

July 14, 2009

Honorable Paul Ryan
Ranking Member
Committee on the Budget
U.S. House of Representatives
Washington, DC 20515

Dear Congressman:

This letter responds to your request for an analysis of H.R. 2920, the Statutory Pay-As-You-Go Act of 2009, as introduced on June 17, 2009. That legislation, which is virtually identical to the proposal recently advanced by the Administration, would establish new statutory pay-as-you-go (PAYGO) requirements and authorize the Administration to enforce compliance through a sequestration mechanism. That process, although similar to the statutory PAYGO system that was in place from 1990 through 2002, would differ from the former system in several significant ways.

Since the expiration of the former statutory PAYGO requirements, the House of Representatives and the Senate have each instituted a rules-based pay-as-you-go process. The statutory process detailed in H.R. 2920 would differ substantially from the House and Senate rules. One significant difference is that the current rules are applied on a bill-by-bill basis as the House and the Senate consider legislation, whereas the proposed statutory process (like the former PAYGO system) would apply to the cumulative estimated impact on the deficit of legislation affecting direct spending and revenues enacted during a given year.

In the Congressional Budget Office's (CBO's) view, the PAYGO process specified in H.R. 2920 includes some features—in particular, the statutory sequestration mechanism—that could enhance overall budget enforcement. However, the proposed process has other features that could lead to greater spending or lower revenues in the coming decade than would occur under the existing House and Senate rules. For example, the provisions in H.R. 2920 that would exempt certain tax and spending policies from the PAYGO requirements and alter the proposed scoring of conversions of programs from a discretionary to a mandatory status could increase future deficits. Removing those provisions might mitigate such an effect.

Honorable Paul Ryan
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Another consideration in enacting statutory PAYGO requirements is how modifications to the budget process would affect the balance between the Congress's and the executive branch's control over the budget. As introduced, H.R. 2920 would shift some control over the budget process from the Congress to the executive branch in ways that could effectively require lawmakers to vote on legislation without a clear indication of the potential impact of their decisions on the triggering of a future sequestration.

The enclosed analysis of H.R. 2920 details some key issues that the Congress may want to consider with regard to the proposed statutory pay-as-you-go legislation. I hope this information is helpful to the Committee on the Budget. If you have follow-up questions, we would be happy to address them. CBO's staff contacts for this analysis are T.J. McGrath, Megan Carroll, and Chad Chirico.

Sincerely,

A handwritten signature in black ink that reads "Douglas W. Elmendorf". The signature is written in a cursive, flowing style.

Douglas W. Elmendorf
Director

Enclosure

cc: Honorable John M. Spratt Jr.
Chairman

Honorable Kent Conrad
Chairman, Senate Committee on the Budget

Honorable Judd Gregg
Ranking Member

CONGRESSIONAL BUDGET OFFICE

An Analysis of H.R. 2920, the Statutory Pay-As-You-Go Act of 2009

July 14, 2009

H.R. 2920 would establish a new statutory form of pay-as-you-go (PAYGO) budget enforcement—which, broadly speaking, is intended to ensure that laws affecting direct (mandatory) spending or revenues are, in total, budget neutral. This Congressional Budget Office (CBO) analysis reviews the statutory PAYGO system that was enacted in 1990 and that remained in place until fiscal year 2002, and the current pay-as-you-go rules adopted by the House of Representatives and the Senate. It then presents an overview of the key features of H.R. 2920 and assesses the possible effects of the legislation on future budget deficits and control of the budget process.

Statutory PAYGO Under the Budget Enforcement Act of 1990

In 1990, lawmakers enacted the Budget Enforcement Act of 1990 (BEA) as part of a multiyear agreement embodied in the Omnibus Budget Reconciliation Act of 1990 that was intended to reduce federal budget deficits.¹ The principal enforcement procedures set in place by the BEA were a PAYGO requirement for new laws affecting mandatory spending (spending not subject to annual appropriation action) and revenues, and a set of annual limits on discretionary spending. Together, the two types of procedures helped enforce the law's multiyear fiscal targets and prevent further deterioration in the federal budget outlook.

Under the BEA, both the PAYGO requirement and the limits on discretionary spending were enforced by the President's ordering of a sequestration, in which a largely uniform percentage reduction of budget authority (that is, a cancellation of budgetary resources) was imposed if the requirement and limits were not adhered to. To help determine whether such a process would be triggered, the incremental net effects on direct spending and revenues from laws enacted during a Congressional session and in prior years were maintained on a rolling PAYGO "scorecard." A sequestration would be ordered if the cumulative effect of legislation enacted during a session was to increase the deficit. No PAYGO sequestration action occurred under the BEA,

1. The BEA amended the Balanced Budget and Emergency Deficit Control Act of 1985 by replacing the deficit targets set out in that legislation with the pay-as-you-go approach and specified limits on discretionary spending.

although one small reduction in discretionary budget authority took place as a result of a sequestration of appropriated funds.²

The nation's fiscal outlook improved considerably during the 1990–2002 period, when the BEA procedures were in place. Much of that improvement was not the direct result of the BEA framework, but the framework may have contributed to more favorable budgetary outcomes by discouraging the adoption of policies that would have worsened the fiscal outlook. Still, because the BEA's PAYGO requirements applied only to incremental changes in policy, they could not address a fiscal imbalance arising from existing policies.

The Current Congressional Pay-As-You-Go Rules

Since the expiration of the BEA's PAYGO requirements at the end of 2002, the House and the Senate have each enforced a pay-as-you-go approach through procedural rules.³ Like the previous statutory PAYGO requirements, the current rules attempt to discourage the enactment of legislation affecting direct spending and revenues that would increase the deficit. Those rules focus on net deficit effects over two time spans: a 6-year period consisting of the current year, the upcoming budget year, and the following 4 years; and an 11-year period consisting of the current year, the upcoming budget year, and the subsequent 9 years. The net effect that a piece of legislation would have on the deficit is determined on the basis of estimates made relative to the baseline that underlies the current Congressional budget resolution. The Congress recently adopted CBO's March 2009 baseline for enforcement under S. Con. Res. 13, the concurrent resolution on the budget for fiscal year 2010.

If the pay-as-you-go requirements are breached as a result of a particular bill, the House and Senate enforce their respective rules solely through points of order while the legislation is being considered.⁴ A supermajority of 60 votes is required to waive a point of order in the Senate; in the House, a point of order may be waived by a majority vote. The current House and Senate rules apply pay-as-you-go requirements on a bill-by-bill basis for consideration of legislation on the floor. In contrast, the proposed

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2. During the years that the BEA was in effect, a sequestration of mandatory spending was never ordered. For 2001 and later years, however, lawmakers enacted legislation to eliminate more than \$700 billion in positive balances—that is, amounts that would have triggered a sequestration—from the PAYGO scorecard. Most of that amount stemmed from the estimated decline in revenues attributed to the Economic Growth and Tax Relief Reconciliation Act of 2001. By contrast, in the years before 2001, the balances on the scorecard were either zero or negative, and lawmakers statutorily removed negative balances so that those savings could not be used to offset the costs of new legislation that affected mandatory spending or revenues.
 3. The Senate and the House have had such rules in place since 1993 and 2007, respectively. Between 2002 and 2007, the House enforced a pay-as-you-go approach using other budget rules.
 4. A point of order is a procedure by which a member of a legislature (or similar body) questions an action that is being taken, or that is proposed to be taken, as contrary to that body's rules, practices, or precedents.

statutory PAYGO regime would cover an accumulation of estimated effects on the deficit for a particular year from legislation affecting direct spending and revenues.

The Statutory PAYGO Regime Proposed in H.R. 2920

H.R. 2920 would establish a statutory PAYGO requirement, enforced through sequestration, for legislation enacted through 2013 that affects mandatory spending and revenues. As under the Budget Enforcement Act, H.R. 2920 would require the Office of Management and Budget (OMB) to maintain a PAYGO ledger and to determine whether a sequestration would be needed; however, the process for maintaining the ledger would differ from that specified in the BEA. The primary difference would be that under H.R. 2920, OMB would develop estimates of the *average* annual impact of legislation over a 10-year period consisting of the upcoming budget year and 9 subsequent years and record that amount on the PAYGO ledger for each year through 2013. (If legislation resulted in current-year effects on the deficit, those effects would be included in the total before computing such an average.)

The sequestration mechanism under H.R. 2920 would be invoked if at the end of a session of Congress the amounts recorded on the PAYGO ledger for the budget year summed to a net cost. In that case, the President would order a sequestration of certain mandatory programs deemed nonexempt under the bill. H.R. 2920 provides an extensive list of programs that would be exempt from sequestration; as was the case under the BEA statute, the exempt programs would represent the vast majority of annual mandatory spending, leaving only a relatively modest amount of such spending to form a “sequesterable base” to which across-the-board reductions could be applied.

For the purposes of PAYGO, estimates of a bill’s effects on the deficit would be made relative to projections of revenues and spending under the current-law baseline in most cases, but exceptions would be made for particular spending and tax provisions. Specifically, H.R. 2920 would establish a temporary rule under which the effects of such provisions would be entered on the PAYGO ledger only to the extent that they exceeded estimated costs under OMB’s “current-policy” projections. (That rule is discussed in greater detail in the next section.)

The proposed bill would also modify the existing set of scorekeeping procedures, concepts, and baseline projection methods that support the current House and Senate pay-as-you-go rules. In particular:

- H.R. 2920 would allow the increased mandatory costs resulting from legislation that would convert a discretionary program into a mandatory one to be offset for PAYGO purposes by the discretionary spending that would be forgone under the legislation but that had been projected previously in the baseline. (Currently, reductions in the need for future appropriations for discretionary activities cannot offset increases in mandatory spending.)

- H.R. 2920 would require that, for the purpose of baseline projections, any mandatory program with outlays in excess of \$50 million be assumed to continue to operate beyond its scheduled expiration date. (Currently, spending for some programs is not extrapolated in the baseline beyond the programs' scheduled expiration date.)
- To avoid counting emergency spending for PAYGO purposes, H.R. 2920 would require the President explicitly to affirm any Congressional designation of an emergency requirement. (Currently, an emergency designation in proposed legislation satisfies the rules of the House and Senate.)

CBO's Analysis of H.R. 2920

Combined with the Congress's existing pay-as-you-go rules, a statutory sequestration mechanism such as the one proposed under H.R. 2920 could enhance overall budget enforcement. However, if the system envisioned in H.R. 2920 was used in place of the current Congressional rules or a more stringent statutory PAYGO system, the legislation's enactment could lead to larger future deficits. In addition, H.R. 2920 would shift a significant amount of control over the budget process from the Congress to the executive branch.

Effects on Future Deficits

Compared with the Congress's current pay-as-you-go rules, H.R. 2920 could lead to higher spending or lower revenues in future years by incorporating certain increases in spending and reductions in revenues into the baseline for budget enforcement purposes. In particular, the legislation might increase deficits through three channels: the proposed temporary rule to score certain changes in spending and revenues relative to "current policy" rather than current law; the bill's modification of the baseline's treatment of some expiring mandatory programs; and the new procedures the bill would put in place for scoring legislation that would convert programs' spending from discretionary to mandatory. In addition, some features of the bill's proposed sequestration mechanism would limit its usefulness in deterring increases in spending.

Temporary Rule to Reflect "Current Policy." Section 7 of H.R. 2920 would establish a temporary rule to address the PAYGO scoring of legislation affecting four areas of the budget:

- Medicare's "sustainable growth rate" mechanism for paying physicians under section 1848 of the Social Security Act;
- The estate and gift tax;
- The alternative minimum tax for individuals; and

- The income tax cuts enacted in the Economic Growth and Tax Relief Reconciliation Act of 2001 and the Jobs and Growth Tax Relief Reconciliation Act of 2003.

In each of those areas, current law would lead, over time, to lower spending or higher revenues than would transpire under “current policy” as many observers might define it, and CBO’s baseline reflects those current-law reductions in spending and increases in revenues. The temporary rule proposed in H.R. 2920 would require that any legislative changes affecting those four areas of the budget be scored relative to the Administration’s estimates of the costs of continuing current policies and not relative to a current-law baseline. In effect, that rule would allow the Congress to enact legislation that would increase deficits by an amount in the vicinity of \$3 trillion over the 2010–2019 period without triggering a sequestration. Under the current Congressional pay-as-you-go rules, legislative changes to policies affecting those four budget areas are scored relative to current law, requiring the Congress to offset increased budgetary costs with spending cuts in those areas, designate such costs as emergency requirements, or waive the pay-as-you-go requirements. Alternatively, through the budget resolution, the Congress may specify allowances for increased budgetary costs in certain policy areas.⁵

Expiring Mandatory Programs. H.R. 2920 would require that all mandatory programs with current-year outlays greater than \$50 million be continued in the baseline after the programs expire. Under current budgetary practices, programs of that kind that existed before enactment of the Balanced Budget Act of 1997 are assumed to continue in the baseline after their expiration, as are some programs that were enacted after the 1997 law—for example, mandatory spending for Pell grants and some agriculture programs. (The assumption that the latter programs continue in the baseline derives from consultations between CBO and the House and Senate Budget Committees.) Several “temporary” programs enacted in recent years, however, are not assumed to continue beyond their scheduled expiration dates. Those programs include some other agriculture programs, certain programs for higher education, and some payments to state and local governments that have federal land within their jurisdictions.

By continuing additional expiring programs in the baseline, H.R. 2920 would facilitate increases in future spending because, unlike the current Congressional rules, it would allow the affected programs to be extended without triggering PAYGO requirements. Under H.R. 2920, any subsequent legislation to extend programs whose extension was already incorporated in the baseline would not trigger a PAYGO sequestration unless the legislation would so modify the program that additional costs would be created beyond those generated by a simple extension.

5. S. Con. Res. 13, the Concurrent Resolution on the Budget for Fiscal Year 2010, includes almost \$2 trillion in allowances for “current-policy” adjustments by the House Budget Committee to take into account changes in certain tax policies and in Medicare’s payments to physicians. For estimates related to the extension of expiring tax provisions, see Congressional Budget Office, *The Budget and Economic Outlook: Fiscal Years 2009 to 2019* (January 2009), Table 7.

That provision of H.R. 2920, in CBO's estimation, could add at least \$25 billion to the baseline over the 2010–2019 period. In keeping with the principle that proposed legislation should be scored to quantify its incremental effects relative to the current budget resolution baseline, CBO believes that H.R. 2920 itself should be scored as increasing mandatory spending.

Conversion of Programs from Discretionary to Mandatory Status. H.R. 2920 departs from the BEA's requirements and from current scorekeeping procedures in yet another way: It would allow legislation that converts a discretionary program into a mandatory one to be scored with the net effect of increased mandatory spending minus the estimated discretionary spending that would be forgone but that had already been projected in the baseline. In effect, that approach would give the legislation credit for reducing projected spending under annual appropriations that had not yet been enacted.

If the statutory PAYGO proposal contained in H.R. 2920 was accompanied by a system of caps, or limits, on discretionary spending, the proposed treatment of program conversions could be combined with a corresponding reduction in the caps to make the conversions budget neutral. However, in the absence of such limits, the program conversion provision could lead to increases in mandatory spending that might not be offset by decreases in discretionary spending. Specifically, the elimination of a discretionary program (by converting it to a mandatory program) could lead to lower appropriations in the future, but without a system similar to the discretionary spending caps that the BEA put in place, such reductions in discretionary outlays could not be enforced.

Sequestration as a Deterrent. Under H.R. 2920, the power of sequestration as a deterrent would be weakened by two factors. First, the PAYGO scorecard would be based on the *average* annual budgetary effects of legislation over a 10-year period rather than year-by-year effects, and the sequestration mechanism would expire after 2014. That combination would require less budgetary discipline than is required to fully offset increases in spending on a year-by-year basis or to continue the sequestration enforcement mechanism indefinitely. In particular, the lack of such a mechanism after 2014 (unless the PAYGO procedures were to be extended beyond that date) would create an incentive for the Congress to adopt legislation that combined near-term costs with anticipated savings in later years—to avoid a sequestration through 2014—and then possibly to repeal or modify those policies after 2014, when the statutory constraints would no longer be binding.

Second, the threat of sequestration would apply only to relatively modest amounts of mandatory spending because the vast majority of such spending would be exempt from that enforcement (as was the case under the BEA's PAYGO framework). As a result, any feasible sequestration would not generate enough reductions in spending to offset the costs of major new spending or revenue initiatives. However, the threat of

sequestration would, in CBO's opinion, probably deter the enactment of legislation that would lead to modest increases in future deficits.

Control of the Budget Process

Compared with the current Congressional pay-as-you-go rules, the statutory PAYGO regime proposed in H.R. 2920 would give the executive branch new authority over the budget process. Certain provisions of the bill would grant specific authority to the executive branch; in particular, OMB would prepare key budget estimates and determine the guidelines for preparing those estimates. Other provisions of the bill are sufficiently ambiguous that they could effectively grant the executive branch additional authority.⁶ Ultimately, those and other changes encompassed by H.R. 2920 would effectively require lawmakers to vote on future legislation without a clear indication of a bill's implications for a potential sequestration.

OMB's Tallying of Sequestration Estimates. Under H.R. 2920, OMB would calculate increases or decreases in the year-end deficit for sequestration purposes. In addition, H.R. 2920 would require OMB to estimate the costs of specific pieces of legislation that would be used in the year-end calculation.

Assigning the calculation of deficit effects to OMB accords with the Constitutional restrictions on legislative branch organizations articulated by the Supreme Court in *Bowsher v. Synar*.⁷ Under the separation-of-powers principles delineated in the *Bowsher* decision, an executive branch agency must maintain a tally of the estimated costs of legislation, calculate the amount to be sequestered, and implement a sequestration. However, there is no Constitutional requirement that the executive branch estimate the costs of individual bills. For the purposes of a statutory PAYGO regime, OMB could be required to use the budget committees' estimates of the costs of legislation.⁸ Indeed, when the Congress was operating under the BEA, it enacted provi-

6. For example, regarding construction of the baseline for mandatory spending, section 9(c) of the bill would require CBO and OMB to assume that "statutory financial insurance guarantees" were fully funded and that "contractual insurance programs" would be sufficiently funded—but it does not define those new terms. Section 9(f) would create a special procedure for legislation in response to "major natural or man-made disasters," but it does not define such disasters. Similarly, the programs that would be exempt from sequestration are left open to interpretation because section 12 of the bill would exempt "activities financed by voluntary payments for goods or services to be provided for such payments."

7. In *Bowsher*, the Supreme Court held that having the Comptroller General, an official accountable to the Congress, trigger sequestrations was unconstitutional because it impermissibly reserved in the Congress postenactment control over the execution of the laws. See 478 U.S. 714, 726 (1986); U.S. Const., art. I, §7, cl. 2.

8. Under current law, the House and Senate Budget Committees determine all estimates used to enforce Congressional budget procedures. To assist the budget committees, CBO analyzes the effects on spending and revenues of specific legislative proposals. Section 201(f) of the Congressional Budget and Impoundment Control Act of 1974 specifies that for purposes of revenue legislation, CBO must use estimates provided by the Joint Committee on Taxation.

sions in at least seven different laws that added or removed balances from the PAYGO scorecard.⁹

For example, the Congress could include an estimate from one of the budget committees as part of the legislation.¹⁰ OMB could then tally those estimates, calculate the total effect on the deficit, and implement a sequestration if necessary. The Constitution requires that before a bill can become a law, it must pass both the House of Representatives and the Senate and be presented to the President for signature.¹¹ Those two requirements are often referred to as “bicameralism” and “presentment.” Because the budget committees’ role would end before the Congress completed action on the legislation and before the legislation was presented to the President, such a process would satisfy both the bicameralism and presentment requirements.

Scoring Rules and Baseline Requirements. H.R. 2920 would grant OMB the authority to specify key guidelines for determining budget estimates. Any PAYGO system requires a set of scorekeeping rules, concepts, and procedures to generate baseline budget projections. Under current law, scorekeeping guidelines and budgetary concepts are modified by unanimous agreement of the House and Senate Budget Committees, CBO, and OMB.¹² Under H.R. 2920, in contrast, OMB would be permitted to develop scorekeeping guidelines after consulting with the budget committees and CBO. The bill would also grant OMB the authority to determine when specific estimating techniques were appropriate and would shield OMB’s assumptions, data, determinations, estimates, and methodology from review in any judicial or administrative proceeding.

9. The seven laws are as follows: Omnibus Budget Reconciliation Act of 1993, Public Law 103-66, §14003(c), 107 Stat. 685; Omnibus Consolidated Appropriations Act, 1997, P.L. 104-208, Division A, §4001, 110 Stat. 3009-500; Balanced Budget Act of 1997, P.L. 105-33, §10213, 111 Stat. 712; Consolidated Appropriations Act, 2000, P.L. 106-113, Division B, §1001(a)-(c), 113 Stat. 1536-1537; Reduction of Preexisting PAYGO Balances, P.L. 107-312, §1, 116 Stat. 2456; Department of Defense Appropriation Act, 2002, P.L. 107-117, Division D, §102, 115 Stat. 2342; and Consolidated Appropriations Act, 2001, P.L. 106-554, §2, 114 Stat. 2763-2764.

10. The cost estimates would not always need to be embedded verbatim in the enacted legislation. Each act of Congress could incorporate the relevant cost estimate by reference as long as the referenced documents were available to the Congress and the President before enactment. See *Hershey Foods Corp. v. United States Department of Agriculture*, 158 F. Supp. 2d (D.D.C. 2001), *aff’d*, 293 F. 3d 520 (D.C. Cir. 2002). As the Comptroller General recently observed, the use of incorporation by reference does not offend the Constitution’s presentment clause or give any power to the Congress that is not already provided in the Constitution. See U.S. Comptroller General, *Opinion of the Comptroller General: Consolidated Appropriations Act, 2008—Incorporation by Reference*, B-316010, at 9 (February 25, 2008).

11. U.S. Const., art. I, §7, cl. 2.

12. See House Committee on the Budget, *Compilation of Laws and Rules Relating to the Congressional Budget Process*, Serial No. CP-3 (November 2008).

Access to Information for Congressional Action. H.R. 2920 would base sequestration on estimates prepared by OMB after a bill's enactment; those estimates could differ from CBO's estimates, which the Congress uses during its consideration of the legislation. Unlike the process in place under the BEA, the PAYGO mechanism proposed in H.R. 2920 would not require OMB to provide "early-warning" reports if cumulative debits on the PAYGO ledger were approaching amounts that might trigger a sequestration. The proposed process would not provide the Congress with sufficient information to understand, before a bill's final passage, how the legislation would affect the potential for a future sequestration.

In addition, H.R. 2920 would grant the President the authority to effectively reject any statutory designation of emergency spending and thus determine whether those amounts would be recorded on the PAYGO ledger. Currently, the designation of spending in proposed legislation as an emergency requirement satisfies the pay-as-you-go rules of the House and Senate. Under H.R. 2920, if the President did not affirm such a designation by the Congress, the PAYGO ledger would reflect greater costs than the Congress had anticipated, thereby increasing the likelihood of a sequestration.

