total medical care funding requirement. The remaining funding requirement is estimated based on other models and assumptions for services such as long-term care. To aid the Government Accountability Office in meeting a requirement contained in P.L. 111-81 to develop a report on the adequacy of the Administration's advance appropriations request within 120 days of the release of the President's Budget, the Department of Veterans Affairs has included more detailed information in its Congressional Budget Justifications about the methodology used to determine the overall 2013 VA medical care funding requirement.

One new advance appropriation that the Administration is proposing to be considered outside of the limit on advance appropriations is for full funding of selected procurement programs at the Department of Defense. DOD has developed an innovative strategy for buying satellites, called Evolutionary Acquisition for Space Efficiency (EASE). EASE will reduce costs and improve the stability of the space industrial base. Advance appropriations of the relevant satellite programs in the Missile Procurement, Air Force account are requested to ensure transparency of costs and full funding, both of which are needed for this initiative to succeed. The first program to begin procurement under EASE in 2012 is the Advanced Extremely High Frequency (AEHF) satellite. A regular appropriation is requested for AEHF in 2012 and advance appropriations are requested for 2013 through 2017. Similarly, advance appropriations in the Missile Procurement, Air Force account are requested to enhance industrial base stability and ensure full funding of classified procurement activities. Additionally, advance appropriations will be requested to implement EASE for the Space-Based Infrared Systems (SBIRS). A regular appropriation will be requested for SBIRS in 2013 and advance appropriations will be requested for SBIRS in 2013 for 2014 through 2018 in the Missile Procurement, Air Force account.

For a detailed table of accounts that have received discretionary and mandatory advance appropriations since 2010 or for which the Budget requests advance appropriations for 2013 and beyond, please refer to the Advance Appropriation chapter that can be found in the Budget *Appendix*.

Debt Net of Financial Assets

In the Summary Tables included in the main *Budget* volume, Summary Tables S-1 and S-14 display both debt held by the public and debt held by the public net of financial assets. Borrowing from the public is normally a good approximation of the Federal demand on credit markets. However, it provides an incomplete picture of the financial condition of the Government and under some circumstances may misrepresent the net effect of federal activity on credit markets. Some transactions that increase the Federal debt also increase the financial assets held by the Government. For example, when the Government lends money to a private firm or individual, the Government

acquires a financial asset that provides a stream of future payments of principal and interest. At the time the loan is made, debt held by the public reflects only Treasury's borrowing to finance the loan, failing to reflect the value of the loan asset acquired by the Government. In contrast, debt held by the public net of financial assets provides a more accurate measure of the Government's net financial position by including the value of loans and other financial assets held by the Government.

This measure is especially useful during times, like the present, when the Government has borrowed large sums of money to address difficulties faced by the economy and financial markets. As shown in Summary Table S-14, a large share of the Government's recent borrowing has financed the purchase of financial assets, so that the increase in debt held by the public net of financial assets is noticeably smaller than the overall increase in debt held by the public. Likewise, while Federal borrowing reduces the amount of private saving that is available through financial markets for private-sector investment, Federal acquisition of financial assets has the opposite effect—it injects cash into financial markets. Thus, the change in debt net of financial assets can better indicate the effect of the Federal Government on the financial markets.

Fannie Mae and Freddie Mac

The Budget continues to present Fannie Mae and Freddie Mac, the housing Government-Sponsored Enterprises (GSEs) currently in federal conservatorship, as non-federal entities. However, Treasury equity investments in the GSEs are recorded as budgetary outlays. The Budget begins the process of reducing the Government's role in the U.S. mortgage market and ending the conservatorship of Fannie Mae and Freddie Mac by allowing the temporary GSE and FHA loan limits to expire on October 1, 2011, and by reducing the GSEs' allowable investment portfolios by at least 10 percent a year. In addition, the Administration is transmitting to Congress a framework of principles for making the transition to a new housing finance system that will end the model of private gains and Federal taxpayer losses. The GSEs are discussed in more detail in Chapter 23, "Credit and Insurance," in this volume.

II. IMPROVED DEFINITION OF BASELINE

The Administration also suggests three changes to the concepts used in formulating baseline projections to make the resulting product more useful to the public and to policymakers: extending certain major expiring tax provisions, adjustments for disaster and other "emergency" costs, and adjustments to reflect the cost of fully funding the existing Pell Grant program. In addition, as explained above, the transition from a highway trust fund in which outlays are treated as discretionary to a transportation trust fund whose outlays are treated as mandatory involves adjusting presentations, including baselines, so that corresponding funding and spending levels will be displayed on a comparable basis during the transition.

For years the baseline used by Congress has followed the definition contained in section 257 of the Balanced Budget and Emergency Deficit Control Act of 1985 as amended, often referred to as the Budget Enforcement Act (BEA) baseline. However, the BEA baseline does not accurately reflect a continuation of current policy. Both last year and this, the Administration has built its budget proposals starting from a baseline that adjusts the BEA baseline to better represent the thrust of current policy in certain major cases, and recommends that Congress, the Congressional Budget Office, and the public use such a baseline in their own analyses as well. The deficit impacts of the adjustments to the BEA baseline are summarized in Summary Table S-7 of the Budget. The adjustments are described below. Further detail about the adjusted baseline is provided in Chapter 27, "Current Services Estimates," in this volume.

While the adjusted baseline provides a more realistic basis for analyzing budgets in general and tax policy in particular, the adjusted baseline is not intended to replace the BEA baseline with respect to mandatory programs and revenues, either for legal purposes or to alter the application of the Statutory PAYGO Act of 2010. Specifically, the costs or savings from legislation affecting mandatory spending or revenues are measured relative to the BEA baseline for purpose of entries on the PAYGO scorecards, discussed earlier in the chapter. In addition, the PAYGO Act requires that certain "current policy adjustments" be made to the entries on those scorecards.

Adjustments to Reflect Certain Tax Policies.—In recent years, Congress has repeatedly extended provisions of law that have a large deficit impact or signaled its intention that a provision be extended when it enacted it for a limited number of years. The Administration's adjusted baseline assumes permanent extension of these policies: continuing the 2001 and 2003 income tax cuts for the middle class (using the same definitions specified in the PAYGO Act), extending the estate and gift tax as in effect in 2009, and extending and indexing for inflation the 2011 parameters of the Alternative Minimum Tax.

Two points are especially noteworthy. First, the PAYGO Act provides current policy adjustments that are generally similar in effect to the baseline adjustments described above. However, the PAYGO Act provided adjustments for AMT and estate tax relief only through 2011. In addition, the PAYGO Act provides a current policy adjustment for relief from the scheduled cuts in Medicare physician

ACQUISITION OF FINANCIAL ASSETS

There are a number of circumstances in which the Treasury disburses cash and receives financial assets in return. In some cases, these transactions are recognized as an exchange of financial assets and so are not considered budgetary transactions at all; rather they are considered non-budgetary financing transactions. Purchasing gold, depositing Treasury operating cash in "tax and loan" accounts, or depositing cash with the Federal Reserve are examples of such transactions. In each case, borrowing from the public is higher than it would be if the transaction did not occur, but the extra borrowing does not represent extra spending or a higher deficit because the financial asset acquired by the Treasury fully offsets the liability of extra debt incurred by the Treasury.

Direct loans are a similar example; in those cases, the Government disburses cash (makes a direct loan) to a borrower (e.g., a student, farmer, small business, etc.) and receives in return a loan asset or IOU from the borrower. In most cases the risk of default (and perhaps an interest-rate differential) makes the loan asset worth less than the cash disbursed by the Treasury. The difference in value represents the loss, or cost, the Government is expected to incur on such transactions. Put differently, the difference in value represents a subsidy to the borrower. The Government measures the cost or subsidy by discounting to the present the estimated present and future cash flows related to the loan contract, and records the amount of subsidy as an outlay. Present-value scorekeeping is used precisely because it is a method of comparing the value of future cash flows with an equivalent amount of up-front cash. Chapter 12, "Budget Concepts," in this volume discusses this subject in more detail and Chapter 23, "Credit and Insurance," also in this volume provides more information on credit programs.

Two other similar examples are the Troubled Assets Relief Program (TARP) and the National Railroad Retirement Investment Trust. In each of these cases, the programs can acquire private-sector equities or equivalent financial instruments, and in each case, Congress mandated scorekeeping methods that do not show the purchase prices as an outlay.

However, budget scorekeeping rules have only partially incorporated the concept that the value of an acquired financial asset is best recorded as an offset against the cost of its acquisition. As a result, the cash paid to acquire stock in Fannie Mae and Freddie Mac is recorded as a pure outlay (and increase in the deficit) at the point of purchase. Dividends paid by the two entities appear as cash inflows to the Treasury (and reductions in the deficit). If and when that stock is later sold to the public, the cash received in return will reduce the deficit at that time.

Over time—and accounting for interest on the cash flows – present value or subsidy scorekeeping produces the same total effect on the deficit as cash scorekeeping. The former may be preferable, however, because it means that the Government records the full expected cost of a transaction up front, when it occurs. The same reasoning suggests that the use of the budget to allocate public resources would benefit from up-front or present-value scorekeeping.

payment rates under the "Sustainable Growth Rate" formula. The Administration's adjusted baseline does not do so, in part because Congress has succeeded in offsetting the costs of such SGR relief (relative to the BEA baseline) each of the three most recent times it has enacted such legislation.

Second, the adjustment to the BEA baseline to assume continuation of middle class tax cuts, AMT relief, and estate tax relief are effective after the provisions of the recently enacted Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 expire. The adjusted baseline, like the BEA baseline, reflects that law as long as it remains in effect.

Adjustments for Disaster and Other "Emergency" Costs.—Because the BEA baseline extends all appropriations already enacted for the year in progress, it can be subject to huge swings as a result of funding enacted as an emergency or supplemental requirement. At times, the BEA baseline extends large one-time emergency appropriations for the next 10 years; at other times it extends very little. The Administration's baseline includes adjustments to account for these swings. Specifically, the Administration's adjusted baseline removes any extension of enacted appropriations for disaster costs and substitutes an allowance for disaster costs in the current and future fiscal years. This allowance reflects the fact that major natural or man-made disasters are likely to occur at some point during the remainder of 2011 and in subsequent years—major earthquakes, hurricanes, catastrophic floods, infrastructure collapses, and so on. Obviously, both the timing and amounts are unknowable in advance. In addition to the inclusion of this entry in the baseline, the Administration includes the same allowance in its Budget.

The baseline and Budget figures are not a "reserve fund," nor are they a request for discretionary budget authority or congressional legislation of any kind.[12]

[12] If a major disaster occurs, Federal assistance is likely to be granted in the form of discretionary appropriations, automatic and legislated increases in mandatory programs, and in some cases tax relief. The summary tables show the allowance for disaster costs within the outlay totals for convenience.

Instead, they are placeholders that represent a meaningful down payment on potential future emergency needs. Consequently, the placeholder for major disaster costs is not included in the request for $1,243 billion in discretionary budget authority for 2012. The 2012 request does include amounts that can be reasonably budgeted to cover the ongoing and inevitable costs of programs that fund natural disasters.

Including a meaningful down payment for the costs of potential major disasters makes the budget totals more honest and realistic. Baselines likewise would be more meaningful if they did not project forward whatever disaster costs happen to have occurred in the current year. Rather, baselines should replace the projection of actual current-year costs—which might be unusually low or unusually high—with plausible estimates of future costs. That is, baselines should remove any projection of non-recurring or one-time emergency disaster costs, consistent with the inclusion of an allowance for such costs. In the 2011 appropriations enacted to date, Congress did not need to enact any non-recurring, emergency disaster funding, but that is no reason to believe the Nation will be as fortunate in all future years.

Adjustments to Reflect the Full Cost of Existing Pell Grants.—As explained earlier in this chapter, the discretionary portion of the Pell Grant program has attributes that make it unique among programs classified as discretionary: it annually receives both mandatory and discretionary funding but the two types are indistinguishable in purpose or effect; the amount of discretionary funding has little or no effect on the size or cost of the program; and in recognition of this fact, congressional and Executive Branch scorekeepers agreed in 2006 to a special scorekeeping rule under which appropriations acts would be scored as providing the amount of discretionary budget authority estimated to fully fund the cost of Pell grants in the budget year (which includes covering any shortfalls from prior years), even if the appropriations bill in question provides a lower amount.

Under these circumstances, the Administration believes that the BEA baseline, which projects discretionary programs by adjusting current-year budget authority for inflation, is inconsistent with both the reality and the existing budgetary scorekeeping for Pell Grants. Since the special scorekeeping rule charges the Appropriations Committees with the full cost of providing Pell grants to all eligible applicants plus covering any shortfalls from prior years, the baseline should do the same. This is especially the case because adhering to the BEA baseline level of budget authority for Pell makes no difference to the actual size and cost of the program in the budget year; funding “cuts” or “increases” from such a baseline do not represent actual reductions or increases in costs, at least in the budget year. Therefore, the Administration adjusts the BEA baseline to follow the existing scorekeeping rule, reflecting the full cost of funding the discretionary portion of Pell while covering any prior shortfalls.

As described earlier, an estimate of the full cost of Pell in any year depends in part on the size of the maximum award for that year. The current maximum award for the discretionary portion of Pell is $4,860 per student per year. The adjusted baseline assumes that award level will remain constant in nominal terms over the next ten years. The baseline projection of the discretionary portion of Pell therefore changes from year to year primarily because of estimated changes in the number of valid applicants. Changes in student income and level of tuition can also make a difference in the size of an individual student’s award and therefore the cost of the program.

The Administration believes that baselines prepared by the Congressional Budget Office and others would likewise be more realistic and better reflect the congressional scorekeeping rule if they projected the discretionary portion of Pell Grants in this way.