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Congressional Budget Office

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# **An Analysis of the President's 2013 Budget**

March 2012

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## Notes

Unless otherwise indicated, the years referred to in this report are federal fiscal years (which run from October 1 to September 30).

Numbers in the text and tables may not add up to totals because of rounding.

Supplemental information about this analysis is available on CBO's Web site ([www.cbo.gov](http://www.cbo.gov)).

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# An Analysis of the President's 2013 Budget

## Overview

This report by the Congressional Budget Office (CBO) presents an analysis of the proposals contained in the President's budget request for fiscal year 2013. The analysis is based on CBO's economic projections and estimating techniques (rather than the Administration's) and incorporates estimates by the staff of the Joint Committee on Taxation for the President's tax proposals.<sup>1</sup>

In conjunction with analyzing the President's budget, CBO has updated its baseline budget projections, which were previously issued in January 2012. Unlike its estimates of the President's budget, CBO's baseline projections largely reflect the assumption that current tax and spending laws will remain unchanged, so as to provide a benchmark against which potential legislation can be measured. Under that assumption, CBO estimates that the deficit would total \$1.2 trillion in 2012 and that cumulative deficits over the 2013–2022 period would amount to \$2.9 trillion.<sup>2</sup>

The President's budget request specifies spending and revenue policies for the 2013–2022 period and also includes initiatives that would have budgetary effects in fiscal year 2012.<sup>3</sup> CBO estimates that enactment of the President's proposals would have the following consequences for the budget:

- The deficit in 2012 would equal \$1.3 trillion (or 8.1 percent of gross domestic product), \$82 billion more than the 2012 deficit projected in CBO's baseline.
- In 2013, the deficit would decline to \$977 billion (or 6.1 percent of GDP), \$365 billion more than the shortfall projected for 2013 in CBO's baseline.
- The deficit would decline further relative to GDP in subsequent years, reaching 2.5 percent by 2017, but then would increase again, reaching 3.0 percent of GDP in 2022. The deficits after 2013 would exceed those in CBO's baseline by between 1.4 percent and 1.9 percent of GDP each year (see Table 1).
- In all, between 2013 and 2022, deficits would total \$6.4 trillion (or 3.2 percent of total GDP projected for that period), \$3.5 trillion more than the cumulative deficit in CBO's baseline.
- Federal debt held by the public would increase from \$10.1 trillion (68 percent of GDP) at the end of 2011 to \$15.2 trillion (77 percent of GDP) at the end of 2017 and then to \$18.8 trillion (76 percent of GDP) at the end of 2022 (see Table 2). Under the assumptions of CBO's current-law baseline, debt held by the public would increase more slowly, ending 2022 at \$15.1 trillion; as a percentage of GDP, however, such debt would decline to 61 percent by the end of 2022.

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1. For more details about the President's revenue proposals, see Joint Committee on Taxation, *Estimated Budget Effects of the Revenue Provisions Contained in the President's Fiscal Year 2013 Budget Proposal*, JCX-27-12 (March 14, 2012).

2. For information about CBO's latest baseline, see Congressional Budget Office, *Updated Budget Projections: Fiscal Years 2012 to 2022* (March 2012).

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3. This analysis does not include an assessment of the macroeconomic effects of the President's proposals or the feedback from those effects on the federal budget. CBO will publish a separate analysis of those economic effects and indirect budgetary effects in a few weeks.

**Table 1.**

## Comparison of Projected Revenues, Outlays, and Deficits Under CBO's March 2012 Baseline and in CBO's Estimate of the President's Budget

(Billions of dollars)

	Actual, 2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Total	
													2013-	2013-
													2017	2022
<b>CBO's March 2012 Baseline</b>														
Revenues	2,303	2,456	2,968	3,283	3,589	3,838	4,066	4,272	4,484	4,719	4,962	5,218	17,744	41,398
Outlays	3,603	3,627	3,580	3,668	3,846	4,097	4,267	4,447	4,708	4,953	5,200	5,520	19,457	44,285
<b>Total Deficit</b>	<b>-1,300</b>	<b>-1,171</b>	<b>-612</b>	<b>-385</b>	<b>-257</b>	<b>-259</b>	<b>-201</b>	<b>-175</b>	<b>-224</b>	<b>-234</b>	<b>-237</b>	<b>-303</b>	<b>-1,713</b>	<b>-2,887</b>
<b>CBO's Estimate of the President's Budget</b>														
Revenues	2,303	2,394	2,741	3,105	3,413	3,657	3,868	4,043	4,227	4,445	4,661	4,885	16,783	39,044
Outlays	3,603	3,647	3,717	3,807	3,952	4,186	4,356	4,553	4,829	5,083	5,339	5,613	20,018	45,434
<b>Total Deficit</b>	<b>-1,300</b>	<b>-1,253</b>	<b>-977</b>	<b>-702</b>	<b>-539</b>	<b>-529</b>	<b>-488</b>	<b>-510</b>	<b>-602</b>	<b>-638</b>	<b>-678</b>	<b>-728</b>	<b>-3,235</b>	<b>-6,390</b>
<b>Difference Between CBO's Estimate of the President's Budget and CBO's Baseline</b>														
Revenues	n.a.	-61	-228	-178	-176	-181	-198	-229	-256	-274	-301	-333	-961	-2,354
Outlays	n.a.	20	137	139	106	90	89	106	121	131	139	92	561	1,150
<b>Total Deficit<sup>a</sup></b>	<b>n.a.</b>	<b>-82</b>	<b>-365</b>	<b>-317</b>	<b>-282</b>	<b>-270</b>	<b>-287</b>	<b>-335</b>	<b>-377</b>	<b>-404</b>	<b>-440</b>	<b>-425</b>	<b>-1,522</b>	<b>-3,504</b>
<b>Memorandum:</b>														
Deficit as a Percentage of GDP														
CBO's baseline	-8.7	-7.6	-3.8	-2.3	-1.5	-1.4	-1.0	-0.8	-1.0	-1.0	-1.0	-1.2	-1.9	-1.4
CBO's estimate of the President's budget	-8.7	-8.1	-6.1	-4.2	-3.1	-2.8	-2.5	-2.5	-2.8	-2.8	-2.9	-3.0	-3.7	-3.2
Debt Held by the Public as a Percentage of GDP														
CBO's baseline	67.7	73.2	75.8	75.8	73.3	70.9	68.8	66.9	65.3	63.9	62.4	61.3	n.a.	n.a.
CBO's estimate of the President's budget	67.7	73.7	78.7	80.4	79.4	78.2	77.2	76.6	76.4	76.3	76.3	76.3	n.a.	n.a.

Sources: Congressional Budget Office; Staff of the Joint Committee on Taxation.

Note: n.a. = not applicable; GDP = gross domestic product.

a. Negative numbers indicate an increase in the deficit relative to CBO's baseline.

**Table 2.**  
**CBO's Estimate of the President's Budget**

	Actual,												Total	
	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2013-2017	2013-2022
In Billions of Dollars														
Revenues														
On-budget	1,738	1,838	2,066	2,374	2,641	2,836	2,996	3,124	3,263	3,435	3,606	3,783	12,912	30,123
Off-budget <sup>a</sup>	566	556	675	731	772	821	872	919	965	1,010	1,055	1,102	3,871	8,921
<b>Total</b>	<b>2,303</b>	<b>2,394</b>	<b>2,741</b>	<b>3,105</b>	<b>3,413</b>	<b>3,657</b>	<b>3,868</b>	<b>4,043</b>	<b>4,227</b>	<b>4,445</b>	<b>4,661</b>	<b>4,885</b>	<b>16,783</b>	<b>39,044</b>
Outlays														
Mandatory	2,026	2,119	2,221	2,368	2,497	2,659	2,756	2,869	3,050	3,217	3,399	3,588	12,501	28,624
Discretionary	1,347	1,303	1,259	1,183	1,155	1,158	1,158	1,170	1,198	1,225	1,248	1,282	5,914	12,035
Net interest	230	225	237	255	300	370	442	513	581	642	692	743	1,604	4,775
<b>Total</b>	<b>3,603</b>	<b>3,647</b>	<b>3,717</b>	<b>3,807</b>	<b>3,952</b>	<b>4,186</b>	<b>4,356</b>	<b>4,553</b>	<b>4,829</b>	<b>5,083</b>	<b>5,339</b>	<b>5,613</b>	<b>20,018</b>	<b>45,434</b>
On-budget	3,104	3,144	3,078	3,098	3,197	3,386	3,507	3,654	3,876	4,071	4,264	4,472	16,266	36,603
Off-budget <sup>a</sup>	499	504	639	708	755	800	849	899	953	1,012	1,075	1,141	3,752	8,832
<b>Deficit (-) or Surplus</b>	<b>-1,300</b>	<b>-1,253</b>	<b>-977</b>	<b>-702</b>	<b>-539</b>	<b>-529</b>	<b>-488</b>	<b>-510</b>	<b>-602</b>	<b>-638</b>	<b>-678</b>	<b>-728</b>	<b>-3,235</b>	<b>-6,390</b>
On-budget	-1,367	-1,306	-1,012	-725	-556	-550	-511	-530	-613	-636	-658	-689	-3,354	-6,480
Off-budget <sup>a</sup>	67	53	36	23	18	21	22	20	12	-2	-20	-39	119	90
Debt Held by the Public	10,128	11,427	12,517	13,331	13,982	14,618	15,215	15,825	16,519	17,246	18,007	18,819	n.a.	n.a.
<b>Memorandum:</b>														
Gross Domestic Product	14,954	15,508	15,914	16,575	17,618	18,704	19,708	20,661	21,616	22,603	23,614	24,655	88,519	201,666
As a Percentage of Gross Domestic Product														
Revenues														
On-budget	11.6	11.9	13.0	14.3	15.0	15.2	15.2	15.1	15.1	15.2	15.3	15.3	14.6	14.9
Off-budget <sup>a</sup>	3.8	3.6	4.2	4.4	4.4	4.4	4.4	4.4	4.5	4.5	4.5	4.5	4.4	4.4
<b>Total</b>	<b>15.4</b>	<b>15.4</b>	<b>17.2</b>	<b>18.7</b>	<b>19.4</b>	<b>19.6</b>	<b>19.6</b>	<b>19.6</b>	<b>19.6</b>	<b>19.7</b>	<b>19.7</b>	<b>19.8</b>	<b>19.0</b>	<b>19.4</b>
Outlays														
Mandatory spending	13.6	13.7	14.0	14.3	14.2	14.2	14.0	13.9	14.1	14.2	14.4	14.6	14.1	14.2
Discretionary spending	9.0	8.4	7.9	7.1	6.6	6.2	5.9	5.7	5.5	5.4	5.3	5.2	6.7	6.0
Net interest	1.5	1.5	1.5	1.5	1.7	2.0	2.2	2.5	2.7	2.8	2.9	3.0	1.8	2.4
<b>Total</b>	<b>24.1</b>	<b>23.5</b>	<b>23.4</b>	<b>23.0</b>	<b>22.4</b>	<b>22.4</b>	<b>22.1</b>	<b>22.0</b>	<b>22.3</b>	<b>22.5</b>	<b>22.6</b>	<b>22.8</b>	<b>22.6</b>	<b>22.5</b>
On-budget	20.8	20.3	19.3	18.7	18.1	18.1	17.8	17.7	17.9	18.0	18.1	18.1	18.4	18.2
Off-budget <sup>a</sup>	3.3	3.2	4.0	4.3	4.3	4.3	4.3	4.4	4.4	4.5	4.6	4.6	4.2	4.4
<b>Deficit (-) or Surplus</b>	<b>-8.7</b>	<b>-8.1</b>	<b>-6.1</b>	<b>-4.2</b>	<b>-3.1</b>	<b>-2.8</b>	<b>-2.5</b>	<b>-2.5</b>	<b>-2.8</b>	<b>-2.8</b>	<b>-2.9</b>	<b>-3.0</b>	<b>-3.7</b>	<b>-3.2</b>
On-budget	-9.1	-8.4	-6.4	-4.4	-3.2	-2.9	-2.6	-2.6	-2.8	-2.8	-2.8	-2.8	-3.8	-3.2
Off-budget <sup>a</sup>	0.4	0.3	0.2	0.1	0.1	0.1	0.1	0.1	0.1	*	-0.1	-0.2	0.1	*
Debt Held by the Public	67.7	73.7	78.7	80.4	79.4	78.2	77.2	76.6	76.4	76.3	76.3	76.3	n.a.	n.a.

Sources: Congressional Budget Office; Staff of the Joint Committee on Taxation.

Note: n.a. = not applicable; \* = between -0.05 percent and 0.05 percent.

a. Off-budget surpluses or deficits comprise surpluses or deficits in the Social Security trust funds and the net cash flow of the Postal Service.

The President's budget contains a host of proposed changes to spending and revenue policies. By CBO's estimate, those policy changes would, on net, add about \$2.9 trillion to projected deficits over the 2013–2022 period and necessitate \$0.6 trillion in additional interest payments (because of increased federal borrowing). Most of the net budgetary impact would come from changes in tax policies, but changes in spending policies would also play a role:

- The President proposes to extend certain tax provisions that are slated to expire or that have already expired. The 2010 tax act (officially the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010, Public Law 111-312) extended through December 2012 many of the income tax reductions originally 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). The President proposes to make those reductions permanent—except, in some cases, for higher-income taxpayers. In addition, the President seeks to reduce the number of taxpayers who would be subject to the alternative minimum tax (AMT) by permanently setting various parameters of that tax at the amounts that were in effect in calendar year 2011 and indexing those amounts for inflation in later years. The President also proposes, starting in January 2013, to permanently restore the rates and exemption levels for estate and gift taxes that were in effect in calendar year 2009. Together, those policies would reduce tax revenues and boost outlays for refundable tax credits by a total of about \$3.5 trillion over the 2013–2022 period relative to the amounts projected in CBO's baseline.<sup>4</sup>
- Automatic procedures specified by last year's Budget Control Act (P.L. 112-25) are set to go into effect in January 2013 and reduce spending in subsequent years.<sup>5</sup> The President's budget does not include those reductions, thereby boosting outlays relative to the current-law baseline by \$1.0 trillion over the next 10 years.

4. A tax credit is refundable if the taxpayer receives a refund when the allowable credit exceeds the amount of tax owed. Such refunds are recorded in the budget as outlays.

- The President is also proposing some policies that would reduce projected deficits relative to CBO's baseline. For example, the President's budget envisions funding for military operations in Afghanistan and for related activities (also known as overseas contingency operations, or OCO) that is less than the amounts in CBO's baseline. As specified in law, the baseline incorporates the assumption that funding for such activities will total \$127 billion (the amount provided in 2012) each year through 2022, with increases to keep pace with inflation; the President's budget, by comparison, includes a request for \$97 billion for OCO in 2013 and \$44 billion in each year thereafter through 2022. The cumulative difference in outlays between CBO's baseline and the President's proposal is \$0.8 trillion over the 2013–2022 period.
- The President would also cap the rate at which certain deductions and exclusions reduce a taxpayer's income tax liability at 28 percent; that change would decrease deficits by a total of \$0.5 trillion over the next decade.
- Other proposals in the President's budget include some initiatives that would widen the deficit and others that would narrow it. Those other proposals would change revenues and noninterest outlays by amounts that sum to a net reduction in deficits of about \$0.2 trillion over the 2013–2022 period.
- Because the net revenue reductions and spending increases that would occur under the President's budget would increase deficits relative to CBO's baseline projections, the amount of interest paid on the debt would also rise. In total, net interest outlays under the President's budget would exceed the amounts projected in CBO's current-law baseline by \$0.6 trillion over the 2013–2022 period.

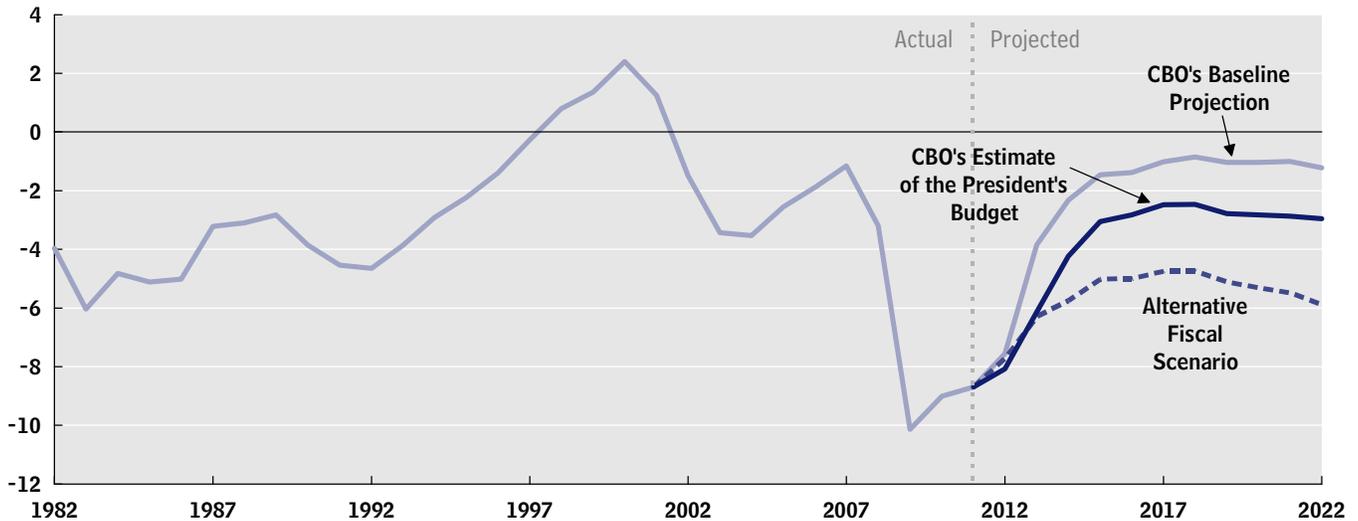
Under current law, a number of significant changes are scheduled to occur to policies that are now in place. To provide another benchmark against which budgetary proposals can be measured—largely reflecting current

5. Under the provisions of that law, because the Joint Select Committee on Deficit Reduction did not report legislation to reduce the deficit, automatic procedures to cut both discretionary and mandatory spending during the coming decade are scheduled to take effect. For more details about those procedures, see Congressional Budget Office, *The Budget and Economic Outlook: Fiscal Years 2012 to 2022* (January 2012), Box 1-2, pp. 12–13.

**Figure 1.**

## Deficits Projected in CBO's Baseline, Under the President's Budget, and Under an Alternative Fiscal Scenario

(Percentage of gross domestic product)



Source: Congressional Budget Office.

Note: The alternative fiscal scenario incorporates the assumptions that all expiring tax provisions (other than the payroll tax reduction), including those that expired at the end of December 2011, are instead extended; that the alternative minimum tax is indexed for inflation after 2011 (starting at the 2011 exemption amount); that Medicare's payment rates for physicians' services are held constant at their current level; and that the automatic spending reductions specified by the Budget Control Act of 2011 do not take effect.

policies rather than current law—CBO has also developed an alternative fiscal scenario. It incorporates the assumptions that tax provisions that have recently expired or are set to expire (other than the 2 percentage-point reduction in the payroll tax rate for Social Security) are extended through 2022, that the AMT is indexed for inflation after 2011, that Medicare's payment rates for physicians' services are held constant at their current level, and that the automatic spending reductions required by the Budget Control Act do not take effect (although the original caps on discretionary appropriations in that law are assumed to remain in place). Under that scenario, budget deficits would total \$10.7 trillion over the 2013–2022 period, and debt held by the public would rise to \$23.0 trillion by 2022. Deficits and debt under the President's budget, though significantly larger than in CBO's baseline, would be significantly smaller than the amounts projected in the alternative fiscal scenario (see Figures 1 and 2).<sup>6</sup>

CBO's estimates of deficits under the President's budget are generally smaller than those of the Administration—by \$74 billion (or 6 percent) for 2012 and by a total of

\$294 billion (or 4 percent) for the following 10 years. CBO projects \$1.5 trillion (or 3 percent) less in outlays under the President's budget than the Administration does, because of differences both in economic assumptions and in modeling and other technical assumptions. CBO's estimates of revenues under the President's budget are also lower than the Administration's—by \$1.2 trillion (or 3 percent)—primarily because of differing economic assumptions (particularly about wages and salaries).

### Impact of the President's Proposals on the Budget Outlook

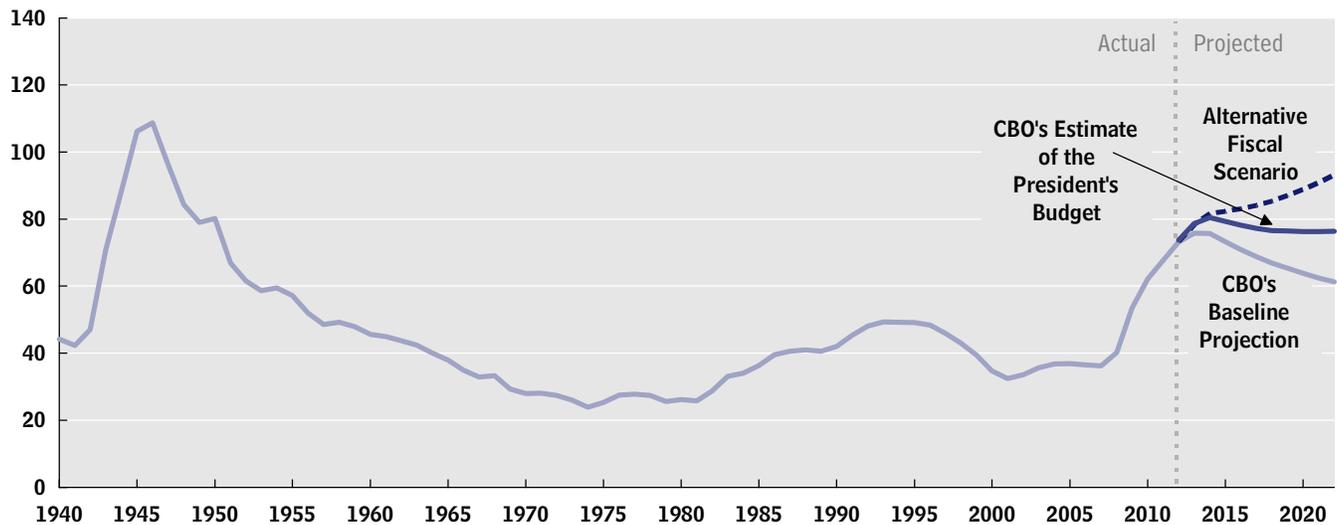
Enacting the President's policy proposals would boost the 2012 deficit by \$82 billion—to a total of \$1,253 billion—relative to CBO's current-law baseline (see Table 3 on page 8). That increase would result from an additional \$20 billion in outlays in 2012 and a decrease of

6. Year-by-year data for the alternative fiscal scenario are presented in Congressional Budget Office, *Updated Budget Projections: Fiscal Years 2012 to 2022* (March 2012).

**Figure 2.**

## Federal Debt Held by the Public Projected in CBO's Baseline, Under the President's Budget, and Under an Alternative Fiscal Scenario

(Percentage of gross domestic product)



Source: Congressional Budget Office.

Note: The alternative fiscal scenario incorporates the assumptions that all expiring tax provisions (other than the payroll tax reduction), including those that expired at the end of December 2011, are instead extended; that the alternative minimum tax is indexed for inflation after 2011 (starting at the 2011 exemption amount); that Medicare's payment rates for physicians' services are held constant at their current level; and that the automatic spending reductions specified by the Budget Control Act of 2011 do not take effect.

\$61 billion in revenues. In 2013, the deficit under the President's budget would be \$365 billion greater than the deficit that CBO projects in its latest baseline, because revenues would be \$228 billion (or 8 percent) lower, and outlays would be \$137 billion (or 4 percent) higher.<sup>7</sup>

Over the 2013–2022 period, the cumulative deficit that would result from enacting the President's budget—\$6.4 trillion (or 3.2 percent of GDP)—would be \$3.5 trillion larger than the cumulative deficit projected under current law. About \$2.9 trillion of that difference stems directly from proposed policy changes, and the other \$0.6 trillion reflects additional interest payments resulting from increased federal borrowing.

7. Since the release of the President's budget on February 13, 2012, a number of policies have been enacted into law—most notably, an extension through December 2012 of the reduced Social Security payroll tax rate for employees—that were either proposed in the budget or were similar to proposals in the budget. CBO has incorporated the effects of all enacted legislation into its new baseline and thus does not assign any effects from those proposals to the President's budget.

### Effects on Revenues

The President is proposing to make a number of changes to tax law. If enacted, those changes would reduce revenues by \$61 billion in 2012 and by \$2.4 trillion—or about 6 percent—during the 2013–2022 period relative to the amounts in CBO's baseline. Those totals represent the net effect of the President's tax proposals, some of which would reduce revenues and others of which would increase them. (Those revenue proposals would also boost outlays by \$442 billion between 2013 and 2022, mostly from increases in refundable tax credits and, to a lesser extent, from the spending component of a proposal to reinstate and alter the Build America Bonds program, which would raise outlays and revenues by similar amounts.) As a share of GDP, revenues would rise from 17.2 percent in 2013 to 19.8 percent in 2022 under the President's budget. Between 2015 and 2022, they would average 19.6 percent of GDP—1.2 percentage points below CBO's baseline projection but 1.7 percentage points above the average ratio of revenues to GDP seen over the past 40 years.

### **Extending and Modifying the 2001 and 2003 Tax**

**Reductions.** Various income tax provisions that were originally enacted in EGTRRA and JGTRRA, modified by the American Recovery and Reinvestment Act of 2009 (ARRA, P.L. 111-5), and extended by the 2010 tax act are scheduled to expire at the end of December 2012. Those provisions include reductions in some individual income tax rates, cuts in tax rates on capital gains and dividends, elimination of the phaseout of personal exemptions and the limit on itemized deductions for certain taxpayers, an increase in the child tax credit, relief from the so-called marriage penalty, and changes in the tax treatment of certain investments in equipment by small businesses.

As estimated by the staff of the Joint Committee on Taxation (JCT), the President's proposal to make those provisions permanent—with some modifications—would reduce revenues by \$2.1 trillion (or 1.0 percent of GDP) over the next 10 years and increase outlays by \$314 billion (or 0.2 percent of GDP) relative to the amounts in CBO's baseline.<sup>8</sup> (Some of those proposals would affect outlays because the tax credits involved are refundable.) Specifically, the President has called for permanently extending, at 2012 levels, the tax rates on income, capital gains, and dividends for couples with income below \$250,000 who file joint tax returns and for single filers with income below \$200,000. (Both of those income thresholds would be adjusted for inflation since 2009.) For taxpayers with income above the thresholds, the President proposes to maintain the income tax rates, the phaseout of the personal exemption, and the limit on itemized deductions that are scheduled to take effect in January 2013 under current law and to tax capital gains at a rate of 20 percent. In addition, the President proposes to continue the \$1,000 child tax credit (which was raised by \$500 in EGTRRA) and the reduced earnings threshold at which families can qualify for at least some of that credit (which was enacted in ARRA).

### **Providing Relief from the Alternative Minimum Tax.**

Besides extending those tax provisions, the President proposes to reduce the number of taxpayers who would be subject to the AMT by permanently setting various parameters of the tax at the levels that were in effect in calendar year 2011 and indexing those amounts for

inflation in later years. Those parameters include the AMT exemption amount, the income threshold for phasing out that exemption amount, and the income threshold for the 28 percent tax rate. The President also proposes to make permanent the unrestricted use of certain personal tax credits under the AMT. Relative to current law, those changes would reduce revenues by \$855 billion between 2013 and 2022, JCT estimates.<sup>9</sup>

**Limiting Deductions and Exclusions.** The President proposes to limit the extent to which higher-income taxpayers can reduce their tax liability through certain deductions and exclusions to 28 percent of those deductions and exclusions. The limit would apply to itemized deductions as well as to deductions or exclusions for tax-exempt interest, employer-sponsored health insurance, and employees' retirement contributions, among other things. That change would boost revenues by \$523 billion over the 2013–2022 period, according to JCT.

**Modifying Estate and Gift Taxes.** The President's budget calls for setting the parameters of the estate, gift, and generation-skipping transfer taxes at the levels that were in effect during calendar year 2009, starting in January 2013. Under that proposal, the amount of an estate that would effectively be exempt from the estate tax would be set permanently at \$3.5 million (and at \$7 million per couple in most cases); any amount above that effective exemption level would be taxed at a rate of 45 percent. The exemption amount for gift taxes would be set at \$1 million, with a top tax rate of 45 percent. Transfers of wealth from a decedent to an heir more than one generation younger (such as a grandchild) would also be taxed at 45 percent. Those proposals, along with some other changes to those taxes, are estimated to lower revenues by \$245 billion between 2013 and 2022.

**Other Revenue Proposals.** Other proposals in the President's budget would reduce revenues by \$48 billion this year but would increase revenues, on net, by \$300 billion over the 2013–2022 period. Those proposals include a set of changes to the U.S. system of taxing international income that would raise revenues by \$168 billion over 10 years, JCT estimates. The changes include targeting

8. That revenue estimate incorporates the effects of interactions between those provisions and the President's AMT proposal discussed below. Such interactions increase the projected revenue reduction relative to what it would be without the AMT proposal.

9. That estimate does not reflect the interactions between the AMT provisions and the proposal to extend and modify the 2001 and 2003 tax reductions extended in the 2010 tax act. The effects of those interactions are included in the estimate for that latter proposal.

**Table 3.****CBO's Estimate of the Effect of the President's Budget on Baseline Deficits**

(Billions of dollars)

	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Total	
												2013-	2013-
												2017	2022
Deficit in CBO's March 2012 Baseline	-1,171	-612	-385	-257	-259	-201	-175	-224	-234	-237	-303	-1,713	-2,887
Effect of the President's Proposals													
Revenues													
Provisions related to EGTRRA and JGTRRA <sup>a</sup>													
Modify individual income tax rates <sup>b</sup>	0	-75	-109	-116	-124	-132	-140	-149	-157	-165	-174	-555	-1,341
Provide relief from the marriage penalty	0	-20	-30	-32	-35	-37	-39	-41	-43	-45	-47	-154	-370
Extend child tax credit provisions <sup>c</sup>	0	-3	-13	-13	-14	-14	-14	-14	-14	-14	-14	-57	-129
Modify tax rates on capital gains and dividends <sup>d</sup>	-1	-5	-8	-15	-15	-15	-15	-15	-16	-16	-17	-58	-137
Other provisions	*	-6	-12	-11	-11	-11	-10	-10	-10	-10	-11	-50	-101
Subtotal	-1	-108	-173	-187	-198	-208	-219	-230	-241	-252	-262	-874	-2,077
Index the AMT starting from 2011 levels <sup>a</sup>	-9	-94	-42	-49	-57	-66	-78	-92	-107	-125	-144	-308	-855
Limit the tax rate at which deductions and exclusions													
reduce tax liability	-3	19	43	43	48	52	56	60	64	67	71	205	523
Modify estate and gift tax provisions	*	-1	-19	-22	-24	-26	-27	-29	-31	-32	-34	-91	-245
Modify the U.S. international tax system	0	7	15	16	17	18	19	19	20	19	18	73	168
Extend the research and experimentation tax credit	-3	-5	-6	-7	-8	-9	-10	-11	-12	-13	-14	-36	-96
Extend the American Opportunity Credit	0	-2	-7	-8	-8	-8	-9	-9	-9	-10	-10	-34	-81
Reinstate and modify the Build America													
Bonds program <sup>e</sup>	*	1	2	3	4	5	7	8	10	11	13	14	63
Extend full expensing for certain property	-32	-16	13	9	7	6	3	2	1	1	1	19	27
Other proposals	-13	-28	-3	25	38	39	30	26	32	31	29	71	219
<b>Total Effect on Revenues</b>	<b>-61</b>	<b>-228</b>	<b>-178</b>	<b>-176</b>	<b>-181</b>	<b>-198</b>	<b>-229</b>	<b>-256</b>	<b>-274</b>	<b>-301</b>	<b>-333</b>	<b>-961</b>	<b>-2,354</b>
Outlays													
Mandatory													
Reclassify surface transportation spending													
as mandatory	0	15	35	45	49	53	55	57	58	59	61	196	486
Other changes to transportation programs	*	10	13	11	13	16	20	17	10	6	4	65	123
Extend or expand certain refundable tax credits	*	1	39	39	40	41	41	41	41	42	42	160	366
Freeze Medicare's physician payment rates													
at 2012 level	0	11	18	21	24	26	28	31	34	37	41	100	271
Other changes to Medicare	*	*	-8	-18	-22	-26	-30	-32	-39	-46	-54	-74	-276
Changes to Medicaid	0	1	2	-3	-4	-9	-9	-10	-9	-10	-15	-14	-66
Reinstate and modify the Build America													
Bonds program <sup>e</sup>	*	1	2	3	4	6	7	9	11	12	14	16	70
Eliminate automatic spending reductions <sup>f</sup>	0	9	13	13	14	14	15	16	17	17	6	64	134
Other proposals	18	45	29	23	7	2	-1	-1	-2	-2	-45	106	54
Subtotal	19	93	144	136	124	122	127	128	120	116	53	619	1,163

Continued

**Table 3.** **Continued**  
**CBO's Estimate of the Effect of the President's Budget on Baseline Deficits**

(Billions of dollars)

	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Total		
												2013-	2013-	
												2017	2022	
Outlays (Continued)														
Discretionary														
Eliminate automatic spending reductions <sup>f</sup>	0	56	79	87	89	91	90	89	88	87	88	402	845	
Changes to spending on overseas contingency operations <sup>g</sup>	0	-12	-52	-75	-85	-90	-93	-96	-99	-102	-106	-313	-810	
Reclassify surface transportation spending as mandatory	0	-15	-35	-45	-49	-53	-55	-57	-58	-59	-61	-196	-486	
Other	*	11	-4	-12	-17	-23	-22	-21	-19	-21	-21	-44	-148	
Subtotal	*	41	-12	-44	-62	-75	-80	-85	-88	-95	-100	-151	-598	
Net interest	2	4	7	14	27	42	59	78	98	119	139	93	586	
<b>Total Effect on Outlays</b>	<b>20</b>	<b>137</b>	<b>139</b>	<b>106</b>	<b>90</b>	<b>89</b>	<b>106</b>	<b>121</b>	<b>131</b>	<b>139</b>	<b>92</b>	<b>561</b>	<b>1,150</b>	
<b>Total Effect on the Deficit<sup>h</sup></b>	<b>-82</b>	<b>-365</b>	<b>-317</b>	<b>-282</b>	<b>-270</b>	<b>-287</b>	<b>-335</b>	<b>-377</b>	<b>-404</b>	<b>-440</b>	<b>-425</b>	<b>-1,522</b>	<b>-3,504</b>	
Deficit Under the President's Budget as Estimated by CBO	-1,253	-977	-702	-539	-529	-488	-510	-602	-638	-678	-728	-3,235	-6,390	
<b>Memorandum:</b>														
Total Effects of Eliminating Automatic Spending Reductions <sup>f</sup>	0	65	92	101	103	105	105	105	105	104	94	466	980	

Sources: Congressional Budget Office; Staff of the Joint Committee on Taxation.

Note: EGTRRA = Economic Growth and Tax Relief Reconciliation Act of 2001; JGTRRA = Jobs and Growth Tax Relief Reconciliation Act of 2003; AMT = alternative minimum tax; \* = between -\$500 million and \$500 million.

- The estimated effects of the President's proposals related to EGTRRA and JGTRRA interact with the effects of the proposal to index the AMT. This analysis first estimated the revenue effects of the proposal for the AMT relative to projections under current law, and then it estimated the effects of the proposals related to EGTRRA and JGTRRA relative to projections under current law modified for the proposed changes to the AMT. Thus, the estimates for the proposals related to EGTRRA and JGTRRA include estimated losses in revenues that would result from interactions with the AMT proposal.
- The estimates include the effects of maintaining, for taxpayers with income above certain levels, the income tax rates of 36 percent and 39.6 percent scheduled to go into effect in calendar year 2013 under current law. For other taxpayers, tax rates would be at the levels originally specified in EGTRRA and extended through calendar year 2012 in the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010.
- This proposal includes extending the \$1,000 child tax credit and the use of that credit to reduce AMT liability.
- The estimate includes the effect of maintaining the capital gains and dividend tax rates of zero and 15 percent for couples who file joint tax returns and have income below \$250,000 and for single filers who have income below \$200,000.
- This proposal affects revenues and outlays. The staff of the Joint Committee on Taxation estimates that the net effect of the proposal for the Build America Bonds program is to increase the deficit by \$7 billion over the 2013–2022 period.
- The Budget Control Act specified that if legislation originating with the Joint Select Committee on Deficit Reduction to reduce the deficit was not enacted, automatic procedures to cut both discretionary and mandatory spending during the coming decade would take effect. Because the committee did not report any legislation, those reductions are scheduled to go into effect on January 2, 2013. The President's budget does not include such automatic spending reductions.
- These changes reflect the net effect of replacing the baseline extrapolation of funding for overseas contingency operations with the President's request for such funding.
- Negative numbers indicate an increase in the deficit relative to CBO's baseline.

specific sources of tax avoidance associated with intangible assets (such as patents and trademarks) and modifying tax rules for calculating foreign tax credits and expenses related to foreign operations.

The tax credit for research and experimentation expired at the end of calendar year 2011. The President proposes to permanently reinstate it, in modified form, and make it retroactive to January 1, 2012. Those changes would decrease revenues by \$96 billion over the 2013–2022 period, according to JCT.

The American Opportunity Tax Credit, which was created by ARRA and extended through December 2012 by the 2010 tax act, provides an annual tax credit of up to \$2,500 per student for qualifying postsecondary education expenses. The President also proposes to make that credit permanent and to index the amount of qualifying expenses and the phaseout limits for inflation. JCT estimates that those changes would decrease revenues by \$81 billion over the next 10 years and increase outlays by \$27 billion, thus adding \$108 billion to the cumulative deficit over that period.

The Build America Bonds program, which was also created by ARRA, provides subsidy payments to state and local governments that equal 35 percent of their interest costs on taxable bonds issued through December 31, 2010, to finance capital expenditures. The program has expired for bonds issued after that date; the President proposes to permanently reinstate and expand it but to lower the subsidy rate to 30 percent through 2013 and to 28 percent thereafter. By substituting taxable bonds for tax-exempt bonds, the program increases taxable interest income. According to JCT, the President's changes would raise revenues by \$63 billion between 2013 and 2022. They would also boost subsidy payments to state and local governments, which are recorded in the federal budget as outlays, by an estimated \$70 billion over 10 years. Thus, the net effect of those changes would be to increase the cumulative 10-year deficit by \$7 billion.

The President also proposes to extend through 2012 a provision that allows all firms that invest in equipment to deduct the full costs of that equipment from their taxable income immediately, instead of spreading the costs out over time. That provision would decrease revenues by \$32 billion in 2012 but boost them by \$27 billion over the 2013–2022 period, JCT estimates.

Taken together, all of the remaining revenue proposals in the President's budget would raise revenues by \$219 billion over the next 10 years relative to current law. Proposals that CBO and JCT estimate would increase revenues include repealing the "last-in, first-out" method of accounting for inventories (an increase of \$67 billion between 2013 and 2022); imposing a "financial crisis responsibility fee" (\$61 billion);<sup>10</sup> providing short-term tax relief to employers and expanding the base for the payroll tax for unemployment compensation (\$30 billion); and boosting spending for enforcement activities of the Internal Revenue Service (\$35 billion).<sup>11</sup> Partly offsetting those revenue increases would be revenue reductions from extending through 2013 a host of tax provisions that have been extended in past years (\$41 billion).

### Effects on Outlays

On the spending side of the budget, the President's policies would increase noninterest outlays by \$19 billion in 2012 and by \$564 billion (or 1 percent) between 2013 and 2022 relative to CBO's baseline projections. Because the President's revenue and spending proposals together would increase deficits and thus require additional federal borrowing, they would also raise interest costs—by an estimated \$586 billion over the 2013–2022 period. Total outlays would equal 23.4 percent of GDP in 2013, decline as a share of GDP through 2018, and then rise. They would equal 22.8 percent of GDP in 2022—about 0.4 percentage points higher than CBO's baseline projection for that year and well above the 21.0 percent average seen over the past 40 years.

10. The Administration did not provide enough detail about the President's proposal to impose a financial crisis responsibility fee to allow for a full assessment of its effects on revenues. Additional specifications would be required for JCT to produce a revenue estimate. However, CBO incorporated the Administration's estimate (rounded to the nearest billion dollars) as a placeholder because CBO judged that the revenues estimated in the budget proposal could feasibly be raised in the general manner described.

11. That proposal would provide funding for the Internal Revenue Service's enforcement activities above the amounts projected in CBO's baseline. If lawmakers provided such increased funding, CBO and JCT estimate that additional revenues would result, and an estimate of such revenues is included in this analysis. However, budgetary savings (such as increased revenues) from providing additional appropriations for administrative spending cannot be counted as an offset to such spending for Congressional score-keeping purposes.

Excluding interest costs, total outlays would exceed the amounts in CBO's baseline in each year from 2012 to 2021. However, such outlays would be lower than CBO's baseline projection in 2022 as a result of a shift in the timing of certain payments for benefit programs. (Under current law, those payments will move into fiscal year 2022 from 2023 because the normal payment date, October 1, falls on a weekend. The President proposes to shift the payments back into fiscal year 2023.)

Outlays for mandatory programs would be \$1.2 trillion higher through 2022 under the President's budget than in CBO's baseline, largely because of two factors: a reclassification of spending for surface transportation that is currently categorized as discretionary, and a greater amount of refundable tax credits. Relative to GDP, mandatory outlays would equal 14.0 percent in 2013 under the President's budget and generally remain at or above that level; by 2022, mandatory outlays would equal 14.6 percent of GDP, 0.2 percentage points higher than in CBO's baseline.

For discretionary programs, the President's budget reflects spending over the next 10 years that is nearly \$600 billion below the amounts in CBO's baseline, mainly because less funding is proposed for war-related activities than is projected in the baseline and because transportation spending is reclassified. In total, discretionary outlays would drop from 7.9 percent of GDP in 2013 to 5.2 percent in 2022, 0.4 percentage points lower than in CBO's baseline.

**Proposals That Would Affect Mandatory Spending.** The proposal with the largest impact on mandatory spending is the one to reclassify most funding for surface transportation programs from discretionary to mandatory (including all surface transportation programs funded through the Highway Trust Fund). That reclassification would not, by itself, have any net budgetary impact, but it would boost mandatory outlays (and reduce discretionary outlays) by \$486 billion over the 2013–2022 period.<sup>12</sup> All other changes to transportation programs proposed by the President would increase mandatory outlays, on net, by \$123 billion over the next 10 years.

The President proposes to extend or expand various refundable tax credits, including the earned income tax credit, the child tax credit, and some education credits. Other tax proposals in the President's budget, particularly the extension of certain provisions originally enacted in

EGTRRA and JGTRRA, would also affect the refundable portion of tax credits. All told, the President's policy changes would increase outlays for refundable credits by an estimated \$366 billion over the 2013–2022 period.

Under current law, Medicare's payment rates for physicians' services are slated to drop by 27 percent in January 2013 and by additional amounts in later years. The President proposes to avoid those reductions by freezing payment rates at their 2012 level for the next 10 years. That freeze would increase net outlays by \$271 billion over the 2013–2022 period, CBO estimates.

The President's budget includes numerous other proposals involving Medicare, most of which are designed to reduce the program's spending. Several provisions would modify payments to health care providers, such as hospitals and skilled nursing facilities. In addition, the President proposes to modify cost-sharing responsibilities for some Medicare beneficiaries. Additional savings would result from proposals to require manufacturers to pay rebates on drugs dispensed to low-income beneficiaries enrolled in Part D of Medicare and to reduce payment rates for certain biological drugs (products derived from living material) covered under Part B of the program. Finally, the budget includes several provisions designed to reduce waste, fraud, and abuse in Medicare. In all, those policies (other than the freeze on physicians' payment rates) would reduce Medicare outlays by \$276 billion over 10 years, CBO estimates.<sup>13</sup>

12. For programs funded through the Highway Trust Fund, budget authority is classified as mandatory under current law, but outlays are considered discretionary because they have historically been controlled by obligation limitations set in appropriation acts. Reclassifying those programs—which could be done without legislation if agreed to by the House and Senate Budget Committees, the Administration, and CBO—would shift \$401 billion from the discretionary to the mandatory category over the 2013–2022 period in CBO's baseline. However, some surface transportation programs are currently funded through discretionary budget authority and would require legislation to reclassify; in CBO's baseline, outlays for those programs total \$85 billion between 2013 and 2022.

13. That figure does not include the effect on Medicare spending of the President's proposal to eliminate automatic budget enforcement procedures, which is discussed separately. CBO's March 2012 baseline projections for Medicare incorporate \$88 billion in net savings from automatic procedures that would reduce payment rates for most Medicare services by 2 percent between February 2013 and January 2022.

The President is also seeking a number of changes to the Medicaid program, which, if adopted, would generate net savings of \$66 billion over the 2013–2022 period relative to CBO’s baseline. The President proposes to limit the amount of revenues from taxes on health care providers that states can use to pay their portion of Medicaid costs, beginning in 2015. In addition, under current law, states receive different federal matching rates for expenditures under Medicaid and the Children’s Health Insurance Program (CHIP), and they will receive enhanced matching rates beginning in 2014 for people who become eligible for Medicaid as a result of the Affordable Care Act.<sup>14</sup> The President proposes to replace that rate structure, starting in 2017, with a single matching rate for each state; that rate would automatically increase if a recession forced enrollment and states’ costs to rise. Other proposed changes to Medicaid include limiting certain payment rates and, in 2022, limiting reimbursements for hospitals that serve a disproportionate number of poor and uninsured people.

The proposal discussed above to reinstate and expand the Build America Bonds program and lower its subsidy rate would boost outlays by \$70 billion through 2022, JCT estimates. Combined with the corresponding revenue increase of \$63 billion, that proposal would result in a net increase of \$7 billion in the cumulative 10-year deficit.

In addition, the automatic enforcement procedures specified by the Budget Control Act are set to go into effect in January 2013 and to reduce mandatory spending by an estimated \$134 billion over the next 10 years. The President’s budget does not include those reductions, thereby boosting mandatory outlays relative to the current-law baseline.

All of the other proposed changes to mandatory programs, taken together, would increase outlays by \$18 billion in 2012 and by \$54 billion over the 2013–2022 period. Such changes include the President’s proposals to significantly increase funding in 2012 for certain education and job-training activities, such as

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14. The Affordable Care Act comprises the Patient Protection and Affordable Care Act (P.L. 111-148) and the health care provisions of the Health Care and Education Reconciliation Act of 2010 (P.L. 111-152).

subsidizing summer employment for young people and providing grants to states to pay teachers and modernize schools. Those proposals, which are similar to ones made by the Administration last fall, would increase spending by \$11 billion in 2012 and by \$69 billion over the 2013–2022 period, CBO estimates.

**Proposals That Would Affect Discretionary Spending.** For 2012, discretionary budget authority would be slightly greater under the President’s budget than in CBO’s baseline.<sup>15</sup> The only difference is that the President is requesting supplemental funding of \$0.4 billion for additional program-integrity initiatives aimed at reducing wasteful or fraudulent spending in certain entitlement programs.

For 2013, the President has requested \$1.15 trillion in discretionary budget authority, which is \$52 billion (or 4 percent) less than the amount enacted for 2012 plus the request for supplemental funding (see Table 4). More than half of the reduction between those two years (\$30 billion) would result from decreased appropriations for overseas contingency operations; other appropriations would decline by about 2 percent. In 2014, total discretionary funding under the President’s budget would drop by 4 percent, to \$1.1 trillion, but it would grow in later years, reaching \$1.3 trillion in 2022.

Most appropriations for 2013 through 2021 are constrained by caps put in place by the Budget Control Act (although funding for certain purposes, such as OCO, is not limited by those caps).<sup>16</sup> The caps currently in law apply separately to defense and nondefense budget authority for each year, but the President’s budget refers to a classification in the Budget Control Act that was previously in effect and that applies caps to “security” and “nonsecurity” funding for 2013 and to a single

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15. Discretionary budget authority is the authority provided in appropriation acts to incur financial obligations that will result in immediate or future outlays.

16. The caps discussed here do not include the further reductions called for under current law as a result of the automatic enforcement procedures in the Budget Control Act. For more details about those procedures, see Congressional Budget Office, *The Budget and Economic Outlook: Fiscal Years 2012 to 2022* (January 2012), Box 1-2, pp. 12–13.

**Table 4.**

**Proposed Changes in Discretionary Budget Authority in the President's Budget, 2011 to 2013**

(Billions of dollars)

	Actual, 2011	Administration's Request		Percentage Change	
		2012 <sup>a</sup>	2013	2011-2012	2012-2013
<b>Defense</b>					
Overseas contingency operations <sup>b</sup>	159	115	88	-27.6	-23.3
Other	551	554	552	0.5	-0.4
Subtotal	711	670	640	-5.8	-4.4
<b>Nondefense</b>					
Overseas contingency operations <sup>b</sup>	0	11	8	n.a.	-26.4
Other	510	518	498	1.5	-3.8
Subtotal	510	529	507	3.7	-4.3
<b>Total</b>	<b>1,221</b>	<b>1,199</b>	<b>1,147</b>	<b>-1.8</b>	<b>-4.3</b>

Source: Congressional Budget Office.

Notes: The numbers shown here do not include obligation limitations for certain transportation programs.

n.a. = not applicable.

- a. The Administration's request for discretionary budget authority for 2012 reflects the appropriations enacted for this year plus \$410 million for additional program-integrity initiatives aimed at reducing wasteful or fraudulent spending in certain entitlement programs.
- b. In this table, "overseas contingency operations" refers to military operations in Iraq and Afghanistan and related activities.

discretionary category from 2014 to 2021.<sup>17</sup> By CBO's estimate, the total appropriations requested for 2013 that are constrained by the caps are roughly equal to the total amount of the caps for that year (\$1,043 billion, which represents the \$1,047 billion specified in current law, adjusted downward by about \$4 billion to account for the President's proposal to reclassify some surface transporta-

tion programs as mandatory). However, according to CBO's estimates, appropriations for 2013 in the security category would exceed their cap by \$2 billion, whereas nonsecurity appropriations would fall below their cap by about the same amount (after adjusting for the reclassification proposal).<sup>18</sup> Nevertheless, by the Administration's estimate—which is the one that would determine whether a sequestration (an automatic cancellation of budgetary resources) would go into effect—no breach of either cap would take place.

On top of the \$1,043 billion in proposed budget authority for 2013 that is limited by the caps, the President proposes \$104 billion in funding for that year that would

17. "Defense" discretionary programs are those in budget function 050; "nondefense" programs comprise all other discretionary appropriations. Under the Administration's classification (namely, the categories originally specified in the Budget Control Act), the security category would comprise discretionary appropriations for the Department of Defense, the Department of Homeland Security, the Department of Veterans Affairs, the National Nuclear Security Administration, the intelligence community management account (95-0401-0-1-054), and discretionary accounts in budget function 150 (international affairs). The nonsecurity category would comprise all other discretionary appropriations. The Budget Control Act initially set caps on discretionary appropriations using the "security" and "nonsecurity" categories. However, under the provisions of that law, because the Joint Select Committee on Deficit Reduction did not report legislation to reduce the deficit, the caps were reset to cover defense and nondefense programs to serve as the basis for the automatic spending reductions that are set to take effect in January 2013.

18. A number of differences exist between CBO's estimates of discretionary budget authority for 2013 and the Administration's estimates. The two largest differences involve the Federal Housing Administration (FHA) and the Department of Defense. CBO estimates that more mortgages will be guaranteed by the FHA than the Administration does; those guarantees will result in more receipts to the FHA in 2013. In addition, CBO estimates that the Administration's proposal to reduce the amount of annual contributions to the Medicare-Eligible Retiree Health Care Fund would not be implemented in time to affect the 2013 accrual payments.

not be constrained by the caps. The additional funding—which, by law, the caps can be adjusted to accommodate—would be used for the following purposes:

- \$97 billion for overseas contingency operations,
- \$6 billion for disaster relief, and
- \$2 billion for program-integrity initiatives.

Overall, budget authority for defense discretionary programs would decrease by \$29 billion (or 4 percent) between 2012 and 2013 under the President's budget. Funding for defense activities classified as OCO would fall by \$27 billion (or 23 percent) to \$88 billion in 2013, and appropriations for other defense activities would decline by \$2 billion (or 0.4 percent).

For nondefense discretionary programs, budget authority would decrease by \$23 billion (or 4 percent) between 2012 and 2013 under the President's budget. That drop stems mainly from four sources:

- A shift of \$8 billion for the Department of Justice's Crime Victims Fund from 2013 into 2014,
- A proposal to reduce by \$6.7 billion the funding available for paying performance bonuses to states under CHIP in 2013,<sup>19</sup>
- An additional \$5 billion in receipts that CBO expects the Federal Housing Administration to receive in 2013 under current law because of increases in the volume of loans and in premiums (relative to 2012) for the mortgage guarantees that it provides, and
- A reduction in budget authority of \$4.2 billion in 2013 because of the proposal to reclassify many

19. States qualify for performance bonus payments under CHIP on an annual basis if they adopt at least five of eight specific enrollment processes (which are generally aimed at simplifying Medicaid and CHIP enrollment and renewal for children) and if the number of children enrolled in Medicaid in the state exceeds certain benchmarks. Because the President is requesting this funding change for a mandatory program through the appropriation process, it is classified as a reduction in discretionary funding. CBO does not expect the reduction to have any effect on outlays, because the amounts available for performance bonus payments, even after the proposed reduction, are well above the amounts that states are expected to qualify for.

surface transportation programs from discretionary to mandatory.<sup>20</sup>

Under the President's budget, most other nondefense discretionary programs would receive funding for 2013 similar to what was provided for 2012.

Thereafter, total discretionary budget authority proposed by the President would rise by an average of about 2 percent per year—from \$1.1 trillion in 2014 to \$1.3 trillion in 2022. The proposed funding includes a placeholder of \$44 billion a year for OCO (although the Administration does not specify how much of that future request would be classified as defense spending).<sup>21</sup> The totals do not include any further request for disaster relief funding, but they include requests of between \$2 billion and \$4 billion a year for program-integrity initiatives. Between 2014 and 2021, appropriations subject to the overall cap on discretionary spending in the President's budget would be below that cap in each year (after adjusting for the proposal to reclassify some surface transportation programs as mandatory).

Outlays from the discretionary budget authority requested in the President's budget would total \$1.26 trillion in 2013 and then decline to \$1.15 trillion in 2015 before beginning to grow again. Such outlays would reach \$1.28 trillion in 2022, returning to about the same level anticipated for 2013. As a share of GDP, discretionary outlays would fall from 9.0 percent in 2011 to 5.2 percent in 2022—the lowest level in the past 50 years. Cumulative outlays over the 2013–2022 period would be nearly \$600 billion (or 5 percent) less than CBO's baseline projection, largely because OCO funding would be set below the level assumed in the baseline and because spending for most surface transportation programs would be reclassified as mandatory, thereby reducing discretionary outlays between 2013 and 2022 by \$810 billion and \$486 billion, respectively. Such reductions would be partially offset by eliminating the automatic spending cuts (which would increase discretionary outlays by

20. Most surface transportation programs are currently funded through mandatory budget authority provided in authorizing legislation. However, annual appropriation acts control spending for those programs by limiting how much of the budget authority the Department of Transportation can obligate.

21. In 2012 and most previous years, some OCO funding was provided for diplomatic operations and foreign aid, which are classified as nondefense spending.

\$845 billion) currently scheduled for 2013 through 2021. Other proposed changes to discretionary programs would reduce outlays by \$148 billion during the 2013–2022 period.

**Effect of the President's Proposals on Net Interest.** The policy changes in the President's budget would increase the government's borrowing needs by \$3.6 trillion over the 2013–2022 period (including the effect on nonbudgetary cash flows for credit programs); as a result, outlays for net interest payments would exceed the amounts projected in CBO's baseline by nearly \$590 billion over that period. In nominal dollars (without adjusting for inflation), net interest costs would triple during those 10 years: from \$237 billion in 2013 to \$743 billion in 2022. Relative to the size of the economy, net interest payments would amount to 3.0 percent of GDP in 2022 under the President's budget, about 0.6 percentage points higher than in the baseline and double the percentage estimated for 2013.

## Differences Between CBO's and the Administration's Estimates of the President's Budget

On net, CBO's estimate of the cumulative deficit for the 2013–2022 period that would result under the President's budget is about 5 percent less than the Administration's estimate. However, there are significant differences, mostly offsetting, in projections of revenues and outlays.

For 2012, CBO's estimate of the deficit under the President's budget is \$74 billion smaller than the shortfall estimated by the Administration; the difference stems from a \$148 billion lower estimate of outlays, which is partly offset by a lower estimate of revenues. For the following 10 years, CBO's estimate of the cumulative deficit under the President's budget is about \$300 billion below the Administration's estimate, because CBO's projections of outlays are \$1.5 trillion lower and its projections of revenues are \$1.2 trillion lower (see Table 5).

### Differences in Estimates of Revenues

CBO attributes the bulk of the difference in revenue estimates for 2012 to differences in the outlook for the economy. In particular, CBO projects lower amounts of personal income, especially wages and salaries, and of corporate profits.

For the 2013–2022 period, CBO projects 3 percent less in revenues under the President's proposals than the Administration does. That disparity results almost entirely from different baseline projections rather than from different assessments of the impact of the President's proposals. CBO's baseline projections of revenues over that period are about \$1.6 trillion lower than the Administration's because of different economic projections, by CBO's reckoning, but are about \$0.4 trillion higher than the Administration's because of different estimates of the amount of revenue that will result from a given set of economic conditions.

Specifically, CBO's economic projections imply less revenue than the Administration's do largely because CBO projects that wages and salaries—the most significant component of the tax bases for individual income and payroll taxes—will be about \$3.2 trillion (or 3 percent) lower over the next 10 calendar years than the Administration projects. In addition, CBO projects that domestic economic profits—the main component of the tax base for corporate income taxes—will be \$1.5 trillion (or 8 percent) lower than the Administration projects.

### Differences in Estimates of Outlays

CBO's estimate of outlays in 2012 under the President's budget is \$148 billion lower than the Administration's estimate, mainly because of technical differences. The proposal to reclassify some surface transportation programs affects how those technical differences are ascribed to mandatory and discretionary outlays. The President's budget reflects the assumption that the reclassification will occur this year and thus shows such outlays as mandatory in 2012. CBO, by contrast, assumes that if the policy was enacted, it would not take effect until 2013. That discrepancy is offset on the discretionary side of the ledger. Without the reclassification, the technical differences in mandatory outlays for 2012 shown in Table 5 would be -\$77 billion (rather than -\$129 billion), and the differences in discretionary outlays would be -\$68 billion (rather than -\$16 billion).

On the mandatory side, CBO estimates \$19 billion less in outlays for the Deposit Insurance Fund in 2012 than the Administration does, mainly because of considerably lower projections of losses. Another large difference for 2012 results from differing estimates for a policy proposal: CBO estimates that certain increases in education funding proposed by the President would be spent more slowly than the Administration expects, leading to a

**Table 5.****Sources of Differences Between CBO's and the Administration's Estimates of the President's Budget**

(Billions of dollars)

	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Total	
												2013-	2013-
												2017	2022
<b>Administration's Estimate</b>													
Deficit Under the President's Budget	-1,327	-901	-668	-610	-649	-612	-575	-626	-658	-681	-704	-3,440	-6,684
<b>Differences Between CBO's and the Administration's Estimates</b>													
<b>Differences in Revenues<sup>a</sup></b>													
Economic	-87	-166	-155	-122	-108	-140	-171	-188	-193	-185	-175	-691	-1,604
Technical	13	5	44	84	85	89	61	37	34	-10	-56	308	373
Total	-74	-161	-111	-37	-23	-51	-110	-151	-159	-195	-231	-384	-1,230
<b>Differences in Outlays<sup>b</sup></b>													
<b>Mandatory</b>													
Economic	-4	-6	-7	-16	-27	-32	-34	-38	-41	-45	-51	-88	-298
Technical	-129	-66	-38	-22	-18	-18	-11	-15	-20	-37	-44	-162	-289
Subtotal	-133	-73	-45	-38	-45	-49	-45	-53	-62	-82	-95	-250	-587
Discretionary (Technical)	-16	-2	23	20	15	-3	-13	-11	-11	-10	-5	52	3
<b>Net interest</b>													
Economic	-4	-20	-55	-87	-103	-101	-86	-69	-56	-47	-41	-367	-664
Technical	4	9	1	-3	-10	-22	-33	-43	-50	-59	-66	-25	-276
Subtotal	1	-11	-54	-90	-113	-123	-118	-111	-106	-106	-107	-392	-940
Total	-148	-86	-76	-108	-143	-175	-176	-175	-179	-198	-207	-589	-1,524
<b>Total Differences<sup>a</sup></b>	<b>74</b>	<b>-75</b>	<b>-34</b>	<b>71</b>	<b>120</b>	<b>124</b>	<b>66</b>	<b>24</b>	<b>20</b>	<b>3</b>	<b>-24</b>	<b>205</b>	<b>294</b>
<b>CBO's Estimate</b>													
Deficit Under the President's Budget	-1,253	-977	-702	-539	-529	-488	-510	-602	-638	-678	-728	-3,235	-6,390
<b>Memorandum:</b>													
Total Economic Differences <sup>a</sup>	-80	-139	-93	-19	22	-8	-51	-82	-96	-93	-83	-237	-641
Total Technical Differences <sup>a</sup>	153	64	58	90	98	132	116	106	115	96	59	442	935

Sources: Congressional Budget Office; Staff of the Joint Committee on Taxation.

a. Positive numbers indicate that such differences cause CBO's estimate of the deficit to be lower than the Administration's estimate.

b. Positive numbers indicate that such differences cause CBO's estimate of the deficit to be higher than the Administration's estimate.

\$20 billion lower estimate of outlays for this year. On the discretionary side, CBO's estimates of defense spending in 2012 are \$36 billion below the Administration's, primarily because of differences in estimates for military procurement (\$14 billion lower), operations and maintenance (\$13 billion lower), and research and development (\$6 billion lower). In addition, CBO estimates about

\$4 billion less in outlays this year for loans to manufacturers of energy-efficient vehicles and related components and about \$3 billion less in spending on disaster relief.

For the 2013–2022 period, CBO's projection of total outlays under the President's budget is \$1.5 trillion below that of the Administration, almost entirely because of a

nearly \$600 billion (or 2 percent) difference in estimates of mandatory spending and a \$940 billion (or 16 percent) difference in estimates of net interest.

The total difference over 10 years between CBO's and the Administration's estimates of mandatory spending under the President's budget is nearly evenly attributable to economic differences (\$298 billion) and technical factors (\$289 billion). Differing projections of Social Security outlays account for \$186 billion of the economic differences; compared with the Administration, CBO projects lower cost-of-living adjustments in most of the next 10 years (an average of 0.4 percentage points lower per year through 2017) and lower average wages for Social Security participants (which lead to lower initial benefit levels). In addition, CBO's projections of Medicare outlays are nearly \$84 billion lower than the Administration's for economic reasons, mainly because of lower projections for the indexes used to calculate prices for Medicare providers.

CBO's estimates of mandatory spending in the 2013–2022 period under the President's budget are \$289 billion lower than the Administration's for technical reasons because of differences in baselines as well as different estimates of the President's policy proposals. The largest technical differences involve estimates of outlays for veterans' compensation and pensions, for Fannie Mae and Freddie Mac, and for Medicaid, as well as the reclassification of surface transportation programs. The Administration projects much higher growth in the population of veterans receiving disability compensation over the next 10 years and higher average benefit payments. As a result, CBO's baseline projection of outlays for veterans' compensation is \$235 billion lower than the Administration's for that period. Conversely, CBO's baseline projection of costs related to Fannie Mae and Freddie Mac is nearly \$210 billion higher than that of the Administration, mostly because CBO's total is in accord with the budgetary practices used for federal credit programs and reflects the anticipated subsidy cost (including an adjustment for market risk) of mortgage guarantees issued by Fannie Mae and Freddie Mac. The Administration, by contrast, records the net payments to and receipts from those two entities.<sup>22</sup> The divergence in baseline projections for Medicaid results from differing estimates of enrollment and other factors; such differences cause CBO's baseline projection to exceed the Administration's by \$157 billion over the 2013–2022 period.

Technical differences in estimates of mandatory spending are also affected by differing classifications of some surface transportation funding provided before 2013. As noted above, CBO's estimate of the President's budget reflects the assumption that the reclassification would not occur until 2013 and that future outlays from funding provided before that year would remain classified as discretionary; the Administration considers such outlays in 2012 and beyond as mandatory, regardless of when the original funding was provided. That difference in classification is largely responsible for CBO's \$131 billion lower estimate of mandatory outlays for surface transportation between 2013 and 2022; the difference has the opposite effect on estimates of discretionary spending.

CBO's estimates of discretionary outlays under the President's budget are significantly lower than the Administration's for a number of programs. The largest such differences involve the Pell Grant program (\$58 billion) and mortgage credit programs administered by the Federal Housing Administration (\$20 billion).

CBO's estimates of net interest outlays under the President's budget are lower than the Administration's by \$940 billion over the 2013–2022 period. About 70 percent of that difference (\$664 billion) is economic in nature and occurs primarily because CBO projects lower interest rates for the coming decade than the Administration does. On average for that period, CBO anticipates rates that are 0.6 percentage points lower for 3-month Treasury bills and 0.5 percentage points lower for 10-year Treasury notes. The other 30 percent of the difference in projections of net interest (\$276 billion) stems mainly from differences in assumptions about the mix of securities that the Treasury will issue over the next 10 years.

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22. The Administration treats Fannie Mae and Freddie Mac as non-governmental organizations and records payments between them and the Treasury on a cash basis. In contrast, CBO projects the budgetary impact of Fannie Mae's and Freddie Mac's operations as if they were being conducted by a federal agency, because of the degree of management and financial control that the government exercises over the two entities. Therefore, CBO estimates the net lifetime costs—that is, the subsidy costs—of new loans and guarantees to be issued by the entities and counts those costs as federal outlays in the year of issuance. See Congressional Budget Office, *CBO's Budgetary Treatment of Fannie Mae and Freddie Mac* (January 2010), and *Fannie Mae, Freddie Mac, and the Federal Role in the Secondary Mortgage Market* (December 2010).

## About This Document

This Congressional Budget Office (CBO) analysis of the President's budgetary proposals for fiscal year 2013 (which were released on February 13, 2012) was prepared at the request of the Senate Committee on Appropriations. In keeping with CBO's mandate to provide objective, impartial analysis, the report makes no recommendations.

Barry Blom of CBO's Budget Analysis Division wrote the report, with assistance from Mark Booth, Pamela Greene, Amber Marcellino, and Santiago Vallinas, under the supervision of Jeffrey Holland, Theresa Gullo, Holly Harvey, Peter Fontaine, and Frank Sammartino. The estimates described here were the work of many analysts at CBO and on the staff of the Joint Committee on Taxation.

Chris Howlett edited the report, with assistance from Sherry Snyder. Maureen Costantino and Jeanine Rees prepared the report for publication. An electronic version is available on CBO's Web site ([www.cbo.gov](http://www.cbo.gov)).



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