An Analysis of the President's Budgetary Proposals for Fiscal Year 1983

FEBRUARY 1982

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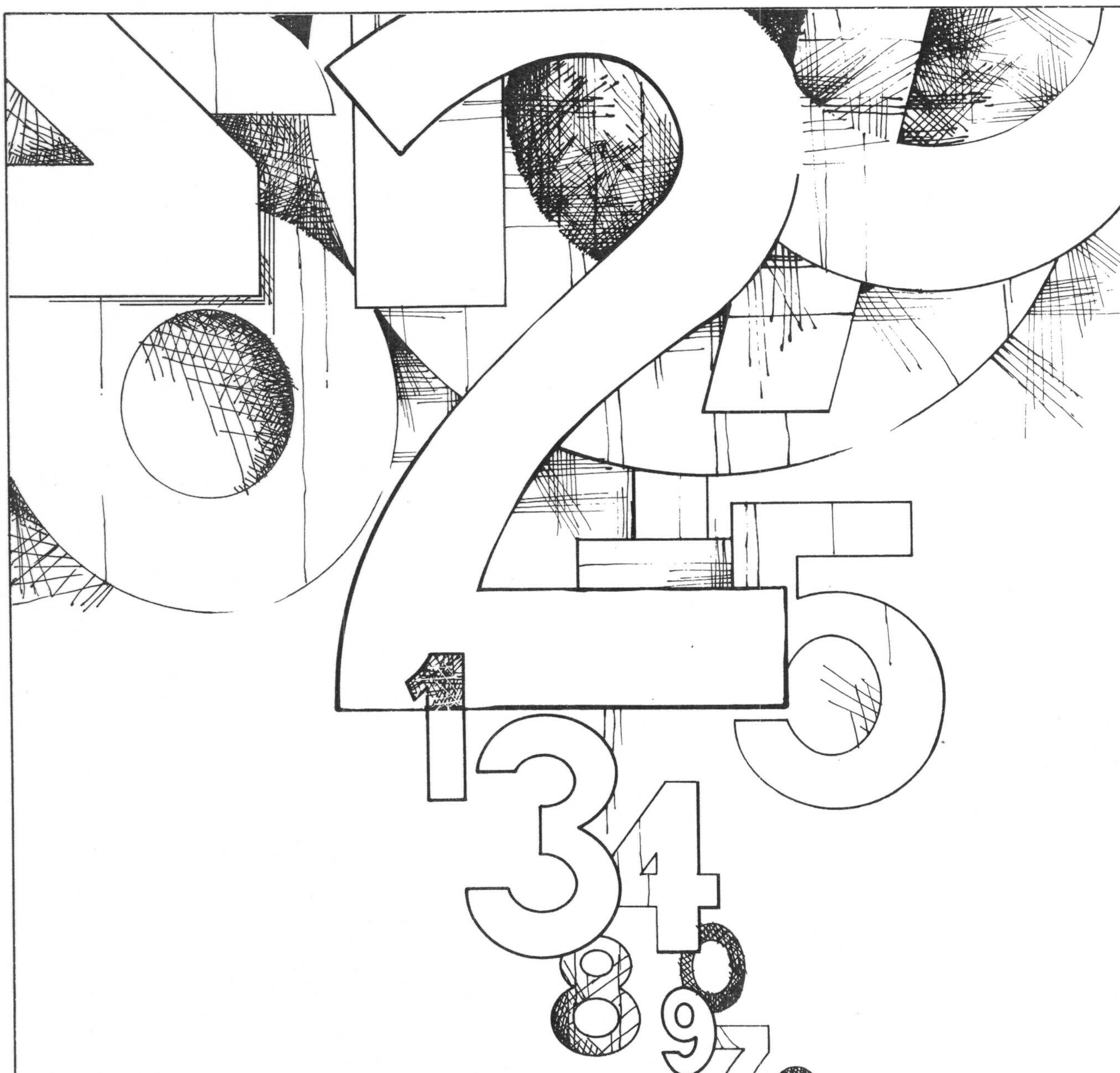
Prepared at the Request of the Senate Committee on Appropriations



CONGRESS OF THE UNITED STATES

CONGRESSIONAL BUDGET OFFICE

AN ANALYSIS OF
THE PRESIDENT'S BUDGETARY PROPOSALS
FOR FISCAL YEAR 1983

The Congress of the United States
Congressional Budget Office

NOTES

Unless otherwise indicated, all years referred to in this report are fiscal years.

Details in the text and tables of this report may not add to totals because of rounding.

ERRATA Sheet

AN ANALYSIS OF THE PRESIDENT'S BUDGETARY PROPOSALS FOR FISCAL YEAR 1983

Page xxv: In Summary Table 7, the 1982 estimate for the debt subject to limit should be \$1,143.0 billion (not \$1,430.0 billion).

Page 74: The last line on this page is missing. It should read: "support basic research in all science and engineering disciplines. For fiscal"

Page 77: In the last sentence of the third paragraph, the Administration's estimate of commercial sales should be \$2.0 billion (not \$2.1 billion).

Page 86: The third stub up from the bottom in the table should read "Free Stock" (not Tree Stock).

Page 110: The last sentence of the fourth paragraph should read: "This would increase projected program costs in 1984 and 1985 by \$279 million and \$364 million."

Page 133: In the table for Function 750: Administration of Justice, the 1984 figure for the President's budget reestimated should be \$4,571 million (not \$4,600 million).

Page 141: The last two sentences in the final paragraph should read: "The deficits resulting from the CBO reestimates (excluding the induced interest costs) exceed the Administration's estimates by about \$12.5 billion in 1982, \$26.1 billion in 1983, \$38.1 billion in 1984, and \$54.3 billion in 1985 (excluding off-budget reestimates). The interest outlays resulting from these higher levels of deficit financing rise from about \$0.7 billion in 1982 to about \$14.5 billion in 1985, as shown in the table at the start of this function."

PREFACE

This analysis was prepared at the request of the Senate Committee on Appropriations to provide Members an overview of the President's budgetary proposals for fiscal year 1983. The report describes the problem of chronic budget deficits faced by the federal government under existing tax laws and current spending programs and the Administration's proposals for dealing with this problem. It discusses the economic outlook and the assumptions used for the February budget.

This report also presents the Congressional Budget Office's reestimates of the budgetary impact of the Administration's proposals based on alternative economic assumptions and on CBO's technical estimating methods and programmatic assumptions. Finally, the report analyzes in some detail the major budget increases proposed for national defense programs.

This report was prepared by the staff of the Budget Analysis, Fiscal Analysis, and Tax Analysis Divisions under the supervision of James L. Blum, William J. Beeman, and James M. Verdier, respectively. Robert L. Faherty, Patricia H. Johnston, Francis S. Pierce, and Johanna Zacharias edited the manuscript. It was typed for publication by Barbara Bakari, Gwen Coleman, Dorleen Dove, Susie Fominaya, Betty Jarrells, Thelma L. Jones, Brice McDaniel, Paula Spitzig, and Nancy Wenzel.

Alice M. Rivlin
Director

February 1982

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SUMMARY

The budget deficit for fiscal year 1982 is now expected to exceed \$100 billion. The sharp rise from previously estimated levels can be attributed largely to the current economic recession, which was not anticipated in last year's budget estimates by either the Administration or the Congress. The economy is expected to recover during 1982 and to move upward thereafter. But budget deficits are projected to increase steadily for the foreseeable future, even after economic recovery, unless existing tax and spending policies change.

The President's 1983 budget contains proposals--mostly affecting spending policies--to reduce projected deficits during the next three years by \$239 billion. According to Administration estimates, adoption of these proposals would result in only marginal reductions in the budget deficit from the record high level of 1982. The Administration anticipates deficits of \$92 billion in 1983, \$83 billion in 1984, and \$72 billion in 1985, all substantially above the 1981 level of \$58 billion.

The Congressional Budget Office (CBO) has analyzed the President's budgetary proposals and finds that revenues are likely to be slightly lower than projected by the Administration and outlays significantly higher. Hence, even if the President's proposals are adopted, CBO estimates that the budget deficit will climb steadily from an estimated \$111 billion in 1982 to \$121 billion in 1983, \$129 billion in 1984, and \$140 billion in 1985. Furthermore, there is the possibility that the budget deficits could be even larger, if tight credit conditions produce a weaker economy than assumed by either the Administration or CBO.

THE BUDGET OUTLOOK UNDER CURRENT POLICIES

Under existing law, the future growth in federal revenues will be sharply reduced from rates experienced over the past decade as a result of the tax cuts contained in the Economic Recovery Tax Act of 1981. Without further cuts in spending, budget outlays will grow at a faster rate than revenues. Consequently, without steps to raise revenues or to lower the growth in spending, the budget deficit will continue to grow.

This budget outlook is portrayed clearly by both the CBO baseline budget projections and the Administration's projection of current services (which includes the Administration's defense spending proposals). These projections are shown in Summary Table 1.

SUMMARY TABLE 1. THE BUDGET OUTLOOK UNDER CURRENT POLICIES (By fiscal year, in billions of dollars)

	1981 Actual	1982 Estimate	Projections 1983	1984	1985
CBO Baseline Projections					
Revenues	602	631	652	701	763
Outlays	660	740	809	889	971
Deficit	58	109	157	188	208
Administration Current Services Baseline with Proposed Defense Spending Growth a/					
Revenues	599	626	653	704	778
Outlays	657	728	799	869	946
Deficit	58	101	146	165	168

a/ The President's 1983 budget has reclassified certain social insurance contributions as offsetting collections to spending, thereby reducing both revenues and outlays but leaving unchanged the deficit.

The budget deficit under baseline assumptions is projected by CBO as almost doubling between 1982 and 1985, from $109 billion to $208 billion. The Administration's projections also show a sharp rise in the budget deficit during this period, although not quite so much as CBO's, largely because of different economic assumptions. In the absence of tax increases or spending reductions, the CBO projections show the deficit rising to 5.0 percent of GNP in both 1984 and 1985; the Administration's show it rising to 4.3 percent of GNP in 1984 and 4.0 percent in 1985. The last time the budget deficit was this large relative to GNP was in 1976 when it was 4.0 percent as a result of the 1974 recession.

THE ADMINISTRATION'S BUDGETARY PROPOSALS

President Reagan's budget for fiscal year 1983 recommends outlays of $757.6 billion, revenues of $666.1 billion, and a unified budget deficit of $91.5 billion. The main features of the President's 1983 budget include:

- No change in the scheduled individual income tax cuts enacted in 1981, but some significant increases in corporate taxes;

- Rapid real growth in defense spending;

- Further reforms in entitlement programs, but no reductions in Social Security benefits;

- Additional cuts in discretionary nondefense spending programs; and

- Substantial savings from various management initiatives.

Total revenues under the Administration's proposals would increase by 27 percent from an estimated $627 billion in 1982 to $797 billion in 1985. Outlays would grow by only 20 percent, from an estimated $725 billion in 1982 to $869 billion in 1985. Net spending by off-budget entities--primarily the Federal Financing Bank and oil purchases for the strategic petroleum reserve--is projected to decline from an estimated $20 billion in 1982 to $11 billion by 1985. As shown in Summary Table 2, the total budget deficit--including off-budget entities--would decline by 30 percent from $118 billion in 1982 to $83 billion in 1985. Relative to GNP, however, the reduction in the total deficit would be larger--falling from 3.8 percent in 1982 to 2.0 percent in 1985. The federal debt subject to statutory limit is projected to grow from $1.0 trillion at the end of fiscal year 1981 to $1.5 trillion by the end of 1985.

The Administration's Budget Deficit Reduction Program

The Administration's proposals to reduce the size of the federal deficit from the levels indicated by current policies are concentrated largely on the spending side of the budget. As shown in Summary Table 3, almost 80 percent of the deficit reduction proposals over the next three years are calculated as reductions in outlays from the Administration's projected current services baseline. The biggest share of the outlay reductions--40 percent--would be accomplished largely through the appropriation process by holding back increases or cutting nondefense discretionary programs. Another 29 percent of these outlay reductions are to be achieved through legislative proposals to reform entitlement programs, primarily Medicare, Medicaid, food stamps, and Aid to Families with Dependent Children (AFDC). No entitlement reforms for Social Security are proposed in the President's budget.

SUMMARY TABLE 2. THE ADMINISTRATION'S BUDGET ESTIMATES (By fiscal year, in billions of dollars)

Budget Component	Actual 1981	Administration Estimates 1982	1983	1984	1985
Revenues	599.3	626.8	666.1	723.0	796.6
Outlays					
Unified budget	657.2	725.3	757.6	805.9	868.5
Off-budget entities	21.0	19.7	15.7	14.3	11.0
Total Outlays	678.2	745.0	773.3	820.2	879.4
Deficit (-)					
Unified budget	-57.9	-98.6	-91.5	-82.9	-71.9
Off-budget entities	-21.0	-19.7	-15.7	-14.3	-11.0
Total Deficit	-78.9	-118.3	-107.2	-97.2	-82.8
Debt Subject to Limit	998.8	1,130.0	1,254.3	1,368.7	1,482.0

An estimated 28 percent of outlay savings would be achieved through various management initiatives, such as accelerated leasing of Outer Continental Shelf (OCS) lands, the sale of surplus or underused federal property, improved debt collection procedures, and further restraint on increases in federal pay. Fully two-thirds of these management initiatives would reduce net outlays by increasing receipts that are recorded on the spending side of the budget. Finally, proposed increases in user fees that would be counted as offsetting receipts make up the remaining 3 percent of the proposed outlay savings.

Only a little more than 20 percent of the Administration's deficit reduction proposals involve revenue increases. About 75 percent of the increases during 1983-1985 would come in corporate income taxes, and would substantially offset the corporate tax reduction enacted in the Economic Recovery Tax Act (ERTA) for that period. No proposals are made in the February budget to delay or eliminate any of the scheduled rate reductions in individual income taxes that also were enacted in ERTA.

SUMMARY TABLE 3. THE ADMINISTRATION'S DEFICIT REDUCTION PROPOSALS (By fiscal year, in billions of dollars) a/

	1983	1984	1985	Total	Percent
Revenues					
Tax revisions	7.2	13.5	13.5	34.1	14.3
Increases in user fees	1.3	1.4	1.6	4.3	1.8
Improved tax collection and enforcement	5.5	5.5	4.7	15.7	6.5
Entitlement reform	-1.1	-1.0	-1.0	-3.1	-1.3
Subtotal	12.8	19.4	18.8	51.0	21.3
Outlays					
Entitlement savings	12.8	18.1	23.8	54.7	22.8
Management initiatives	14.8	18.5	19.2	52.5	22.0
Increases in user fees	1.2	2.1	2.2	5.5	2.3
Reductions in discretionary and other programs	14.2	26.1	35.3	75.6	31.6
Subtotal	43.0	64.7	80.5	188.3	78.7
Total Reductions a/	55.9	84.1	99.3	239.3	100.0

a/ Reductions are calculated by the Administration as changes from a projected current services baseline (see Summary Table 1).

Defense Spending Proposals

The President's February budget includes a 1982 program supplemental appropriation request of \$2.6 billion for the Defense Department, and

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proposes a further increase of $44 billion in national defense appropriations for 1983. The Administration's 1983 budget for national defense programs totals $263 billion in new budget authority. Further large increases in defense appropriations are projected for 1984 and 1985. Measured in constant (fiscal year 1983) dollars, these projected increases for national defense appropriations for 1983-1985 would mean an average real growth of 9.2 percent per year using the Administration's economic assumptions.

Overall, the President's 1983 budget reflects relatively small funding increases for forces and manpower, and large increases to acquire new weapons for future force expansion and modernization. The most significant new policy proposal is the Administration's plan to increase the size of the naval fleet from 514 ships to over 600.

Restructuring of the Federal Budget

The President's budget proposals would dramatically affect the relative composition of federal spending. Outlays for national defense would increase by 56 percent in the next three years--from $187.5 billion in 1982 to $292 billion in 1985. The share of the budget allocated to national defense would rise sharply from 26 percent in 1982 to 34 percent in 1985. Direct federal payments to individuals, which include Social Security, Medicare, and federal employee retirement benefits, would increase by $57 billion between 1982 and 1985--maintaining their relative share of the budget at about 42 percent. Net interest costs are also projected to rise during the next three years and would claim another 11 percent of total outlays in 1985, the same share as estimated for 1982.

All other federal spending would be reduced by 25 percent--about $37 billion--between 1982 and 1985. As shown in Summary Table 4, payments for individuals made through state and local governments--which include Medicaid and AFDC--would be cut back in 1983 from 1982 levels and then allowed to grow slightly in 1984 and 1985. Outlays for other grants to states and localities would be reduced steadily from about $50 billion in 1982 to $41 billion in 1985. Net outlays for "all other federal programs" would have the sharpest cutback, falling by more than one-half, from an estimated $54 billion in 1982 to $25 billion in 1985. This decline, however, masks a projected 60 percent increase in offsetting receipts from the sale of OCS leases, surplus federal property, and other sources. Gross outlays for this sector would be cut back in 1983 by about 15 percent but then held approximately level in current dollars during 1984 and 1985.

SUMMARY TABLE 4. RELATIVE COMPOSITION OF THE UNIFIED BUDGET (By fiscal year)

Budget Component	Actual 1981	Administration Estimates 1982	1983	1984	1985
		Outlays in Billions of Dollars			
National Defense	159.8	187.5	221.1	253.0	292.1
Payments for Individuals					
Direct	276.7	310.1	328.3	345.4	367.5
Through states and localities	39.9	41.5	37.6	40.0	42.3
Other Grants	54.8	49.6	43.7	41.8	41.1
Net Interest	68.7	83.0	96.4	98.7	100.8
Other Federal Programs	57.4	53.6	30.6	27.1	24.6
Total	657.2	725.3	757.6	805.9	868.5
		Percent Change			
National Defense	17.6	17.4	17.9	14.4	15.4
Payments for Individuals					
Direct	16.8	12.1	5.9	5.2	6.4
Through states and localities	16.9	3.9	-9.5	6.4	5.9
Other Grants	-4.3	-9.3	-11.9	-4.4	-1.7
Net Interest	31.0	20.8	16.1	2.4	2.1
Other Federal Programs	-4.5	-6.5	-43.0	-11.2	-9.2
Total	14.0	10.4	4.5	6.4	7.8

CBO ANALYSIS OF THE PRESIDENT'S BUDGET

The Congressional Budget Office's analysis of the President's February budget finds that revenues would be slightly lower than estimated by the Administration for 1983-1985 and budget outlays would be higher. This finding results from CBO's technical analysis of the Administration's budget estimates and a substitution of CBO's economic assumptions for the Administration's. The CBO budget reestimates are shown in Summary Table 5.

SUMMARY TABLE 5. CBO BUDGET REESTIMATES (By fiscal year, in billions of dollars)

	1982	1983	1984	1985
CBO Technical Reestimates				
Revenues	4.3	-5.2	-13.0	-15.6
Outlays				
Unified budget	12.2	19.9	22.1	23.0
Off-budget entities	0.6	0.8	0.9	1.1
CBO Baseline Economic Assumptions				
Revenues	-3.4	-0.8	5.6	-4.9
Outlays	1.2	3.2	16.4	24.2
Total Reestimates				
Revenues	0.9	-6.0	-7.4	-20.5
Outlays				
Unified budget	13.5	23.1	38.5	47.2
Off-budget entities	0.6	0.8	0.9	1.1

These reestimates produce a dramatic increase in the budget deficit, as shown in Summary Table 6 and as portrayed graphically in Summary Figure 1. Under CBO's technical and economic reestimates, the unified budget deficit rises from $111 billion in 1982 to $140 billion by 1985, almost twice the level projected by the Administration. Over the three-year period, 1983 to 1985, CBO estimates that the President's budgetary proposals would result in budget deficits that exceed the Administration's estimates by more than $140 billion. Almost $100 billion, or about 70 percent, of these higher deficits results from technical estimating differences. Another $44 billion results from using CBO's baseline economic assumptions instead of the Administration's.

SUMMARY TABLE 6. UNIFIED BUDGET DEFICITS (By fiscal year, in billions of dollars)

	1982	1983	1984	1985
President's February Budget	98.6	91.5	82.9	71.9
Deficit with CBO's Technical Reestimates	106.5	116.6	118.1	110.4
Deficit with CBO's Technical Reestimates and Baseline Economic Assumptions	111.1	120.6	128.9	139.6

CBO Technical Reestimates

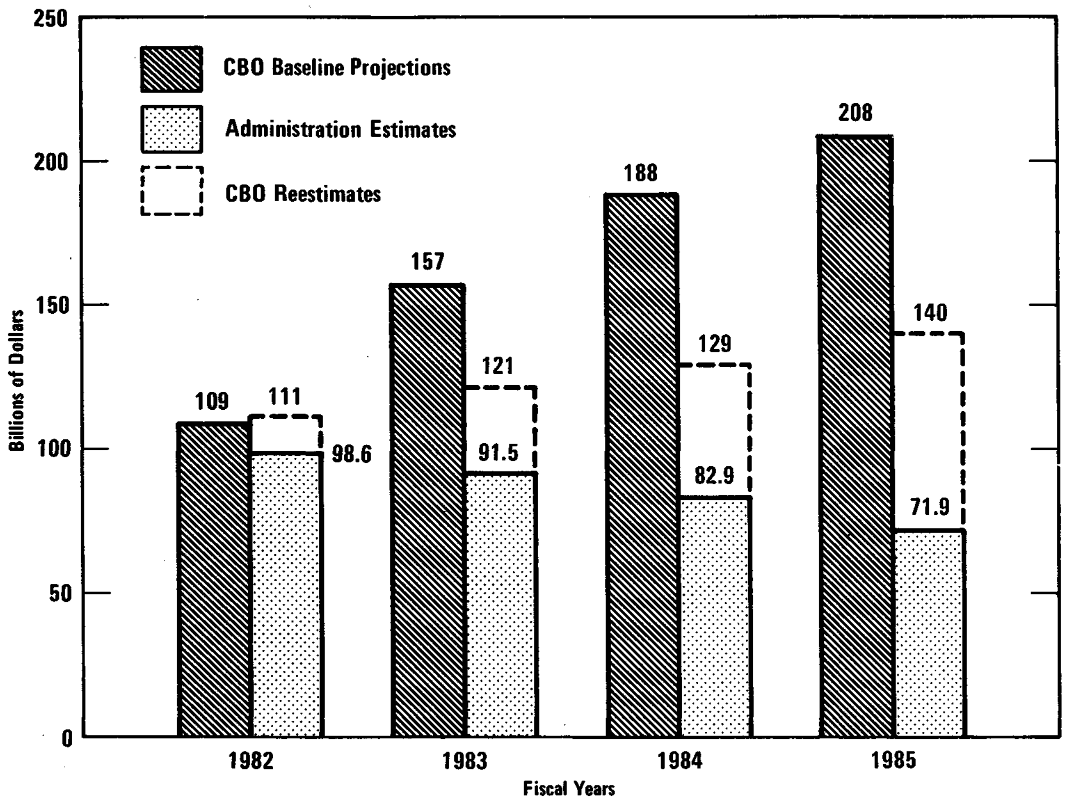
CBO's technical analysis of the Administration's budget estimates suggests that revenues may be overestimated in the February budget by about $5 billion in 1983, $13 billion in 1984, and $16 billion in 1985. The technical reestimates for revenues result mainly from different estimates of the revenue effects of the Economic Recovery Tax Act. On the outlay side, CBO's technical reestimates suggest larger differences, averaging more than $20 billion during 1983-1985. The major differences involve the cost of farm price supports, the rate of spending for defense procurement activities, likely receipts to be derived from the proposed accelerated leasing of OCS lands, and net interest costs. These four areas account for three-fourths of all the differences in CBO's technical reestimates for 1983-1985 outlays.

CBO Economic Reestimates

The economic forecasts of both the Administration and CBO are in close agreement for 1982. Real gross national product (GNP) is projected to rise by about 3 percent over the four quarters of the year, and the unemployment rate is expected to be in the neighborhood of 8½ percent at year's end. The forecasts of inflation and short-term interest rates are also similar in 1982.

In 1983, however, the Administration forecast for inflation and real growth is more optimistic than CBO's. While both forecasts imply virtually the same expansion of nominal GNP, the Administration looks for real GNP to grow by 5.2 percent over the four quarters of 1983, and for inflation (as measured by the GNP deflator) to fall to a rate of 5.5 percent. CBO expects real GNP to grow by about 1½ percentage points less than the Administration does in 1983, and the GNP deflator to rise by about 1½ percentage points more. The slower growth expected by CBO is largely the consequence of higher interest rates in its forecast, which would dampen the recovery in economic activity.

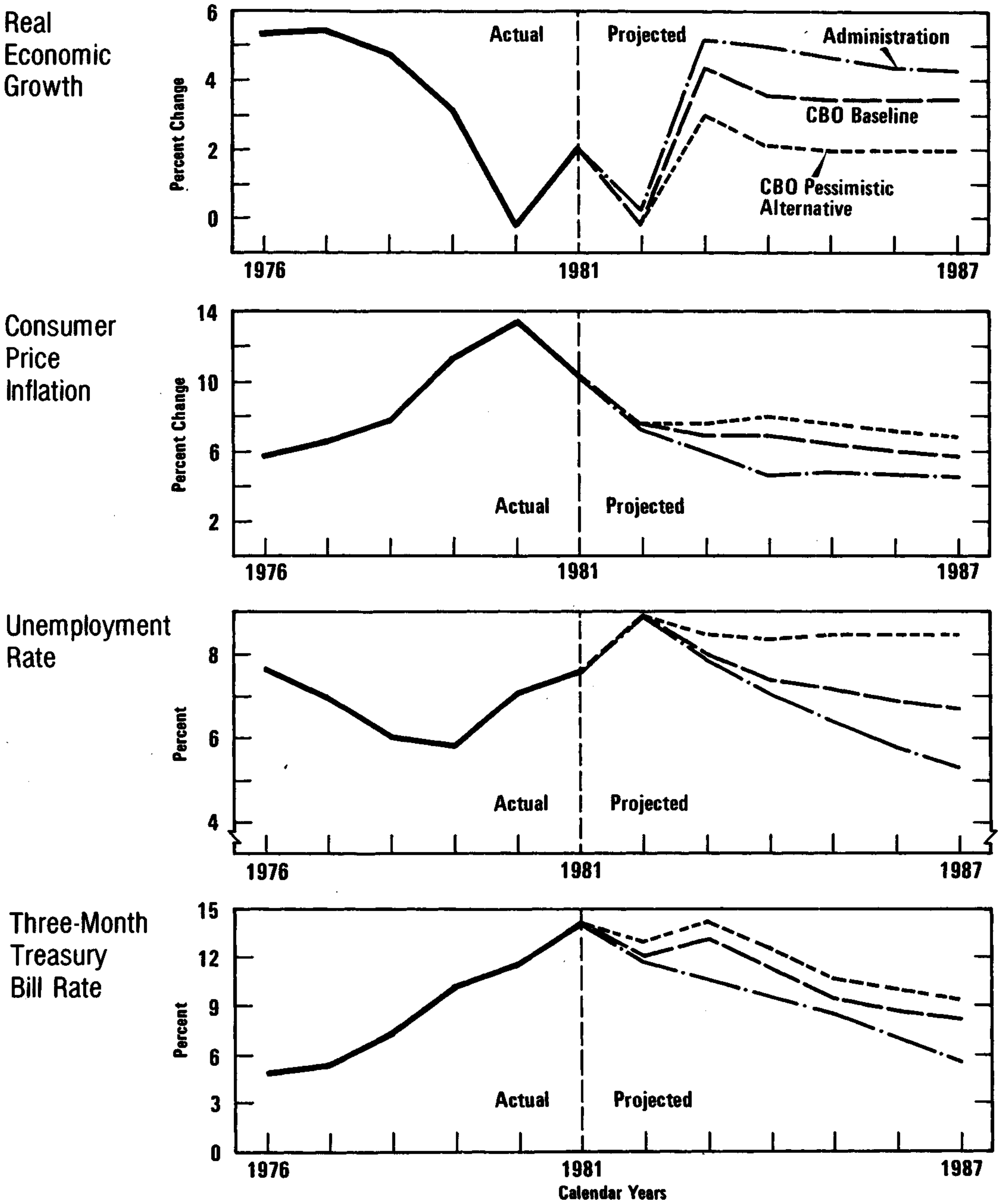
Summary Figure 1.
Budget Deficits



The Administration's economic assumptions for 1984 and beyond are also more optimistic than CBO's (see Summary Figure 2). Compared with CBO's baseline assumptions, the Administration projects higher real growth and sharper declines in inflation, unemployment, and interest rates.

Summary Figure 2.

Comparison of Major Economic Assumptions



SOURCES: For historical data, Department of Commerce, Bureau of Economic Analysis; Department of Labor, Bureau of Labor Statistics; and Federal Reserve System, Board of Governors. For projections, Congressional Budget Office and Office of Management and Budget.

The Administration's real growth assumptions for 1984-1987 are near the upper end of historical experience. In comparable four-year periods following previous postwar recoveries, real growth averaged 3.4 percent a year and ranged between 2.0 and 5.2 percent a year. The Administration assumes an average rate of growth of 4.6 percent a year between 1984 and 1987. CBO, in its baseline projections, assumes an average annual growth rate of 3.5 percent.

As shown in Summary Table 5, the effect of the somewhat less optimistic CBO baseline assumptions with respect to real growth, inflation, unemployment, and interest rates would be to raise unified budget outlays by $1 billion in 1982, $3 billion in 1983, over $16 billion in 1984, and $24 billion in 1985. Over the entire four-year period, budget outlays would be $45 billion higher than projected by the Administration. Revenues, on the other hand, would be very close to the Administration's estimates because of the similar assumptions about nominal GNP.

The Administration's Budget Reestimated

The CBO economic and technical reestimates assume that all of the President's legislative proposals for taxes and spending are approved by the Congress, and also that the Administration is successful in meeting most of its targets for revenue increases and outlay savings from various management initiatives. CBO has not been able to develop its own independent estimates for outlay savings from several of the management initiatives, particularly those that are clearly targets and not allocated to agency accounts. Based on past history, the unallocated targets for reduction of waste, fraud, and abuse; for improved debt collection; and for the sale of surplus or underused federal property appear to be very optimistic.

Summary Table 7 shows the effect on the Administration's budget of CBO's technical reestimates and of substituting CBO's baseline economic assumptions for the Administration's economic assumptions. Under CBO's pricing of the Administration's budgetary proposals, revenues would grow by less than 25 percent between 1982 and 1985, rising from an estimated $628 billion to $776 billion. Unified budget outlays would grow at approximately the same rate as revenues during this period, rising by 24 percent from $739 billion in 1982 to $916 billion in 1985.

The unified budget deficit rises from $111 billion in 1982 to $140 billion in 1985. When net outlays of off-budget federal entities are included, the total deficit rises from $131 billion in 1982 to more than

$1.0 trillion at the end of 1981 to more than $1.6 trillion at the end of 1985, or by more than 60 percent.

SUMMARY TABLE 7. THE ADMINISTRATION'S BUDGET REESTIMATED (By fiscal year, in billions of dollars)

	Actual 1981	CBO Estimates 1982	1983	1984	1985
Revenues	599.3	627.7	660.1	715.6	776.1
Outlays					
Unified budget	657.2	738.8	780.7	844.5	915.7
Off-budget entities	21.0	20.2	16.5	15.2	12.0
Total Outlays	678.2	759.0	797.2	859.7	927.7
Deficit (-)					
Unified budget	-57.9	-111.1	-120.6	-128.9	-139.6
Off-budget entities	-21.0	-20.2	-16.5	-15.2	-12.0
Total Deficit	-78.9	-131.3	-137.1	-144.1	-151.6
Debt Subject to Limit	998.8	1,430.0	1,297.1	1,458.4	1,640.5

MAJOR RISKS

Several risks are inherent in the Administration's budget proposals. One is that the Administration may have underpriced its projected defense appropriation requests. CBO has identified two major elements of concern in this regard. First, inflation may not decline as rapidly as assumed in the Administration's budget estimates. This would require additional funds to complete the Administration's plans for defense purchases. Otherwise, higher than anticipated inflation could cause a scaling back of purchases to stay within available funds. CBO's reestimates of the President's budget did not adjust the Administration's proposed budget authority for defense programs for the higher inflation contained in CBO's baseline economic assumptions. If this were done, \$61 billion in additional appropriations would be needed during the next five years to achieve the same real growth in defense spending as proposed by the Administration.

Second, the real cost of defense purchases has grown in recent years--averaging about 3½ percent per year since 1975. This has occurred for a variety of reasons, including program changes (such as new specifications for weapons or revised production schedules) and underestimates of real resources (such as manufacturing hours and materials costs). If the Administration is unable to curb this cost growth, further funds would be needed to meet its defense procurement objectives. If the 3½ percent average annual cost growth continues, for example, CBO estimates that an additional \$48 billion in new budget authority will be required to fund major weapons procurement during 1983-1987.

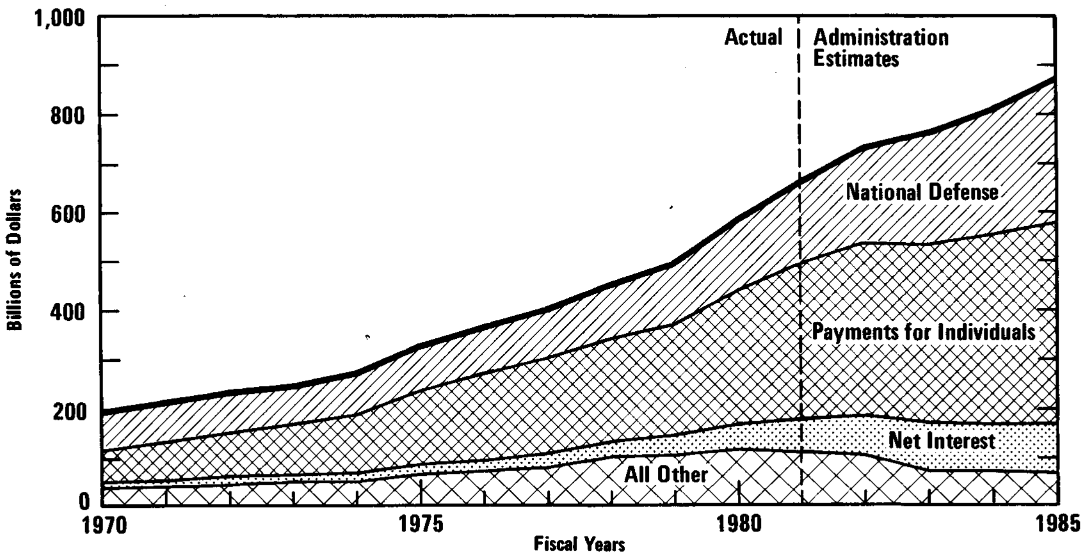
A second risk is that it will be very difficult to achieve lower deficits in the next few years if the major effort is focused primarily on the spending side of the budget. The sharp increases proposed for national defense programs, the rising outlays for Social Security and other benefit payments indexed for inflation, and the growing net interest costs place enormous pressure on the remaining portion of the budget. As shown in Summary Figure 3, these other federal outlays are projected to shrink steadily. The difficulty of finding still further significant reductions in this area of the budget is very great.

A more fundamental risk is the uncertainty in the economic outlook. The Administration's program implies a strong fiscal stimulus in 1982 and 1983. The large budget deficits projected in this report would result in a marked increase in Treasury borrowing that would put further upward pressure on interest rates. At the same time, the Federal Reserve's targets for monetary growth may act as a brake on economic growth during the next few years. Given the combination of monetary and fiscal policies and the projected economic recovery, high interest rates next year seem likely--although the level is hard to predict because this policy combination of a tight monetary policy and a stimulative fiscal policy is virtually without precedent. Nevertheless, there is a significant risk that the outcome could be even weaker growth than projected by either the Administration or CBO.

Since budget estimates are very sensitive to economic assumptions, policymakers must be prepared for the possibility of developments markedly different from those assumed by both the Administration and CBO. To illustrate the sensitivity of the budget to economic assumptions, CBO also has reestimated the President's February budget using a more pessimistic set of economic assumptions. In the CBO pessimistic alternative assumptions, portrayed in Summary Figure 2, real growth averages only 2.0 percent in 1984-1987, unemployment remains at about 8½ percent throughout the period, the rate of inflation remains above 7 percent until the end of the period, and short-term interest rates fall very slowly.

Summary Figure 3.

Federal Budget Outlays



SOURCE: *Budget of the United States Government, Fiscal Year 1983,* Table 22, p. 9-61.

Under this more pessimistic set of assumptions, growth in nominal incomes would be somewhat less and federal revenues would be lower by about $25 billion during 1982-1985 than projected by the Administration. The effect on outlays, however, would be much greater. By 1985, outlays would be over $50 billion higher than projected by the Administration, and over $100 billion higher for the entire four-year period. The effect of using the CBO pessimistic economic assumptions would be to raise the estimated level of the budget deficit under the Administration's proposals to $132 billion in 1983, $155 billion in 1984, and $184 billion in 1985 (see Summary Table 8).

SUMMARY TABLE 8. UNIFIED BUDGET DEFICITS UNDER CBO PESSIMISTIC ECONOMIC ASSUMPTIONS (By fiscal year, in billions of dollars)

	1982	1983	1984	1985
President's February Budget	98.6	91.5	82.9	71.9
Deficit with CBO Technical Reestimates	106.5	116.6	118.1	110.4
Deficit with CBO Technical Reestimates and Pessimistic Economic Assumptions	112.7	132.1	154.9	183.6

AN ANALYSIS OF

THE PRESIDENT'S BUDGETARY PROPOSALS

FOR FISCAL YEAR 1983

CHAPTER I. THE ADMINISTRATION'S PROPOSALS

The federal government's budget, in the absence of major policy changes, faces large and growing deficits. This year, the deficit will probably exceed $100 billion for the first time. By 1985, it could top $200 billion.

The President's 1983 budget contains a lengthy list of spending reductions and a shorter list of tax increases designed to close the deficit gap. To allow substantial increases in spending for national defense, spending for nondefense programs (other than Social Security) would be cut sharply. The Administration also recommends large reductions in off-budget federal spending and in federal credit activities.

This chapter depicts the budget situation under current policies, using both Congressional Budget Office (CBO) and Administration projections, and explains how that situation came about. It then reviews the Administration's revenue and spending proposals, using the Administration's own figures. The chapter concludes with discussions of the Administration's proposals for federal off-budget spending, debt, and credit. The later chapters present CBO's estimates of revenues and spending under the Administration's policies, using CBO's own economic assumptions and estimating methods.

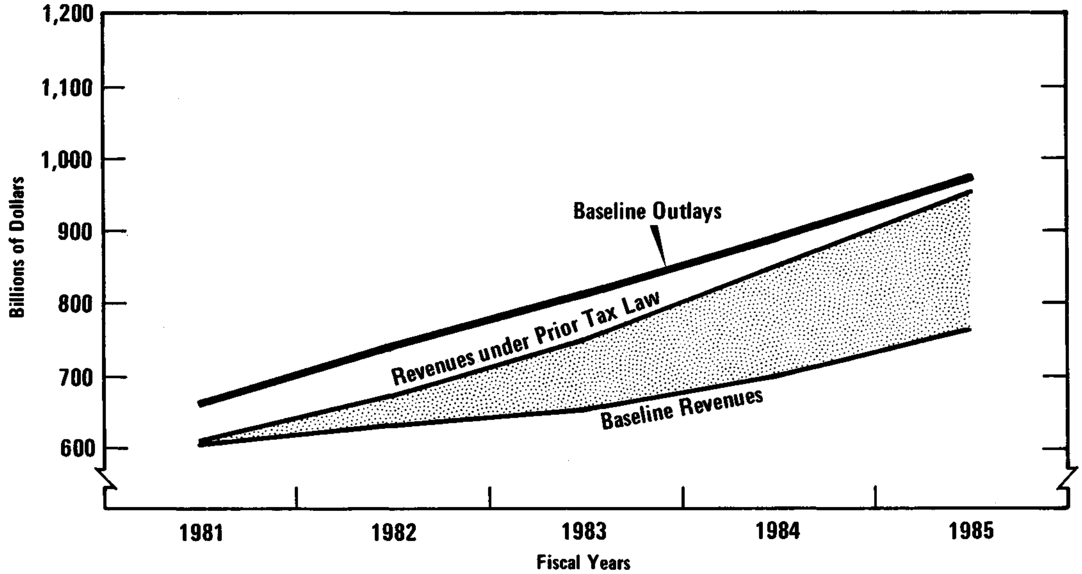
THE BUDGET OUTLOOK UNDER CURRENT POLICIES

While the budget deficit for 1981 was $58 billion, the 1982 deficit is now expected to exceed $100 billion under current policies. This sharp rise in the deficit can be attributed largely to the recession, which was not anticipated in last year's budget estimates. Although most economic forecasters expect that the economy will begin to recover later this year and move into a period of continued growth, budget projections show rising deficits under existing tax laws and current spending policies. This growing deficit gap is illustrated in Figure 1, which shows the CBO baseline budget projections through 1985.

Both the CBO baseline budget projections and the Administration's current services baseline (which includes the Administration's defense spending proposals) tell the same story. Under both sets of baseline projections, shown in Table 1, federal revenues would grow at an average annual rate several percentage points below the expected rate of growth of

Figure 1.

CBO Baseline Budget Projections



SOURCE: Congressional Budget Office.

the economy. Both CBO and the Administration assume that the gross national product (GNP) will grow by an average rate of between 10.5 and 11 percent during the next three years. The CBO baseline projections show revenues growing at an average annual rate of 6.5 percent between 1982 and 1985--somewhat less than the Administration's baseline projections of 7.5 percent.

Baseline outlays, as projected by both CBO and the Administration, would grow at a faster rate than revenues. The CBO projections show total outlays rising from an estimated $740 billion in 1982 to $971 billion in 1985. This represents an average growth rate of 9.5 percent a year, or 3 percentage points above the CBO projected growth in baseline revenues. The Administration projects a similar growth in baseline outlays--9.2 percent a year--that exceeds its baseline revenue projections by almost 2 percentage points.

The budget deficit under baseline assumptions is projected by CBO to almost double between 1982 and 1985--rising from $109 billion to $208 billion. The Administration's baseline projections also show a sharp rise in the budget deficit, although not quite as much as those of CBO,

TABLE 1. THE BUDGET OUTLOOK UNDER CURRENT POLICIES (By fiscal year, in billions of dollars)

	Actual 1981	Estimate 1982	Projections 1983	1984	1985
		CBO's Baseline			
Revenues	603	631	652	701	763
Outlays	660	740	809	889	971
Deficit	58	109	157	188	208
		Administration's Current Service Baseline a/			
Revenues b/	599	626	653	704	778
Outlays b/	657	728	799	869	946
Deficit	58	101	146	165	168

SOURCES: Congressional Budget Office, Baseline Budget Projections for Fiscal Years 1983-1987 (February 1982), p. 9; Budget of the United States Government, Fiscal Year 1983 (February 1982), p. 3-8.

a/ Includes proposed defense spending growth.

b/ The Administration's 1983 budget has reclassified certain social insurance contributions as offsetting collections to spending, thereby reducing both revenues and outlays but leaving the deficit unchanged. The CBO figures reflect the previous classification.

largely because of different economic assumptions. In the absence of tax increases or spending reductions, CBO's baseline projections show the deficit rising to 5.0 percent of GNP in both 1984 and 1985. The Administration's baseline projections show the deficit rising to 4.3 percent of GNP in 1984 and 4.0 percent in 1985. The last time the budget deficit was this large was in 1976, as a result of the 1974-1975 recession.

These baseline projections are quite different from those of the past. In previous baseline projections, revenues grew faster than outlays, and the

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budget began to show a surplus within two or three years. Projected revenues grew more rapidly than the economy, because inflation and economic growth pushed individuals into higher income tax brackets. Projected outlays, on the other hand, grew more slowly than GNP, because most spending was assumed merely to keep pace with inflation.

In the new baseline projections, revenues grow less rapidly than the economy. The projected lower revenue growth results primarily from the individual and corporation income tax cuts enacted in the Economic Recovery Tax Act of 1981 (ERTA). As shown in Table 2, federal revenues will be as much as $189 billion lower in 1985 than they would have been had the 1981 Tax Act not been enacted. The effect of the Tax Act will be to reverse the trend of a growing federal tax burden. Between 1976 and 1981, federal revenues rose from 18.2 percent to 21.0 percent of GNP. Under the current tax law, both the CBO and the Administration project a decline in revenues relative to GNP, to under 19 percent by 1985.

TABLE 2. ESTIMATED REVENUE LOSSES RESULTING FROM THE ECONOMIC RECOVERY TAX ACT OF 1981 (By fiscal year, in billions of dollars)

	1981	1982	1983	1984	1985
CBO Estimates	2	39	95	148	189
Administration Estimates	*	38	92	139	177

SOURCES: Congressional Budget Office, Baseline Budget Projections for Fiscal Years 1983-1987, p. 25; Budget of the United States Government, Fiscal Year 1983, p. 4-10.

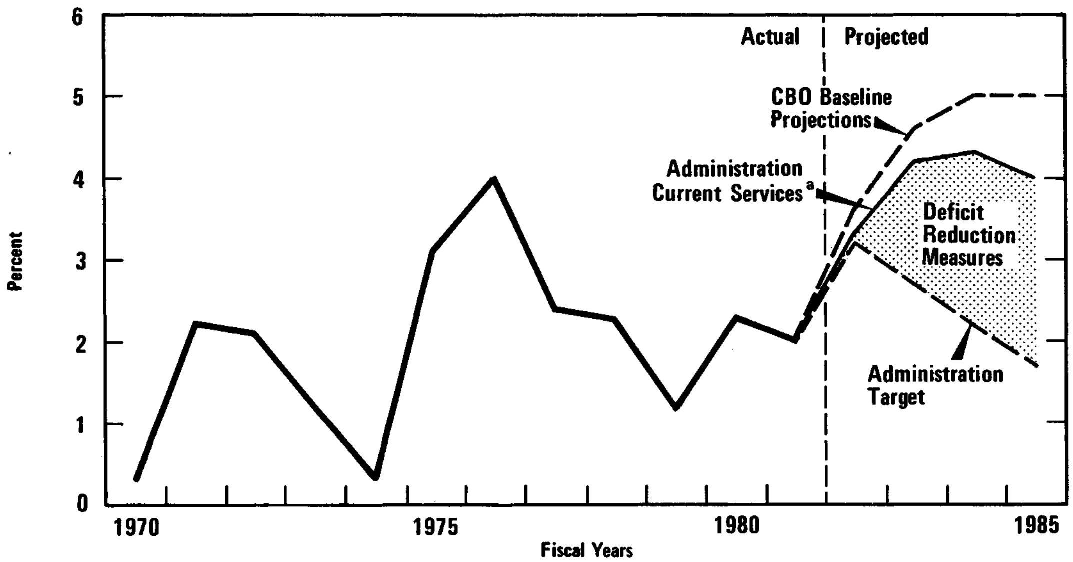
*Less than $500 million.

The price of this reduction in the tax burden is the widening gap between revenues and outlays. Figure 1 shows graphically that revenues under prior tax law would have been sufficient virtually to eliminate the projected deficits by 1985. Under current law, however, the deficits are projected to grow.

THE ADMINISTRATION'S BUDGET PROPOSALS

The Administration's 1983 budget includes a package of measures designed to reduce the federal deficit gradually over the next few years. If these proposals are adopted, the Administration projects that the deficit would decline from 3.2 percent of GNP in 1982 to 2.7 percent in 1983, 2.2 percent in 1984, and 1.7 percent in 1985. In the absence of such policy changes, the deficit by 1985 would widen to 4 or 5 percent of GNP, as shown in Figure 2.

Figure 2.
Federal Budget Deficit as a Percentage of GNP



[a] Includes Administration defense spending proposals.

SOURCES: *Budget of the United States Government, Fiscal Year 1983,* p. 3-8, and Table 21, p. 9-60; Congressional Budget Office, *Baseline Budget Projections for Fiscal Years 1983-1987* (February 1982).

The Administration's budget and the proposed deficit reduction measures represent a continuation of the policies that the Administration recommended, and that were in large part enacted, last year. Defense appropriations would grow rapidly. The major individual income tax reductions passed in 1981 would be left in place. Revenues would be modestly increased compared to the baseline, primarily through the elimination of tax provisions benefiting a few specific industries and through the improved collection of existing taxes. The proposed revenue increases and spending reductions total $242 billion over the 1982-1985 period (see Table 3). Of this amount, revenue increases comprise $50 billion, or about one-fifth, and spending reductions constitute the remaining four-fifths.

TABLE 3. THE ADMINISTRATION'S PROPOSED DEFICIT REDUCTION MEASURES (By fiscal year)

	1982	1983	1984	1985
	In Billions of Dollars			
Administration's Baseline Deficit with Proposed Defense Spending Growth	101	146	165	168
Less: Proposed Revenue Increases	*	-13	-19	-18
Proposed Spending Reductions	-3	-43	-65	-81
Total Deficit Reduction Measures	-3	-56	-84	-99
Plus: Proposed Spending Increases	*	2	2	3
Administration Deficit Target	99	92	83	74
	As a Percent of GNP			
Administration's Baseline Deficit with Proposed Defense Spending Growth	3.3	4.2	4.3	4.0
Administration's Deficit Target	3.2	2.7	2.2	1.7

SOURCE: Budget of the United States Government, Fiscal Year 1983, p. 3-8.

*Less than $500 million.

The spending reductions proposed by the Administration do not touch Social Security cash benefits, the single largest nondefense spending program, or interest costs on the national debt, which depend on the level of debt outstanding and on market interest rates and cannot be directly affected by policy changes. As a result, the proposed spending reductions would cut deeply into federal grants to state and local governments and into spending on the day-to-day domestic operations of the federal government.

Revenue Proposals

The Administration's revenue proposals, listed in Table 4, would increase revenues by about $13 billion in fiscal year 1983 and by roughly $18 billion in 1985, according to Administration estimates. Extension of the highway trust fund taxes beyond their current expiration date, already assumed in Administration and CBO baseline revenues, would yield an additional $4 billion in 1985. About $5 billion a year would come from legislative proposals to improve tax collection and enforcement by accelerating corporate tax payments, increasing staffing at the Internal Revenue Service, and instituting tax withholding on interest and dividends. Roughly $14 billion a year by 1985 would come from proposals characterized by the Administration as eliminating tax abuses and removing obsolete incentives. These include repeal of business energy tax credits, tighter rules for long-term contracts, cutbacks in the use of tax-exempt bonds for private purposes, modifications in the tax treatment of life insurance companies, increased taxes on commercial and industrial real estate construction, and a new minimum tax on corporations. The remaining revenue increases would be derived from reinstating and increasing several airport and airway trust fund taxes--including those on general aviation gasoline and jet fuel and on airline passenger tickets--and by requiring federal civilian employees to pay the hospital insurance portion of the Social Security payroll tax.

The Administration's tax proposals are heavily weighted toward increases in corporation income taxes, which account for about three-quarters of the net tax increases proposed for the 1983-1985 period. They amount to roughly $15 to $16 billion a year by 1985, and substantially offset the corporate tax reductions enacted in the Economic Recovery Tax Act. The proposed corporate tax increases amount to about 75 percent of the ERTA corporate tax reductions for 1984 and almost 60 percent of those for the 1983-1985 period, based on Administration estimates of ERTA revenue reductions. The proposed increases amount to 19 percent of the Administration estimates of total corporate taxes in 1984, and nearly 17 percent of their estimates of corporate taxes for the 1983-1985 period.

The distribution of the additional corporate tax burden, however, would be different from the distribution of the corporate tax savings from ERTA. The proposal to end completed contract accounting would affect primarily the defense, construction, and heavy machinery industries; the proposal to repeal business energy tax credits could have a significant impact on the paper industry; limits on tax-exempt revenue bonds would

TABLE 4. THE ADMINISTRATION'S REVENUE INCREASE PROPOSALS (By fiscal year, in billions of dollars)

	1982	1983	1984	1985
Tax Revisions				
Completed contract accounting	---	3.3	5.0	3.2
Business energy tax credits	---	0.1	0.4	0.6
Tax-exempt revenue bonds	---	-0.2	0.3	1.1
Modified coinsurance	---	1.1	2.2	2.5
Construction period interest and taxes	---	0.5	1.1	1.0
Corporate minimum tax	---	2.3	4.6	5.1
Subtotal	---	7.2	13.5	13.5
Improved Tax Collection and Enforcement				
Withholding on interest and dividends	---	2.0	1.3	1.4
Acceleration of corporate tax payments	---	1.4	1.7	0.9
Internal Revenue Service staff increases	0.2	2.1	2.4	2.4
Subtotal	0.2	5.5	5.5	4.7
Enterprise Zones	---	---	-0.1	-0.5
Airport and Airway Trust Fund	0.1	1.2	1.4	1.5
Railroad Retirement	---	-1.7	-1.8	-1.9
Federal Employee Hospital Insurance Taxes	---	0.6	0.8	0.9
Other	*	0.1	0.1	0.1
Total	0.3	12.8	19.3	18.3

SOURCES: Budget of the United States Government, Fiscal Year 1983, p. 4-16, and the U.S. Department of the Treasury.

*Less than $50 million.

affect firms with geographically dispersed facilities, and steel, paper, and chemical industry users of pollution control bonds; limits on modified coinsurance would affect only the life insurance industry; requiring capitalization of construction period interest and taxes would affect primarily corporations that construct their own offices, stores, and warehouses; and the corporate minimum tax could have a significant effect on the oil and gas industry, exporters, mining companies, banks, and others, depending on its terms.

Some of these industries did comparatively well under ERTA, and some did not. While measurement of the relative corporate tax savings under ERTA is somewhat controversial, a just-published analysis suggests that the tax savings on construction machinery, general industrial equipment, and trucks, buses, and trailers are quite significant, while industrial and commercial buildings received less favorable treatment. 1/ In terms of particular industries, the analysis suggests that petroleum refining, transportation services, motor vehicles, mining, and pulp and paper did especially well, while agriculture, services and trade, and utilities did less well.

The Administration's budget also contains two proposals that would reduce revenues. The first would authorize the establishment of 75 enterprise zones over the three-year period from 1984 to 1986. Businesses locating in designated depressed areas would receive special tax incentives and relief from regulation, designed to increase investment and employment. This would reduce federal revenues by about $0.5 billion, rising to over $1 billion a year by 1987, assuming that no more than 75 zones were established. The second revenue-reducing item is the proposal to eliminate the federal railroad retirement system and replace it with a combination of Social Security and an industry-run pension plan. This would reduce federal receipts by $1.7 billion in 1983 and $1.9 billion in 1985, although federal outlays would be reduced by a slightly greater amount.

The Administration's revenue projections, in total and by major component, are shown in Table 5. Total budget receipts rise from $626.8 billion in 1982 to $796.6 billion in 1985--an increase of about 8.3 percent a year. Social insurance contributions rise more rapidly--about 9.8 percent a year--in part as a result of the Social Security tax rate increase scheduled for 1985. Individual income taxes, on the other hand, because of the scheduled tax rate cuts, grow by only 6.6 percent a year. Corporate income tax payments fall sharply in 1982, because of the recession, but grow rapidly during the next two years, as the economy recovers.

1/ Council of Economic Advisers, Economic Report of the President (February 1982), pp. 122-25.

TABLE 5. COMPOSITION OF REVENUES (By fiscal year)

	Actual 1981	Administration Estimates			
		1982	1983	1984	1985
		In Billions of Dollars			
Individual Income Taxes	285.9	298.6	304.5	322.9	362.0
Corporation Income Taxes	61.1	46.8	65.3	83.7	88.2
Social Insurance Taxes and Contributions	182.7	206.5	222.5	242.5	273.1
Excise Taxes	40.8	43.0	41.7	41.5	40.8
Other Taxes and Receipts	28.7	31.9	32.1	32.4	32.5
Total Budget Receipts	599.3	626.8	666.1	723.0	796.6
		Percent Change			
Individual Income Taxes	17.1	4.4	2.0	6.0	12.1
Corporation Income Taxes	-5.4	-23.4	39.5	28.2	5.4
Social Insurance Taxes and Contributions	15.8	13.0	7.7	9.0	12.6
Excise Taxes	67.9	5.4	-3.0	-0.5	-1.7
Other Taxes and Receipts	9.1	11.1	0.6	0.9	0.3
Total Budget Receipts	15.9	4.6	6.3	8.5	10.2
		Percent Share of Total Receipts			
Individual Income Taxes	47.7	47.6	45.7	44.7	45.4
Corporation Income Taxes	10.2	7.5	9.8	11.6	11.1
Social Insurance Taxes and Contributions	30.5	32.9	33.4	33.5	34.3
Excise Taxes	6.8	6.9	6.3	5.7	5.1
Other Taxes and Receipts	4.8	5.1	4.8	4.5	4.1
Total Budget Receipts	100.0	100.0	100.0	100.0	100.0

SOURCE: Budget of the United States Government, Fiscal Year 1983, pp. 4-2, 9-48.

These tax changes represent for the most part a continuation of the trends of the past 10 or 12 years. Social insurance taxes, as shown in Figure 3, have grown as a federal revenue source from 23 percent of the total in 1970 to 31 percent in 1980, and would reach 34 percent of revenues by 1985. Individual income taxes have represented a relatively constant share of revenues--47 percent in 1970, 44 percent in 1975, 47 percent in 1980, and 45 percent projected for 1985. And corporation income taxes have declined relatively as a source of income to the federal government--17 percent in 1970, 15 percent in 1975, 12 percent in 1980, and 11 percent in 1985.

Spending Proposals

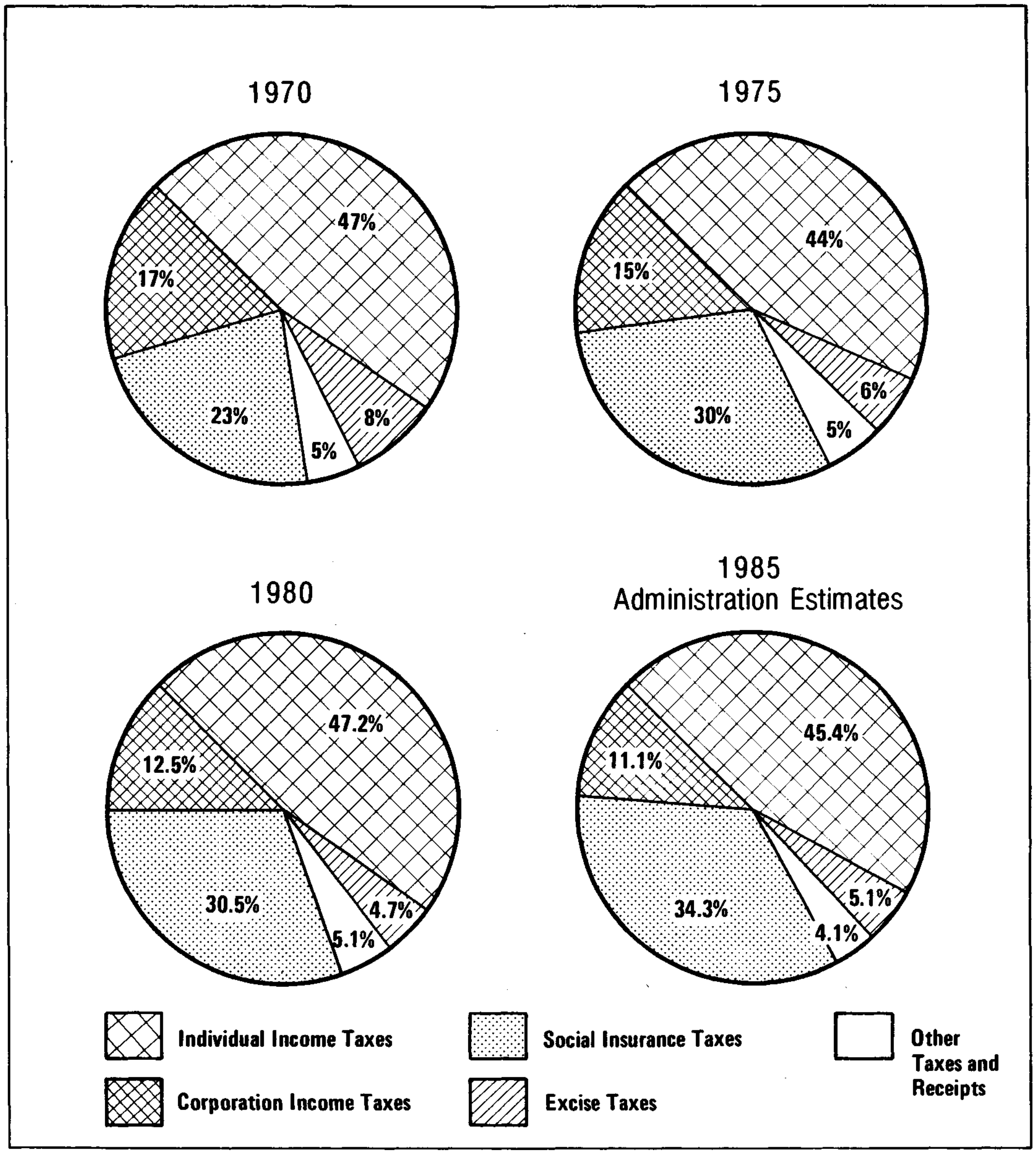
The Administration's budget proposals continue the basic themes introduced last March. Total real federal spending is to be reduced in 1983, with more spent on national defense and less on nondefense programs. Budget outlays in current dollars are projected to rise from $725.3 billion in 1982 to $868.5 billion in 1985 (see Table 6), for an average increase of 6.2 percent a year. This constitutes a sharp reduction from recent growth rates--17.4 percent in 1980 and 14.0 percent in 1981. Including off-budget entities, total federal outlays are estimated to grow by 5.7 percent a year. Since inflation, as measured by the GNP deflator, averages about 5.4 percent over the 1982-1985 period in the Administration's projection, real federal outlays would grow hardly at all under the Administration's program.

Although total federal spending would remain roughly constant in real terms over the next three years, individual categories of spending are projected to grow or contract sharply, as pictured in Figure 4. Defense spending would rise most rapidly--from $187.5 billion in 1982 to $292.1 billion in 1985--an average rate of increase of 15.9 percent a year. Social Security outlays would increase from $154.6 billion to $202.3 billion over the 1982-1985 period--an average annual increase of 9.4 percent.

Benefit payments to individuals, other than for Social Security, would fall in 1983 and grow only slowly in 1984 and 1985, as a result of benefit cutbacks proposed by the Administration. The average growth rate in these other benefit payments would be only 1.8 percent a year--about one-third of the average rate of inflation. Net interest costs are projected to rise at an annual rate of 6.7 percent as the government budget continues to be in deficit. The remainder of nondefense spending, particularly grants to state and local governments, would bear the brunt of the Administration's budget reduction measures. Over the 1982-1985 period, this category of outlays would fall by more than one-third in current dollars and by almost one-half in real terms.

Figure 3.

Major Sources of Federal Revenues



NOTE: Details may not add to 100 percent because of rounding.

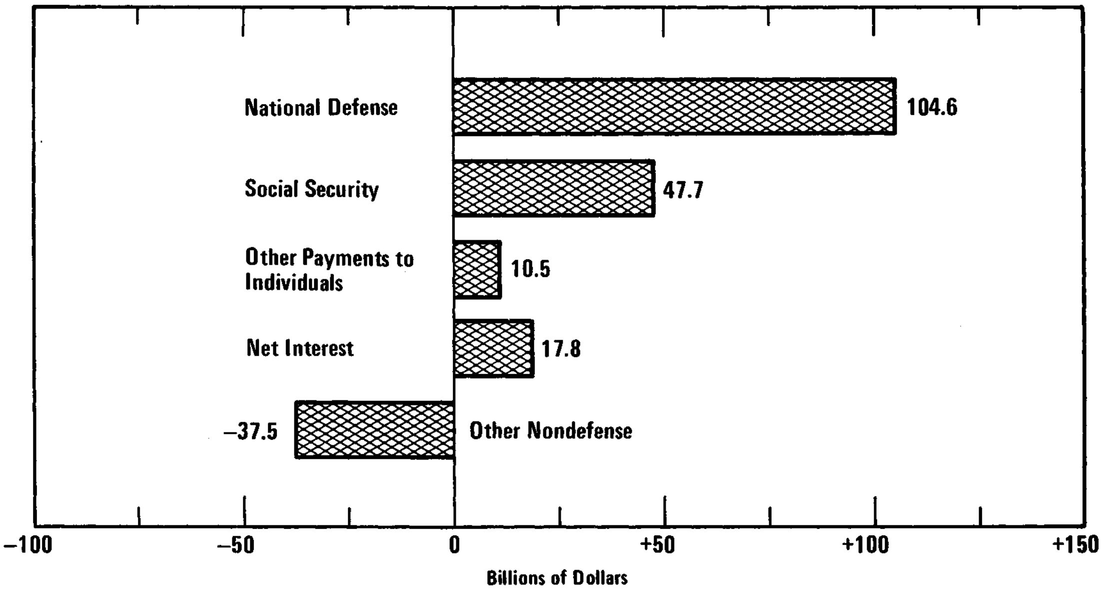
SOURCE: *Budget of the United States Government, Fiscal Year 1983,* p. 4-2, and Table 18, pp. 9-48 and 9-49; and data from the Office of Management and Budget.

TABLE 6. COMPOSITION OF OUTLAYS (By fiscal year)

	Actual 1981	Administration Estimates 1982	1983	1984	1985
		In Billions of Dollars			
National Defense	159.8	187.5	221.1	253.0	292.1
Social Security	138.0	154.6	173.5	188.5	202.3
Other Payments to Individuals	178.6	196.9	192.3	196.8	207.6
Net Interest	68.7	83.0	96.4	98.7	100.8
Other Nondefense	112.1	103.3	74.3	69.0	65.8
Unified Budget Outlays	657.2	725.3	757.6	805.9	868.5
Off-Budget Federal Entities	21.0	19.7	15.7	14.3	11.0
Total Outlays	678.2	745.0	773.3	820.2	879.4
		Percent Change			
National Defense	17.6	17.4	17.9	14.4	15.4
Social Security	17.8	12.0	12.2	8.6	7.3
Other Payments to Individuals	15.9	10.2	-2.3	2.3	5.5
Net Interest	31.0	20.8	16.1	2.4	2.1
Other Nondefense	-4.4	-7.9	-28.1	-7.1	-4.6
Unified Budget Outlays	14.0	10.4	4.5	6.4	7.8
Off-Budget Federal Entities	47.5	-6.3	-20.3	-9.0	-23.3
Total Outlays	14.8	9.9	3.8	6.1	7.2
		Percent Share of Unified Budget			
National Defense	24.3	25.9	29.2	31.4	33.6
Social Security	21.0	21.3	22.9	23.4	23.3
Other Payments to Individuals	27.2	27.1	25.4	24.4	23.9
Net Interest	10.5	11.4	12.7	12.2	11.6
Other Nondefense	17.1	14.2	9.8	8.6	7.6
Unified Budget Outlays	100.0	100.0	100.0	100.0	100.0

SOURCE: Budget of the United States Government, Fiscal Year 1983, pp. 3-21, 3-23, 9-61.

Figure 4.
Proposed Change in Outlays Between 1982 and 1985



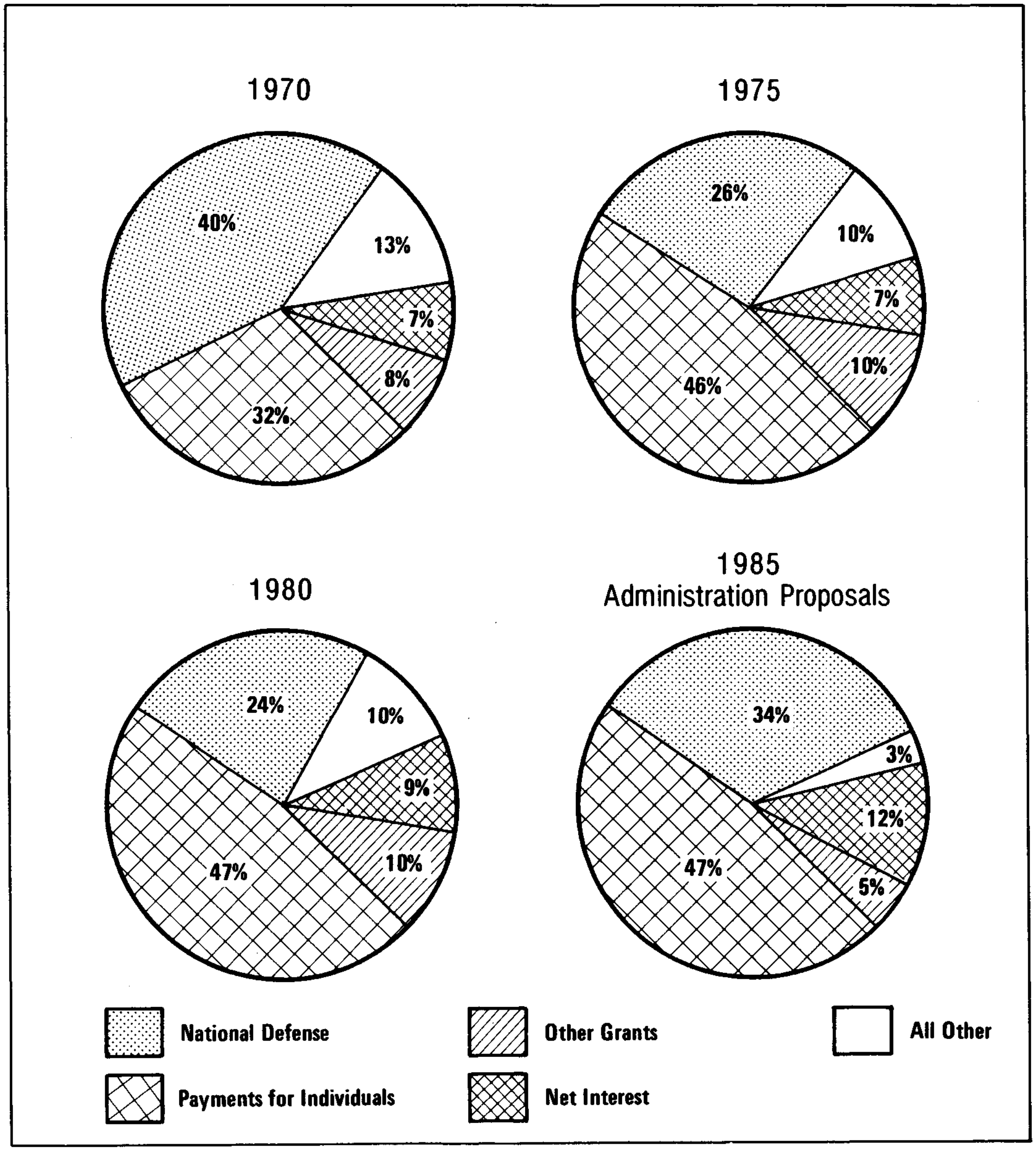
SOURCE: *Budget of the United States Government, Fiscal Year 1983,* p. 3-21.

As a result of such disparate growth rates, the composition of federal spending would be sharply altered over the next three years, as illustrated in Figure 5. By 1985, defense spending would represent 34 percent of the budget--an increase from its 1975 and 1980 levels of 26 and 24 percent, repectively, but less than the 1970 level of 40 percent. The share of the budget devoted to benefit payments for individuals, which grew from 32 percent to 46 percent between 1970 and 1975, would remain roughly constant at about 47 percent of the total. Net interest would grow from 9 percent of the total in 1980 to 12 percent in 1985. The remainder of the budget, which accounted for 20 to 21 percent of the budget from 1970 to 1980, would shrink to 8 percent by 1985.

National Defense. The Administration requests, as it did last year, large increases in spending for national defense. Budget authority would rise by $44 billion in 1983. This represents a real increase of 13.1 percent under the Administration's economic assumptions. Over the 1982-1985 period, defense outlays would grow by $104.6 billion, or by 9.2 percent a year in real terms.

Figure 5.

The Composition of Federal Spending



SOURCE: *Budget of the United States Government, Fiscal Year 1983,* Table 22, p. 9-61.

The Administration argues that spending increases of this size are necessary to provide an adequate level of defense. Its defense plan provides for, among other things, the acquisition of a new bomber (the B-1), the development of an advanced technology (Stealth) bomber to be operational in the early 1990s, the development and procurement of the MX missile, the continued deployment of Trident ballistic missile submarines, and the acquisition of 149 additional ships. These and other Administration defense proposals are analyzed in detail in Chapter V.

Benefit Payments for Individuals. Projected outlays for benefit payments for individuals are shown in Table 7. The Administration is proposing substantial cuts in this category of spending. While it is not now proposing any changes in Social Security cash benefits, it is recommending that physician and hospital reimbursement rates under the hospital insurance program (Part A of Medicare) be reduced and that federal civilian employees be required to pay the hospital insurance portion of the Social Security payroll tax. The budget also assumes, but does not propose, extension of the provision enabling the three major Social Security trust funds to borrow from each other. Under the Administration's economic assumptions, these changes would ensure the solvency of Social Security for the next several years. They would not be sufficient to prevent cash flow problems, however, under a more pessimistic forecast. A recently formed National Commission on Social Security Reform is to examine the financial situation of the Social Security system and report its recommendations by January 1983.

The remaining proposals for cuts in benefit payments are aimed at federal employee benefits and at the means-tested programs, as shown in Table 8. The periodic cost-of-living adjustments in retirement benefits for civilian and military employees of the federal government would be limited to the lower of the percentage increase in federal pay or the increase in the Consumer Price Index. In addition, as noted earlier, Social Security and a private rail industry pension would replace the present federal railroad retirement system.

The proposed cuts in the means-tested programs would affect many of the same programs that were cut during 1981. In Medicaid, most of the President's proposals would increase the states' share of the cost while lowering the federal share; Medicaid beneficiaries would also be required to make small copayments in order to receive services. In food stamps and aid for families with dependent children (AFDC), work requirements would be strengthened, benefit reductions resulting from additional income would be increased, and federal payments for administrative costs would be reduced. In guaranteed student loans, the needs test would be made more stringent, and the fee for taking out a loan would be increased. Most of these changes

TABLE 7. OUTLAYS FOR BENEFIT PAYMENTS FOR INDIVIDUALS (By fiscal year, in billions of dollars)

	Actual 1981	Administration Estimates			
		1982	1983	1984	1985
Social Insurance Programs					
Social Security (OASDI)	139.6	156.6	173.5	188.5	202.3
Railroad retirement	5.3	5.3	---	---	---
Medicare	42.5	49.5	55.3	61.2	68.3
Unemployment compensation	19.7	25.2	22.6	19.8	18.0
Civil Service retirement and disability	17.7	19.4	21.1	22.4	23.9
Veterans' compensation and readjustment benefits	10.8	11.5	11.9	12.0	12.3
Other	11.8	12.6	15.1	15.4	15.8
Subtotal	247.4	280.1	299.5	319.3	340.7
Means-Tested Programs					
Guaranteed student loans and other education	6.2	6.3	5.7	4.3	3.9
Medicaid	16.8	17.8	17.0	18.6	20.4
Food stamps	11.3	11.2	9.6	9.7	10.0
Other food and nutrition programs	4.9	4.2	4.1	4.2	4.3
Housing	6.8	8.1	8.5	8.9	9.4
Supplemental security income	7.2	7.9	8.9	7.8	8.6
Assistance payments (AFDC)	8.5	8.1	5.5	5.5	5.5
Veterans' pensions	3.8	3.9	4.0	4.1	4.2
Other	3.8	4.0	3.1	2.9	2.8
Subtotal	69.3	71.5	66.4	66.0	69.1
Total	316.7	351.6	365.9	385.3	409.8

would concentrate program benefits on families with little or no other income, while reducing the extent to which transfer payments would be available to supplement low or moderate earnings.

The Administration's proposed cuts in means-tested benefits are also an integral part of its plan to transfer full responsibility for the AFDC and food stamp programs to the states. In exchange, it proposes that the federal

TABLE 8. PROPOSED REDUCTIONS IN BENEFIT PAYMENTS FOR INDIVIDUALS (By fiscal year, in billions of dollars)

	1982	1983	1984	1985
Direct Payments to Individuals				
Medicare	0.3	2.5	5.1	7.8
Supplemental security income	0.1	0.3	0.5	0.7
Federal employee retirement and disability	---	0.7	1.4	1.9
Railroad retirement	---	2.0	2.2	2.4
Food stamps	0.3	2.4	2.8	2.9
Guaranteed student loans	0.2	0.8	1.1	1.4
Other	---	0.3	0.6	0.6
Subtotal	0.9	9.0	13.7	17.7
Indirect Payments through State and Local Governments				
Medicaid	0.3	2.0	2.3	3.7
Assistance payments program (AFDC)	0.2	1.2	1.1	1.1
Child nutrition	---	0.3	0.4	0.5
Other	---	0.4	0.6	0.7
Subtotal	0.5	3.9	4.4	6.0
Total Reductions	1.4	12.8	18.1	23.8

SOURCE: Budget of the United States Government, Fiscal Year 1983, p. 3-9.

NOTE: These figures represent the difference between the Administration's proposal and its current services baseline.

government take full responsibilty for Medicaid. The Administration estimates that this exchange would save the states more than $2 billion in 1984. The savings would be contingent, however, upon enactment of the cuts in AFDC and food stamps and upon the increase in state Medicaid costs described above. Without any program changes, CBO estimates that the states would lose $1.5 billion under the swap. Neither a federal cost nor a savings, however, is reflected in the published budget figures.

Direct Grants to State and Local Governments. Grants to state and local governments accounted for $95 billion in federal government outlays in fiscal year 1981. Of this amount, $40 billion represented benefit payments to individuals made through state and local governments; these indirect payment grants were discussed in the previous section of this chapter. Direct grants to state and local governments totaled $55 billion.

Spending for direct grants was substantially reduced during the first session of the 97th Congress. The Omnibus Reconciliation Act of 1981 (Public Law 97-35) reduced authorized spending for sewage treatment plant construction grants, limited obligations for federal-aid highways, and decreased authorizations for urban mass transportation. Existing grant programs in the areas of community development, elementary and secondary education, community services, and social services were combined into new block grants and their funding reduced. Finally, and largest in dollar terms, appropriations under the Comprehensive Employment and Training Act were halved in 1982 and not authorized in later years.

The Administration proposes further substantial reductions in grants for 1983 and later years, as shown in Table 9. New grant consolidations are proposed for vocational and adult education, education for the handicapped, employment and training, rehabilitation services, child welfare services, and welfare administration. Funding for these new consolidated grants would be less than that for the predecessor programs, and funding for the block grants enacted last year and for other grants would also be reduced. Under the Adminstration's program, grant outlays would decline to $44 billion in 1983, $42 billion in 1984, and $41 billion in 1985.

Most of the grants that would be reduced during the 1983-1985 period would be terminated by fiscal year 1988 as part of the Administration's new federalism initiative. One major element of that initiative--the swap of responsibility for certain public assistance programs between federal and state governments--has already been discussed. The second part--called the turnback component--consists of the transfer of responsibility from the federal government to the states of over 40 programs, along with the resources with which the states may finance them. The states would have the choice of continuing to carry out the programs that the federal government gives up, modifying them, or discontinuing them. The plan's details are described by the Administration as a framework for discussion. Specific legislative proposals are to be developed after extensive consultation with Members of Congress and state and local officials.

The new federalism proposal reflects the Administration's concept that state and local governments should have full responsibility for local transportation, community development and capital investment, general education, social service delivery, and cash assistance to the nonelderly needy. The federal government would be involved only in programs deemed

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TABLE 9. OUTLAYS FOR DIRECT GRANTS TO STATE AND LOCAL GOVERNMENTS (By fiscal year, in billions of dollars)

	Actual 1981	Administration Estimate			
		1982	1983	1984	1985
Energy Conservation Grants	0.5	0.5	0.2	0.1	---
Environmental Protection Agency Construction Grants	3.9	4.0	3.4	2.8	2.7
Other Natural Resources and Environment	1.1	1.1	0.8	0.7	0.7
Agriculture	0.8	0.9	0.9	0.9	0.9
Highway Grants	9.1	8.2	8.2	8.2	8.3
Urban Mass Transportation Fund	3.8	3.7	3.1	2.9	2.9
Airport Grants	0.5	0.5	0.4	0.5	0.6
Community Development Grants	4.0	4.0	3.4	3.2	3.5
Urban Development Action Grants	0.4	0.5	0.6	0.5	0.5
Rental Rehabilitation Grants	---	---	---	0.1	0.1
Area and Regional Development	1.2	1.0	0.8	0.5	0.3
Elementary, Secondary, and Vocational Education	6.6	6.7	5.1	4.2	3.6
Training and Employment	8.0	4.2	2.0	2.7	2.3
Social Services	6.2	6.1	4.8	4.8	4.8
Combined Welfare Administration	---	---	1.7	1.7	1.7
General Revenue Sharing	5.1	4.6	4.6	4.6	4.6
Other General Purpose Fiscal Assistance	1.6	1.7	2.0	2.2	2.5
Other	2.0	1.9	1.7	1.2	1.1
Total	54.8	49.6	43.7	41.8	41.1

to be of national significance, such as education for the handicapped and the disadvantaged and interstate highways. This new division of responsibilities, the Administration argues, would encourage diversity among state and local governments, give individuals paying for services more voice in deciding whether and how they should be provided, and make governments more accountable for their actions. The Administration also contends that "income redistribution is not a compelling justification in the 1980s for Federal taxing and spending programs. It is the Administration's view that the Federal Government can do more to provide lasting assistance to the disadvantaged by assuring strong and less inflationary economic growth than through income transfer programs." 2/

Other Federal Operations. Other federal operations include foreign aid, loans and subsidies to individuals and businesses, research and development activities, construction and acquisition of certain physical assets, and other general operating expenses of the federal government. Proprietary receipts from the public, including rents and royalties from mineral leasing and timber sales, as well as various user charges, also fall in this category.

For 1982, the Administration's budget shows a decrease of almost $4 billion in outlays for other federal operations. This reflects the shift off budget of oil acquisition expenditures for the strategic petroleum reserve, as well as a $1 billion allowance for unspecified reductions in fraud, waste, and abuse. Excluding these two items, the Administration's estimate of 1982 outlays for this category is about the same as the 1981 figure. The proposed budget for 1983, however, shows a drastic decline of $23 billion in net outlays, with continued reductions in the later years (see Table 10).

The outlay reductions fall into four basic categories. The largest outlay decrease, relative to the 1982 estimates, is not from spending changes, but rather from increases in receipts and collections. Over $10 billion stems from a planned acceleration in the leasing of Outer Continental Shelf (OCS) lands, which the Administration estimates would almost triple bonus bids in 1983. Proposed user fees account for $1 billion of the outlay reduction in 1983 and $2 billion in 1984 and 1985. The new fees would include levies on users of inland waterways and deep draft harbors, commercial and recreational boatmen, electric utilities that generate radioactive wastes, recipients of loans guaranteed by the Veterans Administration, and visitors to the National Parks and other federal recreational facilities.

2/ Economic Report of the President, p. 92.

TABLE 10. OUTLAYS FOR OTHER FEDERAL OPERATIONS (By fiscal year, in billions of dollars)

	Actual 1981	Administration Estimate			
		1982	1983	1984	1985
Gross Outlays a/	89	83	71	72	71
Rents and Royalties on the Outer Continental Shelf	-10	-8	-18	-18	-18
New User Fees	--	--	-1	-2	-2
Other Proprietary Receipts and Postal Service Payment for Employee Retirement	-11	-14	-15	-17	-18
Administrative Initiatives	--	-2	-5	-8	-9
Asset Purchases by the Federal Financing Bank	-11	-5	-1	*	*
Total (Net Outlays)	57	54	31	27	25

*Less than $500 million.

a/ This figure is an approximation. The figures are understated to the extent that they are net of offsetting collections that are credited to program accounts and not to distinct receipt accounts. Also, the figures include the effects of certain asset transactions, loan repayments, and other factors that can distort the gross spending figures.

The 1983 budget also includes $5 billion in outlay reductions attributable to a number of administrative actions. Of this, $3 billion are unspecified savings resulting from reductions in fraud, waste, and abuse, more effective debt collection, and increased sales of excess federal property. These unspecified savings are projected to rise to $7 billion by 1985.

The remainder of the savings in this category is to be achieved by reductions in gross program outlays. These are projected to decline from $83 billion in 1982 to $71 billion in 1983--a drop of 15 percent--and to remain roughly level in 1984 and 1985. About $7 billion of this drop occurs in nondiscretionary programs, largely in the farm price support programs of the Commodity Credit Corporation (see Table 11). Among discretionary

TABLE 11. GROSS OUTLAYS FOR OTHER FEDERAL OPERATIONS (By fiscal year, in billions of dollars)

	Actual 1981	Administration Estimate			
		1982	1983	1984	1985
Energy	11.0	7.3	5.7	5.9	6.1
Natural Resources and Environment	10.8	10.9	10.2	10.1	10.4
Education, Training, Employment, and Social Services	4.2	4.3	3.7	3.2	3.3
Farmers Home Administration Credit Programs	10.9	7.4	4.2	3.4	3.5
Other Credit Programs a/	5.9	4.3	3.5	2.5	1.9
International Affairs	11.9	11.9	12.8	13.2	13.9
Space Program	4.9	5.3	6.1	6.1	5.8
Federal Aviation Administration	2.7	2.6	3.0	3.3	3.7
Law Enforcement Activities	2.4	2.5	2.7	2.7	2.8
Internal Revenue Service	2.4	2.6	2.9	3.0	3.2
Farm Price Supports	3.6	5.8	1.4	1.7	1.3
Other Nondiscretionary Programs b/	1.1	-0.9	-2.7	-2.5	-3.3
Other	16.8	18.9	18.0	19.6	18.6
Total	88.6	82.9	71.5	72.2	71.2

NOTE: These figures are CBO approximations based on data from the Office of Management and Budget. Allowances for pay raises have been distributed to the appropriate program.

a/ Includes the Export-Import Bank, the GNMA special assistance functions fund, housing for elderly and the handicapped under the Department of Housing and Urban Development, Small Business Administration business and disaster loans, and the Central Liquidity Facility.

b/ Includes the Federal Savings and Loan Insurance Corporation fund, the Federal Deposit Insurance Corporation, the Veterans Administration loan guarantee revolving fund, and settlements of railroad litigation.

programs, the largest cuts are targeted for energy, natural resources, environment, education, and credit activities. These are offset to some extent, however, by proposed spending increases for foreign security assistance, the space program, the air traffic control system, law enforcement activities, and the Internal Revenue Service.

Off-Budget Outlays

The Administration's budget also contains new estimates for off-budget outlays and the federal debt. Off-budget outlays are those of certain federal entities whose spending has been excluded from the unified budget totals. These outlays must be added to the unified budget deficit, however, to derive the total federal deficit that must be financed. When off-budget outlays are financed by Treasury borrowing, the additional debt is subject to the statutory debt limit.

A new off-budget entity was created in 1981, when the Congress removed from the budget the appropriation for acquiring oil for the Strategic Petroleum Reserve. The Postal Service fund was given off-budget status in 1974. Except for these two programs, the outlays of the off-budget federal entities are incurred for carrying out federal loan programs. As shown in Table 12, the Federal Financing Bank (FFB) accounts

TABLE 12. OUTLAYS OF OFF-BUDGET FEDERAL ENTITIES (By fiscal year, in billions of dollars)

	Actual 1981	Administration Estimates			
		1982	1983	1984	1985
Federal Financing Bank	21.0	16.2	12.1	11.0	7.8
Strategic Petroleum Reserve	---	2.8	2.8	2.3	2.2
Postal Service Fund	0.1	0.6	0.7	0.9	0.8
Rural Electrification and Telephone Revolving Fund	*	---	---	---	---
Rural Telephone Bank	0.1	0.2	0.2	0.2	0.2
U.S. Railway Association	-0.3	-0.1	*	---	---
Synthetic Fuels Corporation	---	---	---	---	---
Total	21.0	19.7	15.7	14.3	11.0

*Less than $50 million.

for most of these outlays. The FFB's outlays do not come from programs that the FFB operates itself. Instead, the FFB assists other programs within the government by purchasing their outstanding loans (loan assets) or purchasing obligations that they have guaranteed.

When the FFB buys loan assets, it in effect converts direct loans that have already been made by another agency into off-budget direct loans of the FFB. If the selling agency is in the budget, its loan asset sales reduce net budget outlays. Also, when the FFB purchases newly originated guaranteed loans, it has the effect of converting loan guarantees that are not recorded in the budget totals into direct federal loans outside the budget.

As part of its effort to limit the growth of federal credit, the Administration proposes to reduce substantially the outlays of the Federal Financing Bank. FFB outlays are projected to fall from $21.0 billion in 1981 to $16.2 billion in 1982, $12.1 billion in 1983, and $7.8 billion by 1985. The 1982 and 1983 decreases are primarily the result of reduced purchases of Farmers Home Administration (FmHA) loan assets by the FFB. Net purchases of FmHA loan assets fall from $10.9 billion in 1981 to $1.1 billion in 1983 (see Table 13). Net FFB disbursements of direct loans guaranteed by other agencies will remain stable in 1982, 1983, and 1984, as reductions in loans to the Student Loan Marketing Association and the Rural Electrification Administration offset increases in foreign military sales credit. Most major categories of direct loans decline by 1985.

Federal Debt

Early in fiscal year 1982, the federal debt subject to statutory limit exceeded $1 trillion. By the end of fiscal year 1985, according to Administration estimates, the debt will reach almost $1.5 trillion. The increase in debt from the beginning of 1982 to the end of 1985 represents an average annual increase of about 14 percent--only slightly higher than the projected increase in the gross national product over this period. Debt as a percentage of GNP in 1985 will, therefore, be little changed from its 1981 level. In fact, as Figure 6 illustrates, the ratio of debt to GNP has remained relatively constant since the early 1970s.

The Congress customarily has placed statutory limitations on federal debt, and estimates of federal debt are included in the Congressional budget resolutions. The current limitation--$1,079.8 billion--was enacted on September 30, 1981, and expires on September 30, 1982. Federal debt subject to limit totaled $1,039.3 billion at the end of January 1982 and is expected to reach the statutory ceiling by May. The Administration's

TABLE 13. NET OUTLAYS OF THE FEDERAL FINANCING BANK (By fiscal year, in billions of dollars)

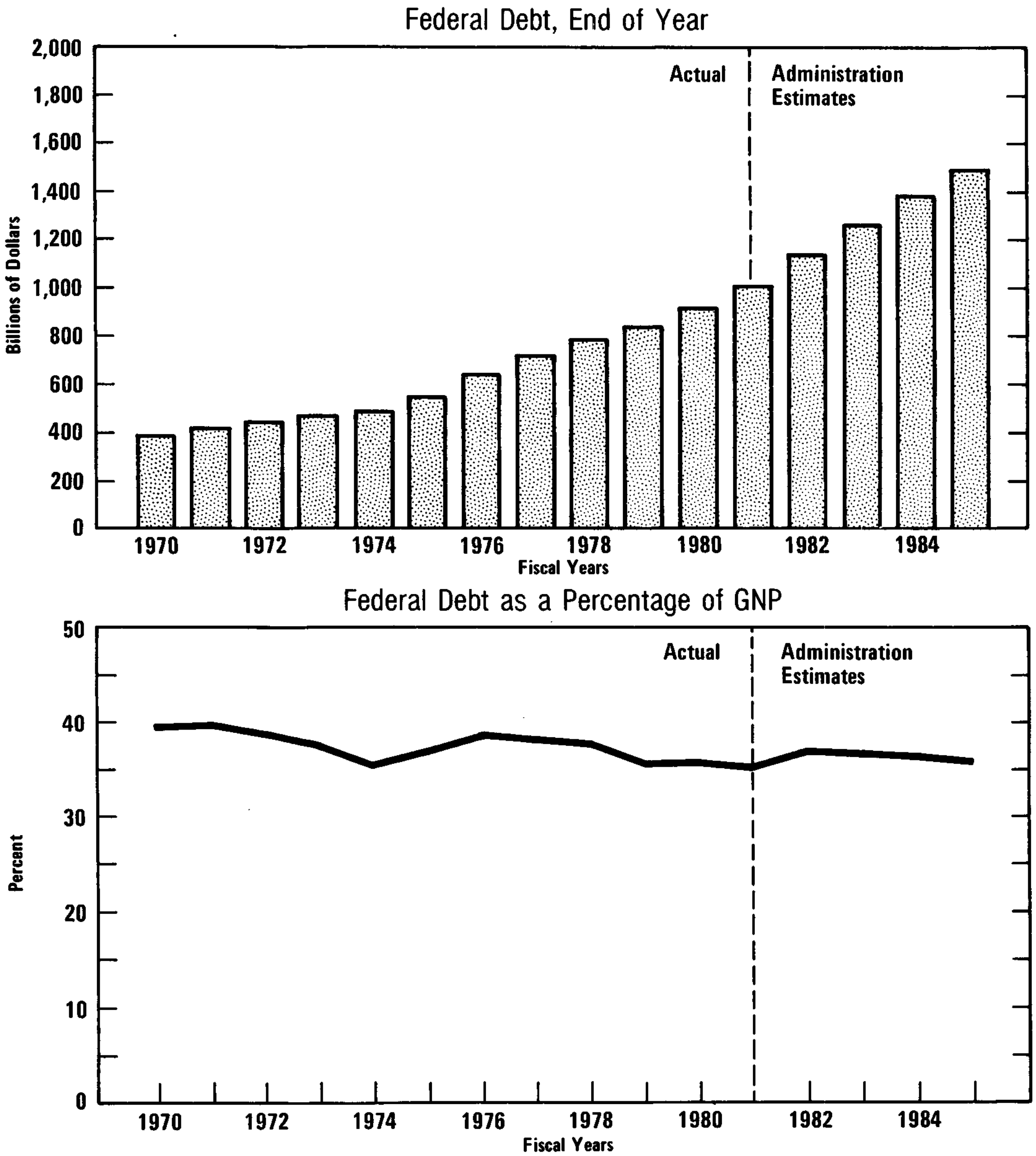
	Actual 1981	Administration Estimates			
		1982	1983	1984	1985
Purchases of Agency Loan Assets					
Rural Electrification Administration	0.7	0.6	0.5	0.4	0.5
Farmers Home Administration	10.9	5.4	1.1	0.2	0.2
Subtotal	11.5	6.0	1.7	0.6	0.6
Direct Loans (Purchases of Agency Guaranteed Loans)					
Foreign military sales credit	1.9	2.7	3.7	4.2	3.0
Rural Electrification Administration	3.9	4.3	4.1	3.6	3.3
Energy Research and Technology Administration	*	0.5	0.9	1.0	0.8
Low-rent public housing	0.8	1.2	1.0	1.4	-0.1
Student Loan Marketing Association	2.0	0.7	---	---	---
Small Business Administration	0.1	0.2	0.2	0.2	0.2
Tennessee Valley Authority	0.2	0.2	0.3	0.2	0.3
Other	0.5	0.4	0.2	-0.2	-0.3
Subtotal	9.4	10.2	10.4	10.4	7.2
Interest, Transfer of Surplus, and Administrative Expenses	0.1	---	---	---	---
Total	21.0	16.2	12.1	11.0	7.8

SOURCES: Budget of the United States Government, Fiscal Year 1983, pp. 8-168-172; and the Office of Management and Budget.

*Less than $50 million.

Figure 6.

Federal Debt



SOURCE: *Budget of the United States Government, Fiscal Year 1983,* Table 21, p. 9-60.

budget estimates that debt subject to limit will reach $1,130.0 billion, or $50.2 billion above the current limitation, by the end of fiscal year 1982. For 1983, the budget projects another increase of $124.3 billion in federal debt subject to limit.

Four elements enter into the calculation of the amount by which the statutory debt limit must be changed: the unified budget deficit or surplus, the investment of trust fund surpluses in federal securities, the deficit of off-budget federal entities, and various means of financing other than borrowing. Table 14 shows the estimates for these elements underlying the public debt levels projected by the Administration. Even if the unified budget were balanced, the debt subject to limitation would increase because of the investment of trust fund surpluses in federal debt securities and because of the deficit of the off-budget entities.

TABLE 14. ESTIMATES OF DEBT SUBJECT TO STATUTORY LIMIT (By fiscal year, in billions of dollars)

	Actual 1981	Administration Estimates			
		1982	1983	1984	1985
Debt Subject to Limit (beginning of year)	908.7	998.8	1,130.0	1,254.3	1,368.7
Increase in Debt Subject to Limit					
Unified budget deficit	57.9	98.6	91.5	82.9	71.9
Trust fund surplus	6.8	12.5	15.4	17.9	31.3
Deficit of off-budget federal entities	21.0	19.7	15.7	14.3	11.0
Means of financing (other than borrowing) and other adjustments	4.3	0.4	1.6	-0.7	-0.8
Total Increase	90.1	131.2	124.3	114.4	113.3
Debt Subject to Limit (end of year)	998.8	1,130.0	1,254.3	1,368.7	1,482.0

THE CREDIT BUDGET

The credit budget, instituted in 1980, attempts to bring together and focus attention on the new lending activities of the federal government. It records estimates by program of new direct loan obligations and new loan guarantee commitments. The credit budget totals are based on gross levels of activity, without offsets for repayments. Guaranteed loan totals are based on the full amount of the loan, even if the amount covered by the guarantee is less than the total.

During its first session, the 97th Congress took a number of actions to control the federal credit budget. Limitations were included in appropriation bills for 40 percent of direct loans and 70 percent of loan guarantees. Language in the Continuing Appropriations Resolution (Public Law 97-92) specified that these limitations should also be taken as target levels that should be met unless there were insufficient qualified borrowers. This stipulation was included to prevent administrative reductions in the credit budget. In response, the Administration has submitted proposals to reduce a number of 1982 limitations as part of its proposed 1983 budget.

The Administration believes that the rapid growth of federal credit activity has adversely affected the nation's productivity by channeling funds to less productive borrowers and has increased pressures on interest rates in the private market. It is, therefore, proposing that the credit budget for 1983 be limited to an increase of 3 percent above the revised 1982 level. Its proposed credit budget for 1983 totals $147.3 billion--$49.0 billion in new direct loan obligations and $98.4 billion in new loan guarantee commitments. The 1983 request for direct loans is 13 percent below the revised 1982 request, while the request for primary loan guarantees is 13 percent above the revised 1982 request. Table 15 provides a comparison of the 1981 actual credit budget and the Administrations' proposals for 1982 and 1983.

Table 16 shows the Administration's major changes in the 1983 credit budget. The only major growth in direct loans is for international security assistance, primarily foreign military sales credit, which will increase by $1.0 billion as part of the Administration's program to increase military assistance to strategically important nations. The Administration proposes a $2.6 billion reduction in direct loans through the Farmers Home Administration, including major decreases in direct loans for rural housing. Commodity Credit Corporation (CCC) loans are projected to decrease by $2.0 billion, on the assumption of improved market conditions for farmers. The reduction of $4 million for direct loans of the Small Business Administration would eliminate this program entirely.

TABLE 15. TOTAL CREDIT BUDGET (By fiscal year, in billions of dollars)

	Actual 1981	Administration Estimates	
		1982	1983
Direct Loan Obligations			
On Budget	40.9	39.9	31.8
Off Budget	31.5	29.6	25.5
Total	72.4	69.5	57.3
Less: FFB Sales of Loan Assets	-15.2	-13.2	-8.3
New Direct Loan Obligations	57.2	56.4	49.0
New Loan Guarantees	152.7	166.1	161.4
Less: Secondary Loan Guarantees	-44.1	-48.7	-38.4
Guaranteed Loans Held as Direct Loans			
Federal Financing Bank	-30.3	-28.5	-24.7
Government National Mortgage Association	-1.8	-1.9	---
Primary Guarantees	76.5	87.1	98.4
Credit Budget Total	133.7	143.4	147.3

The projected increases in loan guarantees are largely the result of the expected improvement in the housing market. Growth is anticipated in the guaranteed loan programs of the Federal Housing Administration (FHA) and the Veterans Administration. An increase of $1.5 billion in guaranteed loans for public housing is also projected, as a result of prior-year commitments. Decreases in guaranteed loans are proposed for the Farmers Home Administration, the Rural Electrification Administration, and the Small Business Administration.

TABLE 16. CHANGES IN THE 1983 CREDIT BUDGET TOTALS (In billions of dollars)

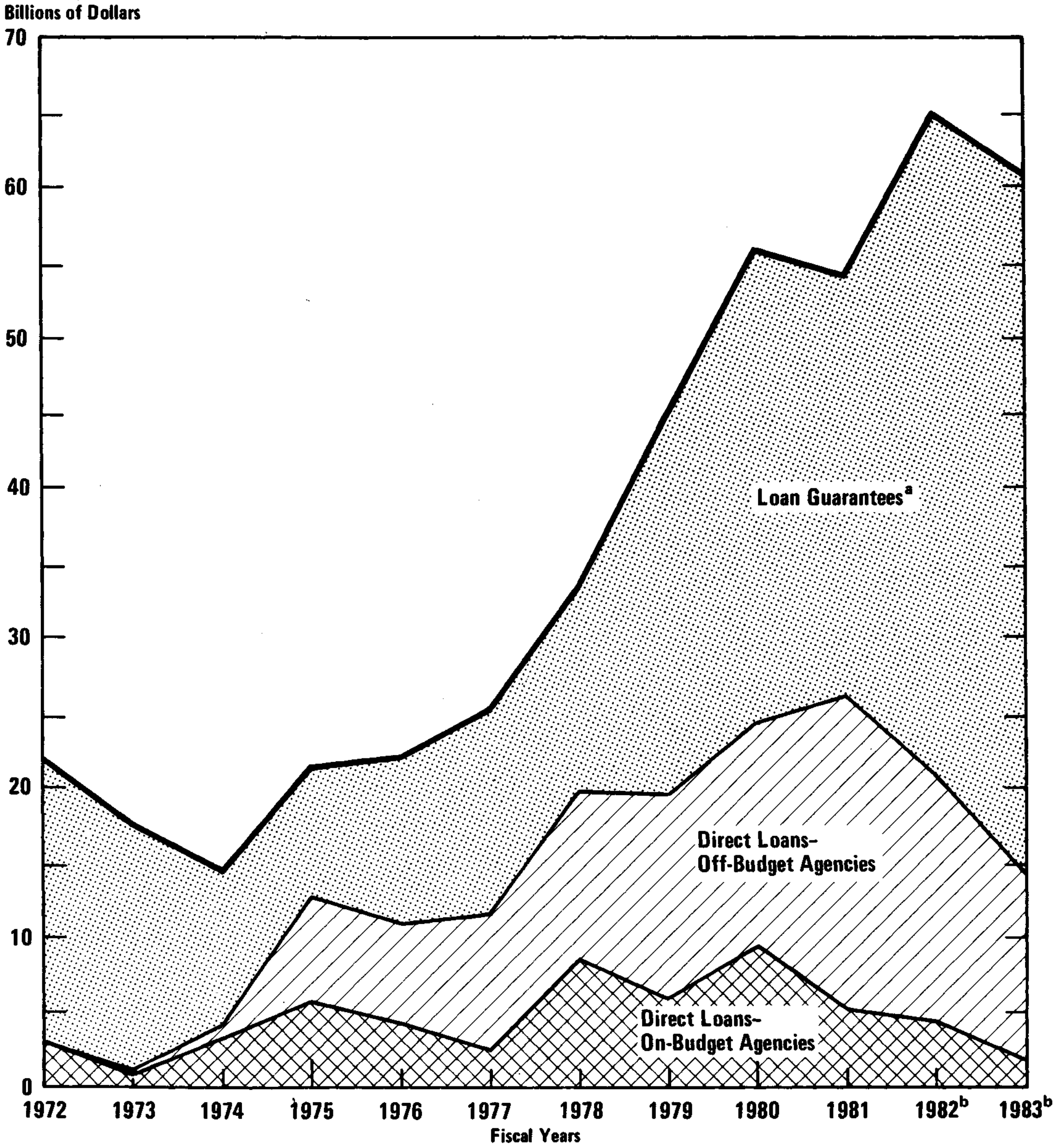
	Direct Loan Obligations	Guaranteed Loan Commitments
Credit Budget Totals for 1982	56.4	87.1
Major Program Changes		
Export-Import Bank	-0.6	---
Farmers Home Administration	-2.6	-0.6
Rural Electrification Administration	-0.4	-0.5
Small Business Administration	-0.4	-0.3
Low-income public housing	-0.5	1.5
International security assistance	1.0	0.8
CCC price supports	-2.0	---
FHA fund	-0.1	6.4
Veterans' housing	*	2.9
Other	-1.8	1.0
Total Program Changes	-7.4	11.3
Credit Budget Totals for 1983	49.0	98.4

SOURCE: Budget of the United States Government, Fiscal Year 1983, p. 3-25.

*Less than $50 million.

As the result of both the reductions in the credit budget proposed by the Administration and increased repayments, net credit extended is estimated to decrease by 6 percent between 1982 and 1983. Figure 7 provides an historical perspective on the components of net federal lending. The 1983 decrease will be only the second reduction since 1974, when federal credit activities began to expand at an accelerated rate.

Figure 7.
Components of Net Federal Credit, Fiscal Years 1972-1983



[a] Primary guarantees: excluding secondary guarantees and guaranteed loans acquired by on- and off-budget agencies.
[b] Estimates

SOURCE: *Budget of the United States Government, Fiscal, Year 1983,* Special Analysis F, Federal Credit Programs.

CHAPTER II. THE ADMINISTRATION'S ECONOMIC ASSUMPTIONS

Both the Congressional Budget Office and the Administration anticipate an end to the current recession early in 1982, with a resumption of moderate growth and a continued slowing of inflation. While the recovery projected by the Administration is not particularly strong compared with earlier cyclical recoveries, its projections through 1987 are more optimistic than those of most economic forecasters, including CBO. 1/ In CBO's view, tight credit conditions are likely to limit economic growth. In fact, there is a risk that the clash between restrictive money growth and fiscal stimulus will lead to higher interest rates and weaker growth than forecast by either CBO or the Administration.

ECONOMIC DEVELOPMENTS IN 1981

The performance of the economy in 1981 was mixed. Economic growth was weak; measured from fourth quarter to fourth quarter, real GNP increased a scant 0.7 percent during 1981 while the unemployment rate rose to 8 1/2 percent by year's end. On the other hand, inflation slowed significantly in 1981; measured from fourth quarter to fourth quarter, the growth in the Consumer Price Index (CPI) slowed from a rate of 12.5 percent in 1980 to a rate of 9.5 percent in 1981.

The sluggish growth in 1981 resulted largely from very tight credit conditions. 2/ Inflation slowed mainly because of bountiful farm output, which resulted in relatively modest food price increases, because of the glut in world oil markets, which stabilized energy prices, and because of the appreciation of the dollar in foreign exchange markets, which reduced prices of imported goods. The developments in food and fuel were largely unexpected by forecasters a year ago. Accordingly, most forecasters, including the Administration and CBO, have modified their projections for 1982 and 1983 to show lower real growth and/or lower inflation than previously expected.

1/ Congressional Budget Office, The Prospects for Economic Recovery (February 1982).

2/ The Federal Reserve's policies in 1981 are analyzed in The Prospects for Economic Recovery, pp. 39-49.

COMPARISON OF ADMINISTRATION AND CBO FORECASTS FOR 1982 AND 1983

The Administration and CBO forecasts are in close agreement for calendar year 1982 (see Table 17). They see output in constant dollars rising by about 3 percent over the four quarters of the year, and unemployment in the neighborhood of 8 1/2 percent at year's end. The forecasts are also in close agreement for inflation and short-term interest rates.

TABLE 17. COMPARISON OF ADMINISTRATION AND CBO FORECASTS (By calendar year)

	1982	1983
Gross National Product (GNP)		
Current dollars (percent change, fourth quarter over fourth quarter)		
President's February budget	10.4	11.0
CBO baseline	10.3	11.1
Constant (1972) dollars (percent change, fourth quarter over fourth quarter)		
President's February budget	3.0	5.2
CBO baseline	2.8	3.9
Prices		
GNP deflator (percent change, fourth quarter over fourth quarter)		
President's February budget	7.2	5.5
CBO baseline	7.2	6.9
Consumer Price Index (percent change, fourth quarter over fourth quarter)		
President's February budget	6.6	5.1
CBO baseline	6.4	7.2
Unemployment Rate (percent, fourth quarter)		
President's February budget	8.4	7.6
CBO baseline	8.7	7.6
Interest Rate (91-day Treasury bills, percent, annual average)		
President's February budget	11.7	10.5
CBO baseline	12.0	13.2

In 1983, however, the Administration's forecast for inflation and growth is more optimistic than CBO's. The Administration looks for real GNP to expand by 5.2 percent, and for inflation (as measured by the GNP deflator) to fall to a rate of 5.5 percent. The unemployment rate in the Administration's forecast falls to 7.6 percent by the fourth quarter of next year and, for the year as a whole, the three-month Treasury bill rate is expected to average 10.5 percent.

By contrast, CBO expects real GNP to grow by about 1 1/2 percentage points less than the Administration in 1983, and the GNP deflator to rise about 1 1/2 percentage points more. 3/ Short-term interest rates average 2 3/4 percentage points higher over the year, while the unemployment rate falls to the same level as in the Administration's forecast. This latter result, despite different rates of economic expansion in the two forecasts, may be caused by assumed patterns of productivity growth during the recovery.

The slow growth expected by CBO for 1983 is largely the consequence of higher real rates of interest in its forecast that serve to dampen the recovery in economic activity. The key factors behind the CBO forecast of a modest further deceleration of inflation are:

- o Wage demands will soften in the face of slack labor markets, but the reduction in labor costs will probably be limited once the recovery is well underway.

3/ As measured by the CPI, the two forecasts of inflation are similar in 1982 but diverge in 1983. The Administration expects a CPI increase of 6.6 percent in 1982, slowing further in 1983 to 5.1 percent, measured from fourth quarter to fourth quarter. CBO, on the other hand, expects 6.4 percent in 1982 and 7.2 percent in 1983. A detailed comparison of these CPI inflation forecasts is not possible given the absence of comparative detail on individual prices used to construct the CPI. The 1983 increase reflected in the CBO forecast does not, however, represent an assumed intensification of underlying inflationary pressures. Rather, it reflects assumed patterns of change in oil prices and in mortgage rates between 1982 and 1983. CBO assumes that energy cost and mortgage interest cost movements will hold down the increase in the CPI below the underlying rate of inflation in 1982 but not in 1983. Thus, by 1983, CBO's forecast of the CPI reflects more modest expectations of the reduction in the inflation rate.

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- o The cyclical increase in labor productivity growth is more likely to affect profits than prices.

- o The supply-inducing effects of the 1981 tax act will probably build slowly, in part because of high real interest rates.

Short-Run Forecast Risk. At present, the key element of uncertainty in the CBO forecast is the prospective course of monetary policy. The CBO forecast for 1982 and 1983 assumes growth in the monetary aggregates at the upper ends of the current target ranges. Given the historical relationship between money and nominal GNP, and the CBO view that inflation will decelerate slowly, the assumed Federal Reserve policy implies that real growth during the cyclical recovery period will be less than normal as the result of continued high levels of interest rates. There is considerable chance, moreover, that economic growth will be much weaker than projected by CBO, especially if the Federal Reserve limits money growth more severely than assumed.

In addition, high federal deficits will result in a marked increase in Treasury borrowing in the CBO forecast, putting further upward pressure on interest rates. As the recovery gets under way, the conflict between the stimulative fiscal policy and a tight monetary policy could push interest rates to high levels. The outcome is very difficult to predict because this policy combination has no historical precedent. However, there is a distinct possibility of even weaker growth than that projected by either the Administration or CBO.

The general rise in interest rates since late November 1981 is most unusual during a recession and represents a significant risk to the forecast in the months ahead. If interest rates do not moderate soon, the projected upturn in economic activity could be delayed. The rise in long-term interest rates since the passage of the tax act, for example, has probably offset much of the reduction in capital costs brought about by the Accelerated Cost Recovery System. Continued high interest rates would bear heavily on residential construction, autos, and other durable goods industries. Tight credit conditions are hitting the economy hardest in those very sectors where fiscal policy is seeking to promote increases in the supply of productive resources and capacity. If this situation persists, little supply response can be expected from the Administration's program, even over the medium term. Indeed, a prolonged period of slack characterized by low rates of capacity utilization and diminished employment opportunities could actually discourage capital formation and inhibit labor supply growth, thereby severely limiting the economy's productive potential. Finally, if tight credit conditions persist, more and more businesses will find themselves in financial distress.

THE PROSPECTS FOR GROWTH THROUGH 1987

The Administration's economic assumptions for the 1984-1987 period are also more optimistic than CBO's (see Table 18 and Figure 8). The projections beyond 1983 are not forecasts of probable economic outcomes but, rather, are assumptions. The Administration's long-range assumptions are, in its words, "projections consistent with the economic policy objectives of the Administration." CBO's baseline assumptions, on the other hand, are projections of what appears to be an attainable improvement in economic conditions. 4/

Real Growth. The Administration assumes an average rate of growth of 4.6 percent a year between 1984 and 1987. CBO, on the other hand, assumes an average growth rate of 3.5 percent. In comparable four-year periods following previous postwar recoveries, real growth has averaged 3.4 percent a year, and ranged between 2.0 and 5.2 percent. 5/ Real growth in the 1984-1987 period could be higher than the average of historical experience for three reasons.

- o The fiscal stimulus over this period will be sizable;
- o The gap between current and potential production is very large, according to most estimates, meaning that there is little chance that the economy will reach its capacity limits quickly even if real growth is rapid; and
- o Some of the 1981 tax act's features could provide a substantial boost to supply over a period of several years, increasing the economy's capacity limits.

4/ The Administration's description is from Budget of the United States Government, Fiscal Year 1982 (January 1981), p. 2-4. CBO's long-range assumptions are described in The Prospects for Economic Recovery, p. 58.

5/ If the business cycle trough is assumed to occur sometime during the first half of this year, as most forecasters now predict, the 1984-1987 period represents a four-year period beginning roughly two years after a business cycle trough as designated by the National Bureau of Economic Research.

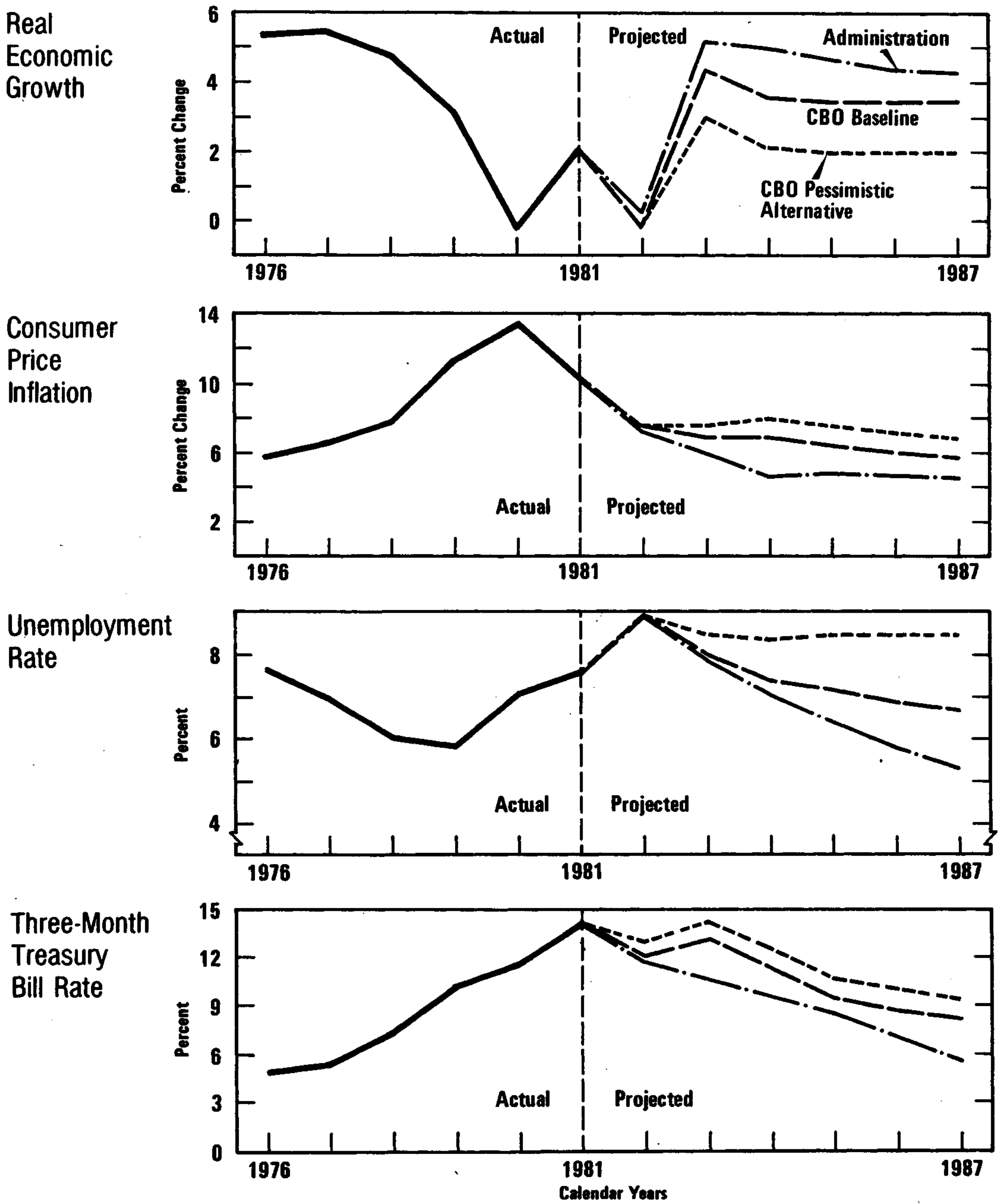
TABLE 18. COMPARISON OF ADMINISTRATION AND CBO LONG-RUN ECONOMIC ASSUMPTIONS (By calendar year)

	1982	1983	1984	1985	1986	1987
Gross National Product (GNP)						
Current dollars (percent change, year to year)						
President's February budget	8.1	11.5	10.2	9.7	9.2	9.0
CBO baseline	7.5	11.9	10.4	9.7	9.4	9.1
Pessimistic alternative	7.3	11.1	9.8	9.2	8.9	8.5
Constant (1972) dollars (percent change, year to year)						
President's February budget	0.2	5.2	5.0	4.7	4.4	4.3
CBO baseline	-0.1	4.4	3.6	3.5	3.5	3.5
Pessimistic alternative	-0.3	3.0	2.1	2.0	2.0	2.0
Prices						
GNP deflator (percent change, year to year)						
President's February budget	7.9	6.0	5.0	4.7	4.6	4.5
CBO baseline	7.5	7.3	6.6	6.0	5.7	5.4
Pessimistic alternative	7.6	7.9	7.5	7.1	6.7	6.4
Consumer Price Index (percent change, year to year)						
President's February budget	7.3	6.0	4.6	4.8	4.6	4.5
CBO baseline	7.5	6.9	6.9	6.4	6.0	5.7
Pessimistic alternative	7.6	7.6	8.0	7.6	7.2	6.9
Unemployment Rate (percent, annual average)						
President's February budget	8.9	7.9	7.1	6.4	5.8	5.3
CBO baseline	8.9	8.0	7.4	7.2	6.9	6.7
Pessimistic alternative	8.9	8.5	8.4	8.5	8.5	8.5
Interest Rate (91-day Treasury bills, percent, annual average)						
President's February budget	11.7	10.5	9.5	8.5	7.0	5.5
CBO baseline	12.0	13.2	11.3	9.4	8.7	8.1
Pessimistic alternative	13.0	14.3	12.7	10.8	10.1	9.4
"Real" Interest Rate a/						
President's February budget	3.8	4.5	4.5	3.8	2.4	1.0
CBO baseline	4.5	5.9	4.7	3.4	3.0	2.7
Pessimistic alternative	5.4	6.4	5.2	3.7	3.4	3.0

NOTE: The Administration's assumptions include the presumed effects of its new budget initiatives. The CBO economic assumptions are based on estimates of current policy taxes and spending.

a/ "Real" interest rates are defined here as the 91-day Treasury bill rate minus the rate of inflation as measured by the GNP deflator.

Figure 8.
Comparison of Major Economic Assumptions



SOURCES: For historical data, Department of Commerce, Bureau of Economic Analysis; Department of Labor, Bureau of Labor Statistics; and Federal Reserve System, Board of Governors. For projections, Congressional Budget Office and Office of Management and Budget.

There are, however, a number of reasons why one might expect growth to be lower than the average of the postwar experience.

- o Inflation may remain stubbornly persistent as the result of "sticky" wage behavior;

- o Interest rates are likely to remain high, in real terms, relative to the postwar average;

- o Trend growth in productivity may remain low relative to postwar experience; and

- o Supply shocks of the sort that wracked the economy in the 1970s could recur.

There is no sure way of predicting the net outcome of all these factors during the decade, particularly since typical cyclical comparisons may not be applicable to the current recovery period. In the interests of prudent budgeting, the Congress may want to consider what the effects would be on the budget if economic growth were weaker than projected by CBO. For this reason, CBO has constructed a pessimistic alternative projection in which inflation is higher and productivity growth is lower than in the CBO baseline (see Table 18 and Figure 8).

Monetary Policy, Interest Rates, and the Deficit. Tight credit conditions may be the most serious impediment to economic growth during the next several years. On October 6, 1979, the Federal Reserve adopted new operating procedures aimed at achieving greater control over the long-run growth of the monetary aggregates. The objective was a gradual reduction in the growth of money and credit in order to reduce inflation. In the light of this policy objective, the question arises whether the realized rates of money growth in future years will permit sustained rapid increases in real economic activity. Ultimately, the answer to this question will be determined by three factors:

- o The rate of money growth;

- o The effective limit on nominal GNP growth resulting from money growth and the rate of money velocity growth; 6/

6/ Velocity may be defined as the number of times an average dollar in the money supply is used to finance transactions over a given period of time. Its rate of growth is thus simply the difference between growth rates in nominal GNP and growth in the monetary aggregate.

- o The actual rate of inflation which, given the ceiling on nominal GNP, will determine how much room is left for real GNP growth.

The Administration assumes a further gradual but steady reduction in the growth of M1 to a rate of about 3 1/2 percent in 1986. 7/ Given the Administration's assumed rates of nominal GNP growth, the implied rates of M1 velocity growth are displayed in Figure 9. The rates of M1 velocity growth through 1986 implied by the Administration's economic assumptions are very high by historical standards. 8/

Past experience suggests that such high rates of M1 velocity growth are associated with high interest rates. Furthermore, the CBO reestimates of the President's budget through 1985 suggest that federal borrowing will be significant in each year even if the Administration's proposals are adopted. This will place still more upward pressure on interest rates. Of course, if the Federal Reserve permitted somewhat more rapid but still declining rates of money growth, the potential velocity (and interest rate) constraint on real growth would be eased, leaving more room for a greater expansion in economic activity. Nevertheless, the assumption of high velocity growth raises the possibility that the strong economic growth assumed by the Administration will not materialize.

CONCLUSION

There is a serious risk that the Administration's economic assumptions will prove to be too optimistic. If so, the budget deficits will be larger than projected by the Administration, even if all of its budget proposals are enacted. Moreover, CBO's technical reestimates of the revenue and spending levels associated with the Administration's programs, presented in

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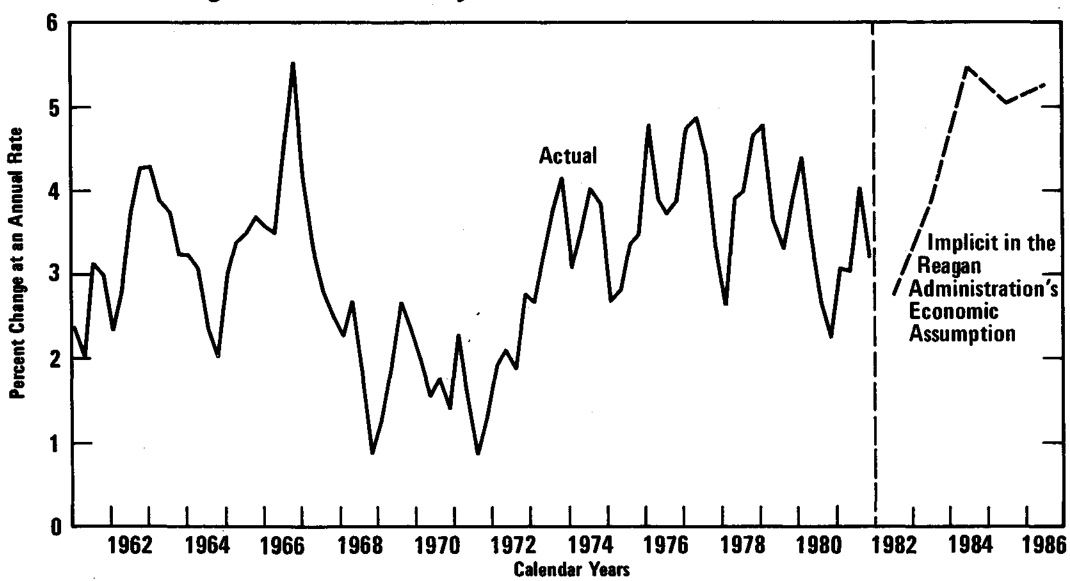
7/ In the Economic Report of the President (February 1982, p. 206), the Council of Economic Advisers states: "From the fourth quarter of 1979 to the fourth quarter of 1980, M1 (currency plus checkable deposits) grew at a 7.3 percent annual rate. The Administration assumes a gradual but steady reduction in the growth of money to one-half that rate by 1986."

8/ It is possible, of course, that high rates of M1 velocity growth could be sustained as long as financial practices aimed at economizing on money balances continue to grow over time. To what extent this will happen, particularly if real interest rates fall (which would reduce incentives to adopt more sophisticated money management techniques) is very much an open question.

subsequent chapters, also raise the prospect of much higher budget deficits. The projections of high deficits for the foreseeable future is a matter of serious concern, particularly because they are only partially the result of the recession. Such deficits would not only increase the risk of a serious clash between monetary and fiscal policy during the next few years; they would also crowd out private investment and this, in time, would adversely affect long-run economic growth.

Figure 9.

Percent Change in the Velocity of M1B from Two Years Earlier



SOURCES: Federal Reserve System, Board of Governors; U.S. Department of Commerce, Bureau of Economic Analysis; Executive Office of the President, Office of Management and Budget.

CHAPTER III. CBO REVENUE REESTIMATES

According to the Congressional Budget Office's analysis of the President's February budget revenue estimates, unified budget receipts could be slightly higher than projected by the Administration in 1982, but lower in subsequent years, ranging from $6.0 billion less in 1983 to $20.5 billion less in 1985.

CBO's reestimates of revenues for the 1982-1985 period are lower than those of the Administration for two reasons:

- o CBO's less optimistic economic assumptions, and

- o Differences in technical estimating.

Economic conditions could be less favorable than those assumed by the Administration. The revenue reestimates attributable to the differences between the Administration's economic assumptions and the CBO baseline economic forecast and longer-run assumptions are small, amounting to a net reduction in revenues of about $3.5 billion over the 1982-1985 period. Reestimation using the CBO baseline economic assumptions causes a reduction in revenues of about $3 billion in 1982 and $1 billion in 1983, an increase of about $6 billion in 1984, and a reduction of about $5 billion in 1985. If more pessimistic economic assumptions were used instead of the baseline assumptions, revenues would be reduced by about $4 billion in 1982, $3 billion in 1983, $1 billion in 1984, and $16 billion in 1985.

CBO's preliminary technical analysis of the Administration's budget estimates suggests that revenues could be about $4 billion higher than projected by the Administration in 1982, but lower in subsequent years, by amounts ranging from about $5 billion in 1983 to $16 billion in 1985.

A potential third reason for reduced revenues over the 1982-1985 period would be the failure of the Administration's new tax proposals to provide the estimated net increases. Two factors could contribute to this shortfall: the Congress might not approve the legislative changes required to implement these proposals; or, if approved, the new proposals might not produce as much revenue as the Administration now predicts.

Since the Administration has provided only limited information on its new tax proposals, CBO could not develop independent estimates of their revenue effects. (See Chapter I for a brief discussion of these proposals.) This chapter presents CBO's reestimates of the President's budget revenues generated by substituting CBO's baseline economic assumptions for those of the Administration and using CBO's technical estimating methods. The CBO reestimates, which are summarized in Table 19, assume that all of the President's new tax proposals are approved by Congress and that these initiatives provide the revenue increases specified by the Administration. Table 20 presents the Administration's revenue estimates and the CBO reestimates by source.

TABLE 19. CBO REESTIMATES OF ADMINISTRATION BUDGET REVENUES (By fiscal year, in billions of dollars)

	1982	1983	1984	1985
President's February Budget	626.8	666.1	723.0	796.6
Preliminary CBO Reestimates				
Different economic assumptions	-3.4	-0.8	5.6	-4.9
Technical differences	4.3	-5.2	-13.0	-15.6
Total Reestimates	0.9	-6.0	-7.4	-20.5
President's Budget Reestimated	627.7	660.1	715.6	776.1

DIFFERENCES IN ECONOMIC ASSUMPTIONS

Revenue estimates are highly sensitive to economic assumptions. In particular, revenue estimates depend upon assumptions about wages and salaries and other income from dividends, interest, rental property, and unincorporated businesses; corporate profits; inflation; and interest rates.

Since the individual income tax system is progressive, revenue estimates depend upon assumptions about the relative effects of productivity increases and inflation on incomes, as well as upon assumptions about the aggregate level of income. Because individual income taxes are such an important source of revenue, accounting for almost 48 percent of total revenues in 1981, slight changes in assumptions about personal income can have significant effects on revenue projections.

TABLE 20. ADMINISTRATION BUDGET REVENUES AND CBO REESTIMATES, BY SOURCE (By fiscal year, in billions of dollars)

	1982	1983	1984	1985
		Administration Budget		
Individual Income Taxes	298.6	304.5	322.9	362.0
Corporate Income Taxes	46.8	65.3	83.7	88.2
Social Insurance Taxes a/	206.5	222.5	242.5	273.1
Excise Taxes				
Windfall profit taxes	24.1	21.2	20.0	19.0
Other excise taxes	18.9	20.4	21.5	21.7
Other	32.0	32.1	32.4	32.5
Total	626.8	666.1	723.0	796.6
		CBO Reestimates		
Individual Income Taxes	300.0	306.2	318.6	346.9
Corporate Income Taxes	50.5	59.8	77.9	77.8
Social Insurance Taxes a/	205.0	222.0	244.3	275.7
Excise Taxes				
Windfall profit taxes	22.9	20.9	20.8	20.4
Other excise taxes	18.6	20.1	20.9	21.3
Other	30.7	31.1	33.0	34.0
Total	627.7	660.1	715.6	776.1

a/ These revenue estimates exclude supplemental medical insurance premiums and voluntary enrollee premiums for medicare coverage. These premiums, which were previously included in revenues, are shown in the February budget as offsets against outlays. The amounts involved range from $3.9 billion in 1982 to $5.3 billion in 1985.

While the corporate income tax structure is also progressive, progressivity is a less important factor in the estimation of corporate revenues. Corporate income taxes, however, are sensitive to assumptions about investment as well as to assumptions about corporate profits.

Social insurance tax estimates depend upon assumptions about wages and salaries, employment, and inflation. Inflation assumptions are important for the estimation of Social Security taxes since the maximum taxable wage for these taxes is indexed for inflation. Windfall profit tax estimates are particularly sensitive to assumptions about oil prices, as Federal Reserve payments estimates are to assumptions about interest rates. Estimates of customs duties and of excise taxes other than windfall profit taxes are more generally responsive to assumptions about the overall level of economic activity.

Unexpected changes in economic conditions can have significant effects on revenue projections. Weakening economic conditions alone are accountable for a $31 billion downward revision since March 1981 in the Administration's estimate of total revenues for fiscal year 1982.

CBO forecasts a slight drop in economic output and a decline in the rate of inflation in 1982, while the Administration projects a slight increase in economic output and a somewhat smaller decline in the rate of inflation. For 1983 and subsequent years, CBO assumes lower real growth and higher inflation in each year than does the Administration. Interest rates are higher throughout the period under the CBO assumptions.

CBO's assumptions of lower real growth and higher inflation over the period combine to provide projected levels of GNP that are quite close to those of the Administration. Since individual and corporate income taxes, which accounted for almost 60 percent of total revenues in 1981, are most sensitive to nominal incomes, these differences in economic assumptions have relatively minor effects on revenue estimates. Therefore, CBO projects total revenues only $3.5 billion below the Administration's estimate for the 1982-1985 period.

Reestimates Based on CBO Baseline Economic Assumptions

CBO assumes lower personal income than does the Administration in every year except 1984, when CBO's income level is higher. These income differences lower the CBO reestimates of individual income taxes relative to the Administration's estimates by about $3 billion in 1982 and $5 billion in 1983, raise CBO's reestimate by less than $1 billion in 1984, and lower CBO's reestimate by about $7 billion in 1985.

CBO's reestimates of corporate income taxes based on economic assumptions result from different assumptions about the level of corporate profits from current production and about the level of business activity, which affects the amount of depreciation deductions and investment credits taken by corporations. In 1982 and 1983, CBO assumes higher corporate profits than does the Administration, which raises the CBO reestimates of corporate income taxes above the Administration's by more than $2 billion in 1982 and $4 billion in 1983. In 1984, the difference in estimates of profits is insignificant. In 1985, CBO assumes lower profits than does the Administration, which lowers the CBO reestimate of corporate income taxes below the Administration's estimate by about $5 billion.

CBO's assumption of lower levels of business activity results in smaller amounts of depreciation deductions and investment credits, and thus raises CBO's reestimates of corporate income taxes relative to the Administration's estimates. The increases in revenues due to these assumptions grow from about $0.3 billion in 1982 to about $3.7 billion in 1985. Over 60 percent of this increase in revenues is attributable to the accelerated cost recovery provisions of the Economic Recovery Tax Act of 1981.

Social Security taxes dominate the differences in estimates of social insurance taxes attributable to economic assumptions. CBO assumes lower wages and salaries than does the Administration in 1982 and 1983. These differences reduce the CBO estimates of Social Security taxes below the Administration's by about $2 billion in 1982 and $1 billion in 1983. In 1984 and 1985, the situation is reversed--CBO assumes higher wages and salaries, raising the CBO estimates of Social Security taxes above those of the Administration by about $2 billion in each year.

Lower CBO oil price assumptions reduce the CBO estimate of windfall profit taxes relative to the Administration's estimates by $0.9 billion in both 1982 and 1983. By 1984, the oil price differential narrows, lowering the CBO windfall tax estimate by only $0.1 billion. By 1985, the CBO assumes oil prices slightly above those of the Administration but not by enough to affect significantly the estimate of windfall taxes in that year.

The largest reestimate of other taxes based on economic assumptions is attributable to the consistently higher CBO interest rate assumptions. These raise the CBO estimates of Federal Reserve System payments above the Administration's in each year. This differential grows from $0.2 billion in 1982 to $1.7 billion in 1985.

Reestimates Based on Pessimistic Economic Assumptions

In developing its baseline economic assumptions, CBO prepared two alternative sets of economic assumptions, one optimistic and the other pessimistic. CBO's optimistic alternative assumed higher economic growth, lower unemployment, and lower rates of inflation than did the baseline. The Administration's economic assumptions are somewhat similar to this optimistic alternative. The pessimistic alternative assumed lower real growth, higher unemployment, and higher rates of inflation than did the baseline.

If economic conditions were to be closer to those in the CBO pessimistic alternative, CBO reestimates of Administration budget receipts would place revenues below those estimated by the Administration in each year of the 1982-1985 period. Lower individual and corporate incomes would decrease total income taxes by slightly over $33 billion for the period. These revenue reductions would be partially offset by increases in excise taxes and Federal Reserve payments, both of which would be higher because of the assumption of higher prices and interest rates in the pessimistic economic alternative.

Substituting the CBO pessimistic assumptions for the Administration economic assumptions would lower net revenues by $4.3 billion in 1982, $3.2 billion in 1983, $0.7 billion in 1984, and $16.3 billion in 1985. For the entire period, total revenues would be about $24 billion below the Administration's estimates.

TECHNICAL ESTIMATING DIFFERENCES

Revenue estimation involves procedures and models which analyze a large amount of data in addition to the economic variables discussed above. For example, estimation of individual income taxes requires information about the portion of personal income that is subject to tax and about the distribution of income across the tax brackets, in addition to data on aggregate income levels. Estimation of corporate income taxes requires information about the distribution of investment between equipment and structures, about the average tax life for each category of investment, and about the amount of used capital purchased each year, in addition to data on aggregate corporate profits. All of the differences from such assumptions are included in the total differences not explained by quantifiable economic assumptions, called technical estimating differences.

Without specific information about these types of assumptions, it is not possible to identify how much of the remaining differences in revenue estimates between the Administration's budget and the CBO reestimates are due to each assumption. In this discussion, the reestimates attributable to specific assumptions are identified.

CBO's revenue reestimates based on technical estimating differences account for $29.5 billion of the estimated potential revenue shortfall over the 1982-1985 period, or almost 90 percent of the total. The revenue reestimates based on technical factors discussed here are divided into two types:

- Those resulting from the estimation of the revenue effects of some of the provisions of the recently enacted Economic Recovery Tax Act of 1981 (ERTA), and

- Those resulting from other technical procedures and assumptions.

Technical reestimates of ERTA provisions mostly affect individual and corporate income taxes. Other technical differences arise from varying assumptions about the timing of tax payments and taxpayer behavior other than that related to ERTA and, to a lesser degree, from differences in estimating procedures. Although these other differences affect all types of taxes, they account for most of the technical differences in the reestimates of the nonincome taxes. This section first discusses the reestimates related to ERTA and then analyzes the reestimates from other technical factors. Total CBO technical differences from both ERTA and other factors are summarized in Table 21.

Economic Recovery Tax Act

Estimates of the revenue effects of the Economic Recovery Tax Act require assumptions about the distribution of income and investment and about the economic and taxpaying behavior of affected individuals. In this analysis, revenue reestimates attributable to such assumptions are classified as technical reestimates.

Other reestimates of the revenue effects of ERTA are directly attributable to the differences in economic assumptions that are discussed above. Table 22 summarizes the CBO revenue reestimates based on the effects of ERTA, distinguishing between those attributable to technical estimating differences and those attributable to economic assumptions.

TABLE 21. CBO REVENUE REESTIMATES, BY SOURCE, BASED ON CBO TECHNICAL ESTIMATING DIFFERENCES (By fiscal year, in billions of dollars)

	1982	1983	1984	1985
Individual Income Taxes	4.8	6.7	-4.9	-8.1
Corporate Income Taxes	1.1	-10.7	-7.9	-9.1
Social Insurance Taxes	0.2	0.1	0.1	0.4
Excise Taxes (including Windfall Profit Taxes)	-0.6	0.2	0.3	1.0
Federal Reserve Payments	-1.2	-1.5	-0.6	0.2
Other	a/	a/	a/	a/
Total	4.3	-5.2	-13.0	-15.6

a/ Less than $50 million.

CBO's estimates of revenue reductions attributable to ERTA are larger in each year than are the Administration's. Relative to prior law, CBO's estimates range from a revenue reduction of $39.0 billion in 1982 to $189.2 billion in 1985. The Administration's estimates range from a reduction of $38.3 billion in 1982 to $176.7 billion in 1985.

CBO's reestimates of the revenue effects of ERTA that are attributable to technical factors lower CBO's revenue projections below the Administration's by growing amounts each year, from $1.4 billion in 1982 to $12.1 billion in 1985. The largest technical estimating differences occur in the provisions for across-the-board reductions in individual income tax rates; the indexing of individual income tax brackets, zero bracket amounts, and personal exemption; and the Accelerated Cost Recovery System (ACRS).

Technical differences in the estimation of the across-the-board rate reductions are most significant in 1984 when the CBO estimate of individual income taxes is over $5 billion below the Administration's estimate. This differential narrows to about $3 billion in 1985. The technical estimating differences for the indexing provisions, which go into effect in 1985, lower

TABLE 22. REVENUE REESTIMATES BASED ON THE EFFECTS OF ECONOMIC RECOVERY TAX ACT (By fiscal year, in billions of dollars)

	1982	1983	1984	1985
Differences from Technical Factors				
Rate cuts	-0.4	-0.7	-5.2	-3.2
Indexing	---	---	---	-3.4
Accelerated Cost Recovery System				
Individual	a/	-0.3	-0.2	-0.3
Corporate	-0.9	-3.3	-3.1	-4.1
Other	a/	-0.8	-1.1	-1.1
Subtotal, Technical Differences	-1.4	-5.1	-9.6	-12.1
Differences from Economic Assumptions (CBO Baseline)				
Rate cuts	0.3	1.1	-0.2	1.0
Indexing	---	---	---	-3.8
Accelerated Cost Recovery System				
Individual	0.1	0.2	0.3	0.5
Corporate	0.2	0.6	1.3	2.5
Other	a/	-0.1	-0.4	-0.6
Subtotal, Economic Differences	0.6	1.7	0.9	-0.4
Total	-0.7	-3.4	-8.6	-12.5

a/ Less than $50 million.

the CBO estimate of individual income taxes by another $3 billion below the Administration's estimate for that year. For the effects of ACRS on individual income taxes, these differences reduce the CBO revenue estimates below the Administration's estimates by $0.3 billion or less each year. Net technical differences attributable to all of the other individual income tax provisions of ERTA raise the CBO revenue estimates above the Administration's by about $1 billion or less in each year. The total net effect of the technical estimating differences for ERTA raises CBO's reestimates of individual income taxes above those of the Administration by about $0.4 billion in 1982, and $0.1 billion in 1983, and lowers the reestimates below those of the Administration by about $4.3 billion in 1984 and $6.6 billion in 1985.

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For corporate income taxes, technical factors related to the estimation of the revenue effects of ERTA reduce CBO estimates below the Administration's by about $1 billion in 1982 and by slightly more than $5 billion annually from 1983 to 1985. Almost 70 percent of these differences are attributable to estimates of the accelerated cost recovery provisions of the act. In 1985, the total technical reestimates of ERTA's effects on corporate taxes are equivalent to fully 8 percent of CBO's estimate of total corporate income taxes under current law.

Other Technical Estimating Differences

Net technical differences from CBO assumptions about the timing of tax payments and other taxpayer behavior, unrelated to ERTA, are quite small, less than 1 percent of revenues annually from 1982 to 1985. These considerations combine to raise CBO's revenue reestimates above the Administration's by $5.7 billion in 1982 and to lower them by growing amounts thereafter, from $0.1 billion less in 1983 to $3.5 billion less in 1985.

For income taxes, these differences are partly attributable to assumptions about the timing of tax collections. For example, based on receipts for the first quarter of fiscal year 1982, CBO has assumed a large overpayment of corporate income taxes this year compared to liabilities. This overpayment may have been caused, in part, by uncertainty about the effects of recent requirements for the prompt payment of taxes and of other recent tax changes. CBO also assumes that more than half of the 1982 overpayments will be offset by refunds in 1983, which would cause corporate taxes to be smaller than liabilities in that year. The Administration also may have assumed a longer time lag between changes in corporate tax liability and related adjustments in payments during the 1983-1985 period.

The net effect of these technical estimating differences unrelated to ERTA raise the CBO estimates of corporate income taxes above those of the Administration in 1982 by about $2 billion. For 1983 through 1985, these factors reduce the CBO estimates of corporate income taxes below the Administration's by between about $3 billion to $5 billion annually. Such technical factors as the timing of tax payments and the distribution of income across tax brackets raise the CBO estimates of individual income taxes above the Administration's by over $4 billion in 1982 and over $6 billion in 1983, and reduce the CBO estimates by small amounts in 1984 and 1985.

CBO's technical reestimates raise the estimates of social insurance taxes by amounts ranging from $0.1 billion to $0.4 billion per year because of CBO's inclusion of federal employee pay raises beyond 1982, which raises federal employee retirement taxes, and because of increased health insurance refunds resulting from a recent court decision, which are included in the Administration's estimates but not in CBO's.

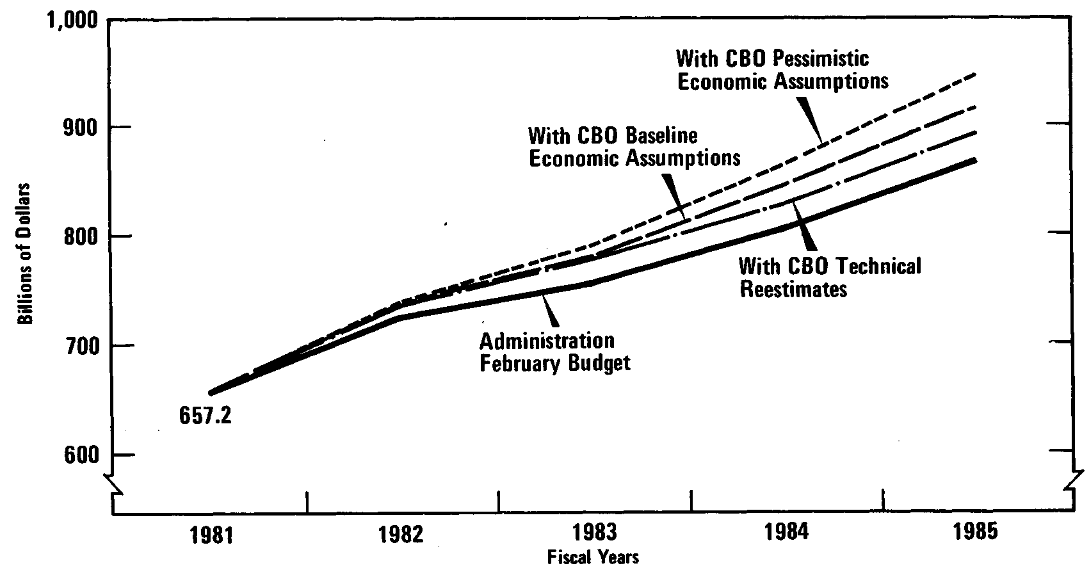
CBO's reestimates of windfall profit taxes tend to be higher than the Administration's, in part, because of technical differences in assumptions about the rate at which domestic oil may be reclassified as incremental tertiary oil for purposes of the tax. CBO assumes a slower rate of reclassification of oil as tertiary oil, which is taxed at a lower rate. These assumption differences raise CBO windfall profit tax estimates above the Administration by about $0.6 billion in 1983, $0.9 billion in 1984, and $1.4 billion in 1985. Differences in technical estimation methods lower CBO net reestimates of excise taxes, other than windfall profit taxes, below those of the Administration by amounts ranging from $0.3 billion to $0.6 billion per year.

All remaining significant technical estimating differences are attributable to different methods used to estimate Federal Reserve payments. CBO identifies as differences due to economic assumptions only those differences estimated to result from different levels of interest rates. Therefore, technical differences include differences because of other assumptions, which might be considered economic or partially economic, but which cannot be estimated without information about the Administration's assumptions. These include assumptions about the extent to which the Federal Reserve's portfolio management will keep earnings high by retaining medium and long-term securities acquired at peak interest rates. Such differences cause CBO estimates to be lower than the Administration's by $1.2 billion in 1982, $1.5 billion in 1983, $0.6 billion in 1984, and higher than the Administration by $0.2 billion in 1985.

The Congressional Budget Office's analysis of the President's February budget spending estimates suggests that unified budget outlays could be much higher than the Administration projects, by amounts ranging from at least $13 billion in 1982 to $47 billion or more in 1985.

One reason why outlays may be higher than the Administration projects is that its budget estimates seem to understate probable expenditures. CBO has made a technical analysis of the Administration's estimates. The preliminary results of this analysis suggest that outlays may have been underestimated by about $12 billion in 1982 and by over $20 billion in each of the next three years (see Figure 10). For the entire 1982-1985 period, CBO's technical reestimates would add more than $75 billion to the Administration's projections of outlays.

Figure 10.
CBO Outlay Reestimates



A second reason why outlays could be higher is that the economy may fail to perform as the Administration assumes it will. Under CBO's baseline economic forecast and longer-run assumptions, total outlays over the 1982-1985 period would be higher by about $45 billion--$1 billion in 1982, $3 billion in 1983, over $16 billion in 1984, and $24 billion in 1985. The adjustments to the Administration's estimates resulting from the use of CBO's baseline economic assumptions are not as large as those resulting from the technical reestimates in any year except 1985. Under CBO's alternative set of pessimistic economic assumptions, however, outlays could be higher than projected by the Administration by at least $12 billion in 1983, $35 billion in 1984, and more than $55 billion in 1985.

A third reason for higher outlays in 1983-1985 is that the Administration may not be successful in meeting all of its savings targets for various management initiatives, such as improved debt collection procedures and disposal of surplus federal property. CBO has not been able to develop its own independent estimates of the results of such initiatives, but believes many of the Administration's estimates to be very optimistic.

Finally, the Administration is proposing significant spending reductions that require legislative action, especially for entitlement programs. The Congress may not approve all of these proposals. Also, the Administration has projected savings from a major reform of health care financing that has not yet been developed and is already greatly delayed.

This chapter provides CBO's reestimates of the President's budget proposals, showing the outlay differences that could result from the first two reasons. The reestimates are divided into two categories: (1) those that result from substituting CBO's economic assumptions for the Administration's, and (2) those that result from using CBO's technical estimating methods and from other factors. The reestimates using CBO baseline economic assumptions and technical estimating methods are summarized in Table 23. They assume that all of the President's legislative proposals are approved by the Congress and that the Administration is successful in meeting most of its targets for savings from management initiatives--in short, they make no adjustments based upon the third and fourth reasons given above.

The next two sections of the chapter discuss the two categories of differences involved in the outlay reestimates. A third section provides a brief discussion of the various Administration budget estimates that CBO was unable to evaluate because of lack of specific supporting documentation or other details. This includes over $7 billion of savings to be achieved in 1985 from planned management initiatives. The remainder of the chapter details the CBO outlay reestimates for each major function of the budget.

TABLE 23. CBO REESTIMATES OF THE ADMINISTRATION'S SPENDING PROPOSALS (By fiscal year, in billions of dollars)

	1982	1983	1984	1985
President's February Budget	725.3	757.6	805.9	868.5
Preliminary CBO Reestimates				
Different economic assumptions	1.2	3.2	16.4	24.2
Technical reestimates	12.2	19.9	22.1	23.0
Total Reestimates	13.5	23.1	38.5	47.2
President's Budget Reestimated	738.8	780.7	844.5	915.7

DIFFERENCES IN ECONOMIC ASSUMPTIONS

Economic conditions have major effects on federal budget outlays. About 30 percent of federal spending is directly indexed for inflation through automatic cost-of-living adjustments (COLAs). Social Security is the largest indexed program, accounting for 21 percent of total outlays in 1981. Other directly indexed programs include retirement benefits for federal civilian and military employees, veterans' pensions, railroad retirement benefits, and Supplemental Security Income benefits. Medicare and Medicaid costs, while not directly indexed for inflation, increase over time with the rising costs of medical care. The costs of certain other benefit programs, such as unemployment insurance and food stamps, vary with changes in the level of unemployment in the economy. Finally, the cost of servicing the federal debt depends on the level of interest rates. In sum, the economic variables having the largest effects on federal outlays are prices, unemployment, and interest rates.

The Congressional Budget Office recently published its baseline economic forecast for calendar years 1982-1983, together with longer-run economic assumptions for 1984-1987. 1/ The Administration's assumptions, which are explained in the President's February budget, are briefly discussed in Chapter II of this report. The following paragraphs describe the differences in these assumptions for the three variables that affect spending estimates--prices, unemployment, and interest rates.

1/ See Congressional Budget Office, The Prospects for Economic Recovery (February 1982).

Prices

Both the Administration and CBO project a further slowing of inflation over the next several years. The projected patterns of price increases differ somewhat, however, and CBO projects a more gradual decline in the rate of inflation than does the Administration. Federal outlays are particularly sensitive to annual COLAs for Social Security and other indexed benefit programs.

The Administration and CBO have identical assumptions for the 1982 and 1983 cost-of-living adjustments for Social Security benefits, but CBO is projecting COLAs for 1984 and 1985 that are about two percentage points higher than assumed for the Administration's budget estimates.

Annual Social Security COLAs (Percent)

	1982	1983	1984	1985
Administration	8.1	6.5	4.8	4.8
CBO	8.1	6.5	7.2	6.5

The Social Security COLA adjustments that are made in July of each year are based on the percentage increase in the Consumer Price Index for urban wage earners and clerical employees (CPI-W), measured from the first quarter of the preceding year to the first quarter of the current year.

In CBO's baseline projections, it is assumed that the Social Security COLAs will diminish in 1982 and 1983, increase again in 1984, and then resume their downward trend. The explanation for this pattern lies in developments in the CPI-W assumed by CBO for preceding calendar years.

- World oil prices are assumed to remain constant through the end of 1982, and then to increase at about the overall U.S. rate of inflation thereafter. Oil prices constitute about one-seventh of the CPI-W, either directly or through their impact on the costs of production of other goods and services.

- Mortgage interest rates are expected to decline through 1982, and then to stabilize in 1983. CBO assumes that house prices will rise enough in 1982 to offset this reduction in mortgage interest costs. Since homeownership costs have a weight of about one-quarter in the CPI-W, movements in interest rates and house prices can affect COLAs substantially.

Both of these factors tend to hold down the growth of the CPI-W in calendar year 1982 but not in 1983. Consequently, the Social Security COLA of July 1984 is projected to exceed that of July 1983. Nevertheless, the underlying rate of inflation, which is driven primarily by wage costs, is expected to be on a steadily declining trend throughout the projection period; therefore, with no further special factors operating, the COLA adjustments should resume their downward movement after 1984.

Unemployment and Interest Rates

For unemployment and interest rates, the Administration forecast and the CBO baseline forecast for 1982 are quite similar. The forecasts and assumptions also show similar patterns for 1983-1985--a declining unemployment rate, and falling interest rates (after 1983 in the case of the CBO assumptions). For each variable, however, CBO projects a more gradual change than does the Administration. As a result, these two variables are somewhat higher in the CBO baseline assumptions for 1983-1985 than in the Administration's assumptions.

The difference in the unemployment rate assumptions is largest in 1985. The Administration's budget estimates assume an unemployment rate of 6.4 percent in that year, whereas the CBO baseline assumptions project an unemployment rate of 7.2 percent. For 91-day Treasury bill rates, the differences range from 2.7 percentage points in calendar year 1983 to 1.8 percentage points in 1984 and 0.9 percentage points in 1985.

CBO Baseline Assumptions

The implications for budget outlays of the differences in the Administration and CBO baseline economic assumptions are shown in Table 24. Use of the CBO economic assumptions has little effect on outlays the first two years, adding only $1.2 billion in 1982 and $3.2 billion in 1983--mostly as a result of higher interest rates projected by CBO.

For 1984 and 1985, the outlay impact of CBO's baseline assumptions is much larger. Projected outlays in 1984 are raised by over $16 billion and in 1985 by $24 billion. The largest increases again are for interest costs. The higher interest rates projected by CBO add approximately $10 billion to outlays in 1984 and $7 billion to outlays in 1985. The higher budget deficits resulting from the application of CBO's economic assumptions to the Administration's budget estimates add another $2.5 billion in interest costs in 1984 and almost $5 billion in 1985.

TABLE 24. OUTLAY REESTIMATES BASED ON CBO'S BASELINE ECONOMIC ASSUMPTIONS (By fiscal year, in billions of dollars)

	1982	1983	1984	1985
Interest Costs				
Higher interest rates	0.9	1.4	9.8	6.6
Higher budget deficits	0.3	0.9	2.5	4.7
Social Security and Other Benefits Indexed to the CPI	---	a/	1.4	6.8
Other Benefits Affected by Inflation	---	0.1	0.9	2.2
Unemployment Compensation and Related Benefits	---	0.9	1.7	4.0
Total	1.2	3.2	16.4	24.2

a/ Less than $50 million.

The higher COLAs projected by CBO in 1984 and 1985 for Social Security and other indexed benefits add about $1 billion to 1984 outlays and close to $7 billion to 1985 outlays. The impact of the higher COLAs for 1984 is not fully felt until 1985. Other benefits affected by inflation--largely Medicare and Medicaid--also show somewhat higher outlays under CBO economic assumptions than projected by the Administration. The increase is relatively small in 1983 and 1984, but reaches nearly $2 billion by 1985.

The more slowly declining unemployment rate in CBO's baseline economic assumptions would raise projected federal outlays by approximately $1 billion in 1983, $2 billion in 1984, and over $4 billion in 1985. The bulk of these increased outlays is for unemployment insurance benefits. Outlays for food stamps, Aid to Families with Dependent Children (AFDC), and Medicaid are also somewhat higher.

Pessimistic Alternative

In developing its baseline economic assumptions, CBO prepared two sets of alternative assumptions--one more optimistic than the baseline assumption, the other more pessimistic. The Administration's economic assumptions are similar to the optimistic alternative. The pessimistic alternative takes account of the potential risks to the economy of a tight monetary policy combined with a stimulative fiscal policy. In this latter economic scenario, the three variables of inflation, unemployment, and interest rates are uniformly higher than in the CBO baseline assumptions (see Chapter II). If the economy were to follow the path of the CBO pessimistic alternative, outlays under the President's budgetary proposals would be much higher than estimated by the Administration, particularly in 1984 and 1985. As shown in Table 25, this alternative adds $12 billion to outlays in 1983, $36 billion in 1984, and $57 billion in 1985. For the entire 1982-1985 period, total outlays would be higher than the Administration's by over $100 billion.

TABLE 25. OUTLAY REESTIMATES BASED ON CBO'S PESSIMISTIC ECONOMIC ASSUMPTIONS (By fiscal year, in billions of dollars)

	1982	1983	1984	1985
Interest Costs				
Higher interest rates	1.5	6.9	19.1	19.1
Higher budget deficits	0.4	2.1	6.1	12.3
Social Security and Other Benefits Indexed to the CPI	---	0.2	3.0	11.5
Other Benefits Affected by Inflation	---	0.2	1.8	3.8
Unemployment Compensation and Related Benefits	---	2.9	5.9	10.2
Total	1.9	12.3	36.0	56.8

The CBO pessimistic assumptions demonstrate how sensitive the federal budget has become to interest rates. Higher interest rates would add $47 billion to federal outlays over the 1982-1985 period, accounting for almost one-half of the total increase under the pessimistic alternative. The remaining $60 billion of the increase can be attributed in roughly equal shares to higher inflation, higher unemployment, and higher budget deficits.

TECHNICAL ESTIMATING DIFFERENCES

Technical estimating differences between the Administration and CBO arise from the use of different assumptions about how quickly appropriated funds will be disbursed, from different programmatic assumptions, and from other factors. For 1982-1985, these technical estimating differences are quite large. The use of CBO estimating methods and programmatic assumptions increases the Administration's outlay estimates by about 2 percent in each year, beginning with about $12 billion in 1982 and averaging over $20 billion for each of the next three years. Over the entire period, these technical differences add more than $75 billion to total outlays. The major CBO technical reestimates are for defense procurement activities, farm price supports, net interest costs, and offsetting receipts from leasing Outer Continental Shelf (OCS) lands, as shown in Table 26.

TABLE 26. CBO TECHNICAL OUTLAY REESTIMATES (By fiscal year, in billions of dollars)

Major Program	1982	1983	1984	1985
Defense Procurement	2.9	1.4	2.6	2.8
Defense Operations	0.5	1.6	-0.3	-0.6
Farm Price Supports	5.1	5.6	2.7	2.4
Medicare	---	0.4	1.0	1.0
Social Security	1.0	0.9	1.2	-0.2
Net Interest	0.9	3.7	8.2	13.5
OCS Offsetting Receipts	0.9	5.2	4.8	3.2
Other (net)	1.0	1.1	2.0	0.9
Total	12.2	19.9	22.1	23.0

The CBO technical reestimates for defense procurement and defense operations result mainly from different assumptions about how quickly appropriated funds spend out over time. CBO's spending rate assumptions are derived from analyses of historical spending patterns, with particular emphasis on recent spending trends. CBO staff carefully monitor the monthly Treasury statements of actual outlays and consult with defense agency personnel to obtain the latest information on spending patterns. CBO's outlay estimates proved closer to the actual level for fiscal year 1981 than did the Administration's, and spending in the first quarter of 1982 has been consistent with CBO's estimate for the current fiscal year.

The CBO technical reestimate for farm price supports is based on more recent information about the outlook for farm production and commodity prices than was available for the Administration's budget estimates. The outlook has changed dramatically in the last two months, resulting in a substantial increase in the demand for government crop loans. The reestimate also reflects the Administration's voluntary set-aside program for wheat and feed grains, which was announced too late to be included in the February budget estimates.

The technical reestimate for Medicare reflects different assumptions about the utilization of hospital and physician services by the eligible population, hospital costs, and administrative costs of private contractors who process benefit claims. Both the Administration and CBO have underestimated Medicare spending in the past, as costs have continued to increase rapidly.

The CBO technical reestimate for Social Security benefits results mainly from the use of different assumptions about the growth in the number of beneficiaries. CBO staff carefully monitor program data on beneficiary population trends and other cost factors, and base their estimates on the most recent data available. The reestimate for Social Security is less than 1 percent of total program costs--well within the range of estimating error for this program.

The technical reestimate for net interest largely reflects the cost of servicing the higher deficit levels that would result from using CBO's technical reestimates for both revenues and outlays. The increased interest cost resulting from these higher deficits rises from $2.8 billion in 1983 to $9.9 billion in 1985.

The technical reestimate for OCS offsetting receipts reflects CBO's preliminary analysis of the Administration's proposed accelerated leasing program for Outer Continental Shelf oil- and gas-bearing lands. Based on actual experience to date with this program, discussions with industry experts, and the outlook for world oil prices, CBO believes that the February budget estimates are overly optimistic about the likely level of receipts to be derived from the accelerated program. A recent lease sale of Gulf of Mexico offshore lands produced less receipts than CBO expected, and the outlook for 1982 receipts is now much lower than previously estimated. The accelerated program should produce greater receipts, but the prospects for 1983 and beyond are very uncertain at this point.

CBO has also reestimated outlays of off-budget federal entities to take account of projected higher loan asset sales to the Federal Financing Bank (FFB). This technical reestimate adds over $500 million to projected FFB net outlays in 1982, almost $800 million in 1983, over $900 million in 1984, and more than $1 billion in 1985.

UNEVALUATED ADMINISTRATION SAVINGS ESTIMATES

The Congressional Budget Office has been unable to evaluate some of the Administration's outlay estimates, mainly because of a lack of information. Estimated savings from several proposed management initiatives, for example, cannot be evaluated until they have been carried out. These include the prevention of waste, fraud, and abuse in unspecified programs; improved debt collection; and the sale of surplus federal property. The Administration projects savings from these initiatives at $7.0 billion by 1985, a target that appears optimistic in light of past experience.

Spending estimates sometimes reflect estimating biases, which may be either upward or downward depending upon the kinds of policies being advocated. For example, all administrations tend to overestimate outlays for new programs. The Administration's outlay estimates for the new hazardous substance response trust fund are a case in point (see Function 300 reestimates). On the other hand, federal agencies also tend to overestimate the savings to be achieved through administrative or other economies. This would appear to be the case for many of the management initiatives included in the February budget estimates, especially the unallocated targets in Functions 920 (allowances) and 950 (undistributed offsetting receipts). Since no supporting information is available for these initiatives, CBO has not been able to make an independent evaluation.

The President's February budget also includes estimated savings from future legislative proposals not yet developed. For example, savings of nearly $2 billion in 1984 and over $4 billion in 1985 are included for health care financing reforms in the Medicare programs. Similar estimates were included in the Administration's budget projections last year, but a specific legislative proposal has not yet been developed. CBO has no basis, therefore, for evaluating the accuracy of these estimates.

Table 27 provides a list of the savings estimates in the President's February budget that CBO was unable to evaluate and, therefore, did not include in its technical reestimates. They are described in more detail in the function-by-function discussion that follows.

TABLE 27. UNEVALUATED ADMINISTRATION SAVINGS ESTIMATES (By fiscal year, in billions of dollars)

Function and Program	1982	1983	1984	1985
Health (550)				
Reform of health care financing (future legislation)	---	---	-2.0	-4.1
Other health care program savings	---	-0.4	-0.4	-0.5
Allowances (920)				
Prevention of fraud, waste, and abuse	-1.0	-1.0	-1.0	-1.0
Undistributed debt collection	---	-1.0	-1.0	-2.0
Undistributed Offsetting Receipts (950)				
Disposition of federal surplus property	---	-1.0	-4.0	-4.0
Total	-1.0	-3.4	-8.4	-11.5

OUTLAY REESTIMATES BY MAJOR FUNCTION

This section provides further details on the CBO technical analysis of the Administration's outlay estimates for fiscal years 1982-1985 for each major functional category of the budget. The reestimates for different economic assumptions were derived by using CBO's baseline assumptions.

FUNCTION 050: NATIONAL DEFENSE

(Outlays in millions of dollars)

	1982	1983	1984	1985
President's February Budget	187,497	221,068	252,969	292,075
Preliminary CBO Reestimates				
Different economic assumptions				
Retired pay	---	-28	168	510
Technical reestimates				
Operations	466	1,583	-306	-635
Procurement	2,950	1,403	2,587	2,753
All other, net	-100	-1,120	-632	-664
Total, Reestimates	3,316	1,838	1,817	1,964
President's Budget Reestimated	190,813	222,906	254,786	294,039

EXPLANATION OF PRELIMINARY CBO REESTIMATES

Different Economic Assumptions

Retired Pay. The costs of military retired pay benefits rise automatically with increases in the Consumer Price Index. The cost-of-living adjustment (COLA) for 1982—8.7 percent—is already known based on actual data through December 1981. CBO and the Administration have similar COLA assumptions for 1983, but CBO projects higher COLAs for 1984 and 1985, as shown below. The use of CBO's COLA assumptions adds $650 million in outlays over the 1983-1985 period.

Annual Military Retired Pay COLAs (Percent)

	1982	1983	1984	1985
Administration	8.7	6.6	4.9	4.8
CBO	8.7	6.3	7.2	6.6

Technical Reestimates

The Administration and CBO use comparable methods to estimate defense outlays. Computations for 1982 and 1983 are based on account-level detail, and subsequent years' estimates are based on title-level aggregations consistent with the 1982-1983 analysis. The resulting projections may differ because of factors not easily measured--for example, the outlay impacts of economic conditions and acquisition policies.

The historical spending rates used by both CBO and the Administration actually may understate future spending rates. Factors indicating possible spending rate increases include:

- Greater use of multiyear procurement;
- Greater economic production levels;
- The slowdown in the economy, especially in commercial aviation, prompting more immediate action on defense contracts;
- Faster progress payments to ease contractors' needs for working capital and to induce earlier deliveries; and
- Shorter lead times on materials and components used in weapon systems production.

Last year there were large technical estimating differences between the Administration and CBO for defense outlays. Although these differences persist, they have narrowed considerably, largely because the Administration raised its estimates to reflect actual experience. The estimating differences that remain primarily reflect different judgments about the timing of outlays, such as how quickly procurement funds will be disbursed for major weapon systems and when the effect of a large supplemental appropriation bill for operations will appear. Using 1981 estimates as a test case, CBO had a better track record than the Administration for procurement and operations activities. Actual 1981 outlays for each of these activities were within $0.2 billion of CBO's estimates, but about $1.0 billion apart from the Administration's estimates.

Operations. CBO estimates that outlays for operations and maintenance (O&M) and for the revolving and management funds will exceed Administration estimates by $0.5 million in 1982 and $1.6 million in 1983. CBO estimates for these accounts are derived from historical outlay rates that proved to be very accurate for 1981. For 1982, actual operations outlays for the first four months of the year are consistent with CBO's higher estimate for the entire year.

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The CBO estimate for 1983 is based on the same spendout rates used in its analysis for 1981 and 1982. In addition, CBO expects that enactment of the proposed 1982 supplemental will occur late in the year—as was the experience in 1981—causing most of the outlays to occur in 1983. The Administration's estimates, in contrast, assume earlier enactment of the proposed supplemental, with most of the spending occurring in 1982. This difference in assumptions raises CBO's estimate for 1983 outlays about $358 million over the Administration's (in 1982, it has the opposite effect by $469 million).

Also, CBO expects that 1983 appropriations to the revolving funds will disburse at the average rate for O&M purchases (about 76 percent in the first year), and that usual revolving fund transactions will net to zero, consistent with general cash management goals. The Administration, on the other hand, outlays revolving fund appropriations at 100 percent, but this higher estimate is more than offset by its lower estimates for other activities not requiring appropriations.

For 1984 and 1985, CBO estimates are lower than the Administration's for reasons that are somewhat harder to discern. The effects of changes in program mix are less evident within operation and maintenance accounts. Most categories of O&M spending appear to increase, but the absence of any clear criteria for separating fast-spending from slow-spending programs prevents decisive outlay analysis. Consequently, CBO uses essentially the same outlay rates for the outyears as for 1981, 1982, and 1983. One possible explanation for the outyear estimating differences is that CBO adjusts the rate downward to reflect a somewhat greater proportion of slower-spending purchases in the outyears and the outlay impact of unused or lapsing budget authority.

Between 1977 and 1980, the Defense Department had average annual lapses of about $99 million in O&M accounts; in 1981, O&M lapses totaled about $332 million. Lapses represent funds that were not obligated and therefore will not be spent; they represent a floor for total unexpended funds because some obligations are never liquidated. CBO's outlay rates for O&M accounts assume that about 1 percent of budget authority is never spent; this assumption recognizes an annual phenomenon that would otherwise raise outlays.

Procurement. Procurement outlays have grown in line with in CBO's estimates of March 1981; for the first three months of fiscal year 1982, they have exceeded CBO estimates by about $100 million, averaging $3.4 billion per month. The Administration's estimate for 1982, $41.3 billion, implies average monthly outlays of $3.4 billion, or no growth between now and the end of 1982. Its estimate for 1983, $55.1 billion, implies average monthly outlays of $4.6 billion, 33.4 percent higher than in 1982. CBO assumes that procurement outlays will grow gradually following the sharp increases in appropriations in 1980 and 1981. Consequently, CBO believes that the Administration's estimates for 1982 are too low; the implicit growth rate is too irregular to be consistent with historical data and the implementation of the approved procurement program.

Actual procurement obligations for the 12-month period ending in November 1981 averaged $4.0 billion per month. As a result, procurement outlays should rise to about $4 billion per month at the end of 1982. This would produce a 1982 average of $3.7 billion per month, or $0.3 billion higher than estimated by the Administration. The Administration's obligation plans call for $4.8 billion per month in 1982 growing to $6.7 billion per month in 1983. CBO estimates that 1983 outlays will grow to average about $4.7 billion per month, only slightly higher than the Administration estimates. Consequently, the estimating difference for 1983 procurement outlays is relatively small.

The CBO outlay estimates for 1984 and 1985 assume that the mix of spending programs for procurement activities will be consistent with the programs for 1982 and 1983, as shown in the following table. The Administration's goal of a 600-ship Navy does not necessarily mean that the slow-spending shipbuilding account will receive a significantly increasing share of future procurement budget authority; other expensive programs will be competing with shipbuilding for budget authority, including: the MX missile, B-1 bomber, improved strategic command and control, tracked combat vehicles (for example, M-1 tanks and Fighting Vehicles), and tactical aircraft for an additional four Air Force air wings, an additional two carrier air wings, and continued modernization of current forces.

If the Administration continues a relatively higher priority for spare parts and support equipment programs than was the case in recent years, overall spending rates will exceed the historical average. Outlays for spare parts programs will not be faster than for major end items when the spare parts programs are only big enough to fund initial provisioning. However, when the programs expand to make up for past shortfalls in replenishment spares, as in the 1982 budget, one can expect these spare parts programs to be executed well ahead of the major end-item program. The CBO estimates do not anticipate an acceleration in outlay rates for this shift in program composition; to that extent, CBO's projections may underestimate procurement outlays.

CBO Outlay Estimates For Defense Procurement Based on the President's February Budget Authority Request

	1982	1983	1984	1985	1986	1987
			Billions of Dollars			
Budget Authority (BA)	65.7	89.5	101.9	125.5	142.8	155.1
Outlays from						
1981 and prior BA	35.9	21.5	8.3	4.1	2.3	0.3
1982 BA	8.4	24.6	19.7	6.7	3.3	1.7
1983 BA	0	10.5	32.1	26.2	9.4	5.3
1984 BA	0	0	12.5	38.3	30.5	10.0
1985 BA	0	0	0	15.7	48.0	37.9
1986 BA	0	0	0	0	17.8	54.6
1987 BA	0	0	0	0	0	19.1
Total Outlays a/	44.3	56.5	72.6	91.0	111.3	129.0
			Percent			
Implicit Outlay Rates from New BA for						
1982	12.9	37.8	30.0	10.0	4.9	2.4
1983		11.7	35.9	29.3	10.5	5.9
1984			12.3	37.6	29.9	9.8
1985				12.5	38.2	30.2
1986					12.5	38.3
1987						12.3

a/ Details may not add to totals because of rounding.

All Other, Net. CBO estimates lower outlays than the Administration for most remaining categories of defense spending. The CBO estimate for military retired pay shows less growth in the annuitant population, consistent with past CBO estimates. The Administration has lowered its estimates of retired pay from levels projected last year to come closer to CBO's projections. The Administration's outlay estimate for the 1982 pay raise appears to be based on a combined outlay rate for military personnel and O&M to include slower spending purchases; CBO uses a higher rate, one pertaining to pay only, causing its estimate to be about $230 million higher in 1982 and lower by the same amount in 1983. The remaining differences arise from different analytical interpretations of historical spending data. The CBO reestimates for these other national defense programs are summarized in the following table.

CBO Technical Reestimates for Other Defense Programs (By fiscal year, in millions of dollars)

	1982	1983	1984	1985
Military Personnel	-18	-49	-75	-125
Retired Pay	---	-142	-249	-290
RDT&E	68	-330	-76	223
Military Construction	-162	-461	-232	-472
Family Housing	-172	47	---	---
Pay Raises	230	-230	---	---
Other	-46	45	---	---
Total	-100	-1,120	-632	-664

FUNCTION 150: INTERNATIONAL AFFAIRS

(Outlays in millions of dollars)

	1982	1983	1984	1985
President's February Budget	11,074	11,968	12,323	12,990
Preliminary CBO Reestimates				
Different economic assumptions				
Export-Import Bank	15	8	16	27
Exchange Stabilization Fund	-22	-43	-70	-41
Technical reestimates				
Export-Import Bank	-17	-221	249	-60
Exchange Stabilization Fund	135	179	172	174
Foreign military sales credit	-5	88	-51	-87
Public Law 480 food aid	-138	-14	---	---
Other	61	---	---	---
Total Reestimates	29	-3	316	13
President's Budget Reestimated	11,103	11,966	12,639	13,003

EXPLANATION OF PRELIMINARY CBO REESTIMATES

Different Economic Assumptions

Estimated outlays by the Export-Import Bank and the Exchange Stabilization Fund are sensitive to interest-rate assumptions. Higher interest rates increase the cost of the Export-Import Bank's borrowing to finance its loans, but also result in greater interest income for the Exchange Stabilization Fund on its holdings of U.S. securities. The net effect of CBO's higher interest-rate assumptions, therefore, is quite small for these two programs.

Technical Reestimates

Export-Import Bank. The Bank has restricted new loans on aircraft to newer-generation commercial jets. The 1982 loan commitments may include a large nuclear power project. Payments made on these contracts will be lower than the average historical disbursement pattern for Bank loans. The effect of this change in program mix will be to lower outlays in 1983 from the level estimated in the budget, but to raise outlays in 1984 as disbursements slip from one year into the next.

Exchange Stabilization Fund. The Secretary of the Treasury is authorized to use the resources of the Exchange Stabilization Fund and foreign exchange and other instruments of credit and securities in matters regarding orderly exchange management. Funds not being used in exchange transactions are invested in interest-bearing U.S. securities. Estimated negative outlays are interest earnings on those U.S. securities.

The Administration's estimate is based on an opening balance of $3.1 billion. In November, $1.5 billion of the securities were used to repay the Treasury for advances to the Fund on drawings from the International Monetary Fund, thereby lowering the principal of securities held and the estimated interest income. The Administration's February budget estimates for 1982-1985 do not reflect the lower balance of securities held by the fund. As a result, the February budget overestimates interest income by the fund during this period.

Foreign Military Sales Credit. The President is requesting an expanded direct credit sales program to assist friendly countries with the purchase of defense articles and services. The direct credits may be tied to particular procurement cases or provided as cash-flow financing of all sales cases for a country. Funds provided as cash-flow financing are fully disbursed in the fiscal year provided, whereas credits tied to new sales cases take up to five years to be spent.

Over one-half of the proposed direct credits for 1983-1985 are expected to be used for cash-flow financing. If this is done, 1983 outlays are underestimated in the February budget and overestimated for 1984 and 1985. The CBO reestimate assumes that there will be $900 million in cash-flow financing provided in each of these three years.

Public Law 480 Food Aid. The February budget estimate for 1982 assumes full disbursement of all new funds appropriated for this fiscal year plus all of the unspent balances carried over from the previous year. Historically, there has been a lag between the obligation of funds for this program and their payment, which results in obligated but unspent balances at the end of each year on the order of $140 million. The Administration has not provided any rationale to suggest that this historical pattern will not continue in 1982. Accordingly, CBO believes that the Administration has overestimated 1982 outlays by $138 million.

Other. A number of minor estimating differences for other programs in this function for 1982 result from the use of different spending rate assumptions. The CBO reestimate for these programs represents the difference between its previous scorekeeping tabulations and the Administration's latest estimates.

FUNCTION 250: GENERAL SCIENCE, SPACE, AND TECHNOLOGY

(Outlays in millions of dollars)

	1982	1983	1984	1985
President's February Budget	6,942	7,633	7,779	7,379
Preliminary CBO Reestimates				
Different economic assumptions	---	---	---	---
Technical reestimates				
General science	-34	---	---	---
National Science Foundation	-8	---	---	---
NASA space flight	54	---	---	---
NASA space science	38	---	---	---
Other	12	---	---	---
Total Reestimates	62	---	---	---
President's Budget Reestimated	7,004	7,633	7,779	7,379

EXPLANATION OF PRELIMINARY CBO REESTIMATES

Different Economic Assumptions

This function has no reestimates resulting from different economic assumptions.

Technical Reestimates

General Science. The President proposes to transfer the Department of Energy's General Science and Research Activities program to the Department of Commerce's Energy Research and Technology Administration. In so doing, the Administration's latest budget estimates imply that 1982 spending will accelerate nearly 10 percent from previously estimated levels. The CBO reestimates assume that the rate of spending will not change with the proposed reorganization.

National Science Foundation. The National Science Foundation's Research and Related Activities account is the principal source of grants to year 1982, the latest Administration budget estimates indicate unusually high outlays in this account from prior-year contractual obligations. Although CBO anticipates an acceleration of spending out of prior-year obligations, it assumes a somewhat slower rate than the Administration's.

NASA Space Flight. This program incorporates the development, production, and operation of the Space Shuttle; the procurement and operation of the Spacelab for use with the Shuttle; and the development and procurement of expendable vehicles to launch satellites and planetary exploration spacecraft. CBO estimates that 1982 outlays for this program will be approximately $55 million greater than the Administration's expectations. CBO sees greater outlays associated with maintaining the delivery schedule of the second orbiter "Challenger" and faster spending associated with shuttle operations. This program is evolving from its development, test, and production stage into its operations phase. (The two flights planned for Columbia during fiscal year 1982 are scheduled to be the final flights in the shuttle's developmental stage.) As the program becomes operational, CBO estimates that spending will accelerate. The flow of actual outlays to date supports this.

NASA Space Science. This program includes funds for the physics and astronomy, planetary exploration, life sciences, and space and terrestrial applications programs of the National Aeronautics and Space Administration. Among the specific development projects funded are the space telescope, the gamma ray observatory, the Spacelab payload, Explorer, and the Galileo mission to Jupiter. CBO estimates outlays for this account to be $39 million more than the Administration's projections. This difference stems from CBO's expectations of greater costs for the development of these projects and from the Administration's use of spending rates inconsistent with the previous fiscal year's experience and with actual outlays to date.

FUNCTION 270: ENERGY

(Outlays in millions of dollars)

	1982	1983	1984	1985
President's February Budget	6,413	4,215	3,807	3,756
Preliminary CBO Reestimates				
Different economic assumptions	---	---	---	---
Technical reestimates				
Fossil energy	131	230	41	-17
Energy supply	158	9	-3	-103
Uranium enrichment	46	45	20	-20
Naval Petroleum Reserves	-97	-138	-175	-146
Energy production	-80	-68	-32	-4
Departmental administration	---	72	55	-1
Other	1	---	---	---
Total Reestimates	159	150	-94	-291
President's Budget Reestimated	6,572	4,364	3,713	3,465

EXPLANATION OF PRELIMINARY CBO REESTIMATES

Different Economic Assumptions

This function has no reestimates resulting from different economic assumptions.

Technical Reestimates

Fossil Energy. CBO estimates that outlays for fossil energy programs will be $131 million higher than estimated by the Administration in 1982 and $230 million higher in 1983. CBO's analysis indicates that more than $600 million in obligated balances and $195 million in unobligated balances were available to be spent at the beginning of fiscal year 1982. An additional $417 million was appropriated in 1982 for fossil energy programs. CBO's estimate assumes that spending from these balances and the 1982 appropriation will occur at rates consistent with historical spending patterns. The

Administration's estimate assumes spending from prior-year obligations at a rate much slower than experienced by the program in recent years. The Administration's estimates also apparently assume a deferral of $45 million that is not specified in the February budget and has not yet been transmitted to the Congress. CBO's reestimate does not reflect the possible deferral. CBO's analysis reveals that without future deferrals or rescissions the estimated outlays projected by the Administration for these programs will be difficult to achieve.

Energy Supply. CBO believes that the Administration underestimated outlays for solar, nuclear, and other nonfossil energy programs by $158 million in 1982. The CBO reestimate assumes that a substantial portion of the approximately $1.6 billion in obligated balances incurred before 1982 will be disbursed during 1982. This assumption is based on information provided by the Department of Energy (DOE) concerning spending patterns for the nonconstruction energy supply programs indicating that more than 90 percent of all obligations will be disbursed within two years of obligation. Funds for construction programs are projected to spend over three years, with the largest proportion of spending occurring in the second year. The Administration's estimates of outlays reflect a rate of spending from prior obligations slower than the program has experienced in the past.

Uranium Enrichment. CBO's estimate of outlays for uranium enrichment exceeds the Administration's estimate by approximately $45 million in both 1982 and 1983. The difference results from CBO's lower estimate of uranium enrichment revenues, based on information provided by the Administration and an analysis of previous revenue projections. The Administration has consistently overestimated these revenues. Its July and September estimates for revenue from commercial sales totaled nearly $2.2 billion for 1983. In July, CBO had projected revenues of approximately $2.1 billion for 1983. The Administration now projects revenues from commercial sales of approximately $2.1 billion, near the CBO estimate.

Naval Petroleum Reserves (NPR). Receipts from the sale of petroleum products are estimated by CBO to be $97 million higher in 1982 than estimated by the Administration. CBO's estimate is based on an oil price for NPR-1 oil of approximately $30.70 per barrel in 1982 and a windfall profits tax payment of approximately $520 million. CBO believes that the Administration overestimated the payment for the windfall profits tax and thus underestimated NPR receipts. Using the Administration's estimates for total oil revenue from the reserves, and assuming a base price of $12.81 per barrel of oil, CBO estimates the windfall profits tax payment at approximately 35 percent of the revenue from oil sales, or $550 million in 1982. This is almost $90 million less than estimated by the Administration. Therefore, net receipts from the NPR would increase by $90 million in 1982.

Energy Production. Based on information provided by the Administration and an analysis of program activity at the Naval Petroleum Reserves, CBO estimates that outlays in 1982 will be $80 million less than projected by the Administration. The Administration projects faster spending of new obligations in 1982 than in the last several years and thus projects outlays of $294 million, twice the level experienced in 1981. CBO projects slower spending because of the proportion of construction activity under this account. Based on information provided by the Department of Energy concerning construction activity, CBO assumes that outlays will reflect the time needed to complete a construction activity once it has been commissioned. This results in a large proportion of outlays occurring after the year in which construction begins. Outlays would reach the levels projected by the Administration only if construction activity were completed at a rate faster than that which has occurred at the reserves in the past.

Departmental Administration. The Administration's projected outlays are below the level that would be expected to result from the amounts appropriated and from the prior balances in this account. The level of unspent obligated balances that would be maintained throughout fiscal years 1983-1987 is inconsistent with both past trends and the mix of activities in the account. CBO's estimate assumes that the $198 million in prior balances at the start of fiscal year 1982 will be spent by 1984, and that program spending will follow historical patterns. As a result, CBO's outlay estimate is $72 million higher than the President's in 1983 and $55 million higher in 1984.

FUNCTION 300: NATURAL RESOURCES AND ENVIRONMENT

(Outlays in millions of dollars)

	1982	1983	1984	1985
President's February Budget	12,626	9,911	8,359	7,732
Preliminary CBO Reestimates				
Different economic assumptions	---	---	---	---
Technical reestimates				
EPA construction grants	-20	350	480	150
Hazardous substance response trust fund	-55	-89	-90	-84
Offsetting receipts, primarily from onshore mineral leasing and sale of timber	322	324	400	574
Other	-75	19	78	18
Total Reestimates	172	604	868	658
President's Budget Reestimated	12,799	10,515	9,227	8,390

EXPLANATION OF PRELIMINARY CBO REESTIMATES

Different Economic Assumptions

This function has no reestimates resulting from different economic assumptions.

Technical Reestimates

EPA Construction Grants. CBO has reestimated upward outlays for Environmental Protection Agency (EPA) construction grants in 1983 to 1985, because the Administration estimates do not adequately reflect the likely spending in those years from previous years' obligations. The construction grants program provides funds to states and municipalities to plan, design, and construct wastewater treatment facilities. Once obligated, grant awards for construction are spent over several years, frequently taking seven or more years to be entirely expended. Projects usually have small outlays in the first year after funds have been obligated, with the bulk of outlays falling between the second and fifth years after obligation. Consequently, large changes in obligational authority for the program do not result in immediate changes in outlays. The President's budget, however, projects a sharp decline in outlays only one year after a corresponding drop in obligations.

The Administration estimates that only $3.4 billion will be obligated in 1982, and projects that obligations will drop further to $2.4 billion in 1983 and to $2.0 billion in 1984 and 1985. The February budget estimates also show a rapid decline in outlays from the estimated $4 billion level in 1982, with outlays dropping to $2.8 billion by 1984. Based on past experience, and in view of the large size of obligated balances from previous years' appropriations, a more gradual decline in outlays is likely, which is reflected in CBO's reestimate.

Hazardous Substance Response Trust Fund. The CBO outlay estimates for the hazardous substance response trust fund, commonly known as the "Superfund," are substantially lower than the Administration's for 1982 through 1985. CBO believes that the Administration has assumed unrealistically high obligation and outlay rates for this new and controversial program. Money in the Superfund is to be spent primarily for short-term response to uncontrolled releases of hazardous substances posing an immediate health or safety threat and for longer-term cleanup action at hazardous waste sites (such as Love Canal).

Most new programs start slowly; yet administration budgets typically overestimate how quickly funds will be spent. For this new program, $75 million was provided in 1981 budget authority, of which $40 million was obligated and only $8 million was spent. Experience to date suggests that the very process of obligating funds--determining which sites warrant remedial action--will be lengthy. There are over 10,000 potential sites, and differences are sure to arise regarding which most merit federal remedial action. Once sites have been chosen, site evaluation and project design and construction will likely take three or more years to complete. Thus, outlays will occur gradually over a few years once funds are obligated. The Administration has assumed that obligations in 1982 and 1983 will equal 1982 and 1983 budget authority levels and that 95 percent of obligations will be spent within two years of obligation. The CBO reestimate assumes slower rates of obligations and outlays that are more in line with new programs.

Offsetting Receipts. The offsetting receipts in this function are derived mainly from the sale of timber on public lands and onshore mineral leasing, and appear in the budget primarily in subfunctions 300 and 302.

Historically, the Administration's estimate for function 300 offsetting receipts has been overly optimistic. In fact, in three of the past four years, the President's original budget estimate has been higher than the actual amount received and has been modified upward in January of the following year. The overestimates ranged from 3 to 7 percent above the actuals in the original budget requests for those years, and grew to between 5 and 22 percent over the actuals during the mid-year review. In fiscal year 1981, CBO's estimating methods for these receipts resulted in a January estimate that was about $160 million (or 7 percent) closer to actual receipts than the Administration's.

In fiscal year 1982, the Administration is projecting that function 300 receipts will grow by 49 percent, or $1,109 million, over the 1981 actual receipts of $2,283 million. If this increase occurs, it would be the largest increase ever, both in magnitude and as a percentage of the previous year's actual total. Of this increase, approximately $400 million is expected from the sale of timber by the Forest Service (FS), and approximately $700 million from increased receipts by the Department of the Interior (DOI), primarily from onshore mineral leasing. CBO's estimate of FS timber receipts in fiscal year 1982 is $127 million lower than the Administration's because of lower timber price assumptions. In addition, the CBO estimate for DOI receipts is approximately $195 million below the agency's. A large portion of this reestimate can be explained by actual receipts in January from offerings in the National Petroleum Reserve--Alaska (NPRA). Receipts realized were approximately $100 million less than anticipated by DOI. The remainder of CBO's reestimate for DOI receipts stems from lower timber and oil and gas price assumptions.

The estimate in the President's budget for fiscal year 1983 represents an additional increase of $664 million, or 20 percent, over the 1982 estimate for these receipts. Virtually all of the increase (92 percent) is expected to result from timber receipts; the volume of timber cut and the price received for this timber are anticipated to increase concurrently by 25 percent. Information from the agency indicates that these increases are expected because of pending expiration of existing contracts and increased activity in new housing construction. CBO also anticipates that these factors will produce large increases in timber harvest, but projects more moderate price increases consistent with historical timber price patterns. Thus, in fiscal year 1983, the CBO estimate for FS timber receipts is approximately $324 million below the Administration's.

The President's five-year budget projections include increases in function 300 receipts of $665 million in fiscal year 1984. This large increase is expected partly as a result of increases in price and volume of timber cut. In addition, DOI receipts in that year are expected to grow significantly because of large increases in onshore mineral receipts from increased coal production and renegotiation of coal royalty contracts. CBO expects that increases in receipts as a result of these factors will be more moderate, and continues to project lower timber prices in that year. Thus, CBO's estimate of receipts in 1984 is $400 million lower than the Administration's.

For 1985, the Administration projects an increase of $574 million as a result of continued renegotiation of coal leases, continued growth in the volume of coal to be mined, and large natural gas price increases after the scheduled January 1, 1985, price decontrol. Although CBO anticipates that increased receipts will result from these factors, CBO's estimate remains $575 million below the Administration's, largely because of a slower anticipated rate of response to the changes mentioned.

These technical reestimates of receipts will cause reestimates in function 850--where payments to states resulting from timber and mineral leasing receipts appear in the budget.

Other. CBO also has a number of smaller technical reestimates for programs in this function. The Administration has estimated 1982 outlays for the urban park and recreation fund at $64 million. This program was initiated in 1979 to provide grants to cities for improving deteriorated park and recreation facilities. Funded projects involve construction, and larger ones are likely to take three to four years to complete. Obligations for grants in 1979 through 1981 were nil, $57 million, and $66 million, respectively. Total outlays in those years were $200,000, $4 million, and $18 million. Based on obligations to date and the length of time needed to complete funded projects, CBO has estimated a more gradual rate of spending. As a result, CBO estimates outlays for this program to be $25 million lower than the Administration estimates in 1982, and $20 million higher in 1984.

CBO has also reestimated downward by $39 million the Administration's 1982 outlay estimate for EPA's salaries and expenses account because the Administration has assumed a 95 percent first-year outlay rate. In recent years, this rate has not exceeded 90 percent.

FUNCTION 350: AGRICULTURE

(Outlays in millions of dollars)

	1982	1983	1984	1985
President's February Budget	8,633	4,494	5,090	4,586
Preliminary CBO Reestimates				
Different economic assumptions	---	---	---	---
Technical reestimates				
Farm price supports	5,052	5,563	2,681	2,422
Agricultural credit	66	177	36	122
Other	-45	---	---	---
Total Reestimates	5,072	5,740	2,717	2,544
President's Budget Reestimated	13,705	10,234	7,807	7,130

EXPLANATION OF PRELIMINARY CBO REESTIMATES

Different Economic Assumptions

This function has no reestimates resulting from different economic assumptions.

Technical Reestimates

Farm Price Supports. CBO estimates that Commodity Credit Corporation (CCC) outlays for farm price supports and related programs will be $11.4 billion in 1982 and $7.4 billion in 1983. These amounts exceed the Administration's February budget estimates by $5.1 billion and $5.6 billion, respectively. CBO's estimates are based on the most recent production assessment and reflect the deteriorating outlook for exports resulting from political tensions with the Soviet Union and an embargo on exports to Poland. The recent announcements of 1982 crop planting restrictions and increased support levels have also been incorporated.

As shown in the following table, 60 percent of 1982 outlays are expected to be for wheat, feed grain, and cotton programs; in 1983 these

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programs account for 53 percent of estimated CCC outlays. Record harvests and low farm prices result in direct deficiency payments to be made to producers and increase the demand for commodity loans. Of these commodity loans, $6.3 billion in 1982 and $1.4 billion in 1983 are loans and storage payments for wheat and feed grain placed in the farmer-owned reserve where they are likely to stay until corn prices rise more than 27 percent and wheat prices 25 percent. Storage payments must be continued on grain in the reserve until prices increase to the release level; these payments are estimated to be $600 million annually.

CBO Estimates of Major CCC Program Expenditures (In millions of dollars)

	1982	1983	1984	1985
Wheat	1,817	1,231	491	450
Feed grain	5,223	2,070	847	418
Cotton	950	629	214	153
Dairy	1,907	1,972	1,814	1,695
Interest	1,370	1,300	1,200	1,100
Other	84	180	345	302
Total	11,351	7,382	4,911	4,118

Dairy outlays reflect continuing growth in production in spite of reduced increases in dairy price supports. Net government removals of dairy products remain about 10 percent of production in 1982 and 1983. Because the expenditures for dairy supports are outright purchases, no offsetting receipts are expected.

Net interest outlays are those interest payments owed the Treasury from the use of permanent borrowing authority, now at 14 percent, to fund commodity support programs less interest paid by farmers on commodity loans and storage facility loans and by users of export credits. Interest on direct payments to producers, cumulative dairy purchases, and administration and operating expenses comprise part of the net interest estimate. In addition are interest owed on grain reserve loans, which farmers are not required to pay after the first year, and interest paid on loans of commodities such as tobacco, which were made in previous years at rates well below current borrowing costs.

The large increases in CBO's estimate of CCC outlays above the President's February budget arise because the Administration had to prepare its budget estimates during the conference on the 1981 farm bill. Not only do these estimates not incorporate the most recent production estimates, they predate the imposition of martial law in Poland and the subsequent embargo on exports. Next to the Soviet Union, Poland is the largest Eastern Bloc customer for U.S. grain exports. Under the embargo, 1982 feed grain export estimates have declined 325 million bushels. More than $800 million in reserve loans will be spent if the entire decrease in exports is placed in the farmer-owned reserve. In addition, the Secretary of Agriculture announced in January a program for the 1982 crops that requires a 15 percent set-aside of wheat, cotton, and rice acreage and a 10 percent set-aside of feed grain acreage as a condition for receiving increased price supports. For wheat, the loan rate is increased 35 cents per bushel and the reserve loan rate 50 cents per bushel; for corn, the rate is up 15 cents to $2.55 per bushel and the reserve loan rate up 35 cents to $2.90 per bushel. The set-aside requirement will reduce eligibility for price supports in 1983 below the unrestricted program available in 1982; however, even with modest participation, 395 million bushels are projected to enter the reserve and net commodity lending is estimated to be $2.1 billion, while deficiency payments and reserve storage costs are estimated to be $1.4 billion.

The greatest difference between the CBO and Administration estimates is in the estimates of crop and dairy production underlying program costs. The President's budget estimates of CCC outlays are based upon 1981 crop conditions estimated in the August 1981 crop reports. As a result, they do not reflect the considerable revisions that have been made in crop estimates as reported in the February 1982 U.S. Department of Agriculture (USDA) World Agricultural Supply and Demand Estimates. These changes and their impact on farm price supports are discussed in the following sections.

Commodity Loan Programs

The most significant change in relation to outlay estimates is the one-billion-bushel increase in the farmer-owned corn grain reserve. In August, the Department of Agriculture forecast an increase in the reserve to 250 million bushels, and the Administration's total CCC outlay estimate is consistent with that forecast. By February 3, 1982, however, 958 million bushels had actually been placed in the reserve and the department increased its estimates to 1,250 million bushels for the year, a fourfold increase (see the following table). For each bushel a farmer places in the reserve, he receives a $2.55 loan plus a $0.265 storage payment. Based on the USDA estimate of 1,250 million bushels entering the reserve, and on the assumption that each farmer receives $2.82 for each bushel placed in the reserve, corn loan outlays for 1982 will be at least $3.5 billion dollars. These corn loans cannot be redeemed by farmers unless the farm price of corn averages above $3.15 per bushel. This is $0.67 per bushel higher than the season average farm price forecast by the Department of Agriculture for fiscal year 1982. Nor is it likely that much of this corn will be redeemed by farmers during fiscal year 1983 either.

Supply and Demand Estimates for Corn

	August 1981	February 1982	Percent Change
Area Planted (millions of acres)	84.3	84.2	0
Area Harvested (millions of acres)	74.1	74.6	+1
Yield per Acre (bushels)	104.3	109.9	+5
Production (millions of bushels)	7,735	8,201	+6
Domestic use	5,025	5,035	0
Exports	2,450	2,175	-11
Total Use	7,475	7,210	-4
Farmer-Owned Reserve Stocks	250	1,250	+500
CCC Inventory Stock	225	315	+140
Tree Stock	802	461	-43
Total Ending Stock	1,277	2,026	+59
Estimated Average Farm Price (dollars per bushel)	2.95	2.48	-16

SOURCE: World Agricultural Supply and Demand Estimates Approved by the U.S. Department of Agriculture World Agricultural Outlook Board.

As of February 3, 1982, in addition to the 958 million bushels farmers had placed in the corn farmer-owned reserve, 713 million bushels of corn had been pledged for nine-month nonrecourse loans. For each bushel put under loan, a farmer receives $2.40. During January, the CCC was charging interest of 12.25 percent on these nine-month nonrecourse loans. Therefore, for a farmer to redeem his loan at the end of the nine-month loan period, he must repay the $2.40 plus nine months' interest at 12.25 percent, which means a total redemption cost of $2.62 per bushel. The average price received by farmers for corn during January was $2.40 per bushel; therefore, unless a farmer needs the corn to feed livestock or to meet other sales commitments, he has very little economic incentive to redeem these corn loans. As a result, most of the 713 million bushels of corn under nine-month loans are likely to move into the farmer-owned reserve. If 75 percent of those bushels move into the reserve, which lends farmers $2.81 per bushel as opposed to the current market price of $2.40 per bushel, the farmer-owned reserve could reach 1,490 million bushels while corn loans outstanding would total $4.2 billion. Farmers are only required to pay the interest cost on farmer-owned reserve loans for the first year of the loan. Subsequently, the CCC continues to pay $0.265 per bushel storage cost and the interest for the second and third years of the loan. In 1983 and 1984, the storage cost per year would be $395 million and interest could cost $588 million per year, if the reserve was 1,490 million bushels.

Similar changes in outlook affect the other feed grains. For example, the August crop estimate did not project that sorghum would enter the farmer-owned grain reserve. As of February 3, 1982, farmers had placed 191 million bushels in the reserve and 59 million more bushels were pledged for nine-month nonrecourse loans. With the current estimated farmer-owned sorghum reserve at 225 million (see the following table) and a potential of 300 million bushels, the outlay estimates for the 1982 farmer-owned sorghum grain reserve range between $600 million and $800 million.

Supply and Demand Estimates for Sorghum

	August 1981	February 1982	Percent Change
Yield per Acre (bushels)	61.1	64.1	+5
Production (millions of bushels)	833	880	+6
Domestic use	461	411	-11
Exports	325	275	-15
Total Use	786	686	-13
Farmer-Owned Reserve Stock	0	225	
Total Ending Stock	91	303	+333
Estimated Average Farm Price (dollars per bushel)	2.70	2.30	-1

SOURCE: World Agricultural Supply and Demand Estimates Approved by the U.S. Department of Agriculture World Agricultural Outlook Board.

Although the wheat crop estimates have not been revised substantially between August and February, an increase of 11 percent in the farmer-owned wheat reserve affects estimated outlays. Farmers receive $3.50 per bushel for each bushel placed into the reserve plus an additional $0.265 per bushel for storage. As a result of an additional 50 million bushels being placed into the reserve, estimated outlays increase by $188 million.

Supply and Demand Estimates for Wheat

	August 1981	February 1982	Percent Change
Area Planted (millions of acres)	88.8	88.9	---
Area Harvested (millions of acres)	80.7	80.9	---
Yield per Acre (bushels)	34.1	34.5	+1
Production (millions of bushels)	2,750	2,793	+2
Domestic use	882	872	-1
Exports	1,825	1,850	+1
Total Use	2,707	2,722	+1
Farmer-Owned Reserve Stocks	475	525	+11
CCC Inventory Stock	185	185	---
Free Stock	376	352	-6
Total Ending Stock	1,036	1,062	+3
Estimated Average Farm Price (dollars per bushel)	3.75	3.70	-1

SOURCE: World Agricultural Supply and Demand Estimates Approved by the U.S. Department of Agriculture World Agricultural Outlook Board.

The most recent information relating to wheat outlays is the USDA plantings report released on December 22, 1981, on the 1982 winter wheat crop. According to that report, farmers seeded 66.255 million acres for winter wheat last fall to be harvested this spring. This is the largest acreage seeded to winter wheat since records were begun in 1909. Winter wheat production for fiscal year 1983, based on the condition of the crop as of January 1, 1982, is forecast at a record high of 2.13 billion bushels. This estimate was made before the Secretary of Agriculture announced a voluntary 15 percent acreage reduction program on January 29, 1982. This acreage reduction is required for eligibility for government price support loans, target price protection, and the farmer-owned grain reserve program. CBO estimates that only 35 percent of U.S. wheat producers will participate in the program because of the lateness of the final set-aside announcement and a historical unwillingness to plow up already-planted crops.

Deficiency Payments

Using the crop production estimates contained in the August crop report, the Department of Agriculture forecast no deficiency payments in fiscal year 1982. However, as a result of actual crop size and reestimated data, there have been and will be additional deficiency payments. The national weighted average market price for the first five months of the wheat marketing year was $3.66 per bushel, $0.15 below the target price of $3.81 per bushel; as a result, payments of approximately $400 million have been made to eligible wheat producers. The weighted average national market price for barley for the first five months of the marketing year was $2.49 per bushel, $0.11 cents below the target price, and total outlays to eligible barley producers are estimated to be $50 million dollars. As of February, it is projected that $200 million will be paid in deficiency payments to eligible sorghum producers, $22 million to eligible rice producers, and $530 million to eligible cotton producers. Therefore, a total of $1.2 billion will be paid in fiscal year 1982 in deficiency payments that were not expected based on the August crop report.

Dairy Program

CBO estimates of dairy supply, demand, and program costs, as shown in the following table, are based upon USDA reports of production, cow numbers, heifer replacements, the milk-feed price ratio, and commercial use. When the August estimates were developed, these reports supported the analysis that discontinuing the level of dairy support price increases that had prevailed in the past would lead to an adjustment in supply and demand that would result in reduced government purchases. By July 1981, the rate of increase in milk production had declined from March's increase of 4.4 percent over the previous year to 2.57 percent. The milk-feed price ratio had declined from 1.42 in March to 1.36 in June, below the profitability threshold of 1.4. Also, commercial disappearance had increased 6.2 percent over the previous year in the second quarter of 1981 and increased again during the month of July. For these reasons, CBO and the Administration projected that supply and demand would move into balance over the next five years, so that decreasing outlays would be needed for dairy price supports.

CBO Dairy Supply and Demand Estimates

	August 1981	February 1982	Percent Change
Production (billions of pounds)	131.2	135.82	+3.5
Commercial use	122.6	121.6	-8
Removals	8.7	14.3	+64.4
Support Price (dollars per cwt)	13.10	13.10	--
Net Support Outlays (millions of dollars)	987	1,907	+93.2

In February's analysis, CBO estimates indicate that the adjustment will not begin in 1982 even though the support price has not been increased since October 1, 1981. Through December 1981, milk production increases had climbed to 3.2 percent, and the milk-feed price ratio had risen to 1.58 because of low crop prices. Milk cow numbers had not decreased in their gains over the previous year since July. The July cattle inventory of dairy replacement heifers showed an annual increase of 5.9 percent and declining utility cow prices indicate a reluctance to cull the dairy herd. This leads to projections of continued increases in production in 1983 and beyond but at declining rates as feed grain prices rise with the expected return of normal weather and harvests. Commercial disappearance increased only 0.7 percent in the fourth quarter of 1981, more in line with per capita consumption trends. Commercial use is expected to continue to increase 1 to 2 percent in 1983 and after. As a result of February's analysis, net removals are projected to decrease from 14.3 billion pounds of milk equivalent in 1982 to 10.8 billion pounds in 1985. The decline in removals is partially offset by the increase in price supports, causing projected dairy expenditures to decline to $1,700 million in 1985.

CCC Outlays to Date

As of February 12, 1982, CCC has net outlays of almost $8.9 billion in fiscal year 1982, of which $3.3 billion is for nine-month loans that could be redeemed within the fiscal year. Dairy outlays were $260 million through December 1981, above the $175 million in December 1980. The peak dairy purchase months of March through August are yet to come.

The following table shows monthly and cumulative CCC outlays to date. The November crop report, which contained realistic assessments of 1981 crop production, coincided with the sudden increase in loan demand that resulted from the large harvest.

CCC Actual Monthly Net Outlays for Fiscal Year 1982 (In millions of dollars)

Month	Actual Outlays	Cumulative
October	789	789
November	1,748	2,537
December	2,803	5,340
January	3,175	8,515
February 12, 1982	390	8,882

In addition to the above actual monthly outlays, the CCC is committed to pay interest on borrowings from the Treasury of approximately $1.4 billion before the end of the 1982 fiscal year. During February, the CCC will also spend an additional $750 million in sorghum, rice, and cotton deficiency payments. At the end of February 1982, the CCC will have made or have been committed to make outlays of $11 billion, of which $7.7 billion are not likely to be redeemed or offset by sales.

Agricultural Credit. CBO reestimates of agricultural credit insurance outlays principally reflect differing estimates of disaster loans. Following a 1981 record of $5.1 billion, the Administration assumes program levels of $1.6 billion in 1982 and $1.5 billion in 1983. CBO calculates a five-year average, equal to $2,940 million, and increases that average by the estimated inflation rate from 1982 to 1987. The new constraints on eligibility, deductible losses, higher interest rates mandated in the Reconciliation Act of 1981 and the availability of federal crop insurance reduce this projected average to $2.15 billion in 1982 and $2.3 billion in 1983, increasing to $2.6 billion in 1985. Asset transactions with the Federal Financing Bank (FFB) mask the increased estimate of disaster lending. Higher outlays for disaster loans will be included in reestimated FFB activity.

Other Subfunction 352. For 1982, CBO's estimates of outlays from previous years' obligations differ from those of the Administration. Most of these differences are in accounts where expenditures are mainly for personnel and operating expenses that largely spend in the year they are obligated.

FUNCTION 370: COMMERCE AND HOUSING CREDIT

(Outlays in millions of dollars)

	1982	1983	1984	1985
President's February Budget	3,265	1,591	1,298	-516
Preliminary CBO Reestimates				
Different economic assumptions	---	---	---	---
Technical reestimates				
FSLIC	226	93	76	169
Postal Service	215	---	---	---
FDIC	---	---	---	450
SBA business loans	116	137	160	200
Payments to copyright owners	-62	---	---	---
CFTC user fees	---	-22	-22	-22
Other	10	---	---	---
Total Reestimates	505	208	214	797
President's Budget Reestimated	3,770	1,799	1,512	281

EXPLANATION OF PRELIMINARY CBO REESTIMATES

Different Economic Assumptions

This function has no reestimates resulting from different economic assumptions.

Technical Reestimates

FSLIC. The Federal Savings and Loan Insurance Corporation (FSLIC) fund provided more than $1.2 billion in 1980 and $0.9 billion in 1981 for assistance to member savings and loan (S&L) institutions. For the last two years, the net worth of many S&Ls has declined as short-term interest rates paid on deposits exceeded the earnings from long-term deposits, resulting in an estimated ratio of reserves to total industry savings deposits below 1.25 percent at the end of calendar year 1981.

Within the last two years, the FSLIC has been changing the type of assistance it provides to problem institutions. This has helped to slow down budget outlays even though the number of problem institutions has continued to grow. The current approach includes allowing interstate mergers, often packaging undesirable S&Ls with those in more favorable markets; revising accounting procedures to encourage the sale of mortgage loans and other assets; creating a new market instrument that improves the net worth of S&Ls while allowing the FSLIC to make only semiannual interest payments, rather than large, immediate cash outlays; and making contributions to institutions rather than acquiring assets.

Nonetheless, the outlay estimates provided by the Administration appear to be too low primarily because of relatively optimistic interest rate assumptions. The Administration is assuming that obligations will be more than $300 million lower in 1982 than in 1981, although the number of problem institutions and the size of their assets continue to increase. At the same time, fees from assessments are expected to decline from 1981 to 1982 by approximately $65 million. While it is not possible to estimate precisely, CBO assumes that a greater number of failures are likely to occur, and that the cash outlays needed to resolve these problems will exceed the Administration's estimates by $226 million in 1982, $93 million in 1983, $76 million in 1984, and $169 million in 1985. These estimates are consistent with the CBO baseline projections for fiscal years 1982 through 1985.

Postal Service. The 1982 payment to the Postal Service in the February budget incorrectly shows the President's September request of $619 million rather than $834 million, which is the amount provided in the continuing resolution for 1982. CBO understands that the Administration may request a rescission for the Postal Service in 1982, but none has been transmitted to date.

FDIC. While it is likely that continued assistance to mutual savings banks will be required from the Federal Deposit Insurance Corporation (FDIC), in general the banking industry is not suffering to the same degree as S&Ls from an earnings squeeze because of high interest rates. In addition, the FDIC has a portfolio approximately twice the size of the FSLIC ($12.7 billion versus $6.3 billion), which is expected to increase as earnings grow each year. Furthermore, by reducing rebates on insurance premiums, outlays can be more easily controlled. As with the FSLIC, the trend is to spread out payments for losses over time, thus minimizing federal outlays.

CBO has reestimated the Administration's 1985 net outlays upward by $450 million. While the Administration's outlay estimates for the FDIC vary from year to year in 1981-1984 by no more than about $50 million to $200 million, they jump by $800 million from 1984 to 1985 because of an anticipated payment on a note coming due in 1985. Based on an analysis of the bank concerned, it seems unlikely that the entire amount will be paid as currently scheduled, and some refinancing will be required.

SBA Business Loans. Outlay estimates for the business loan and investment fund of the Small Business Administration (SBA) have been revised upward by amounts ranging from $116 million in 1982 to $200 million in 1985, primarily because of different assumptions regarding repurchases of guaranteed loans and increased collections.

Each year since 1979, the Administration's estimates regarding disbursements for repurchases of guaranteed loans have been understated. SBA currently assumes that 18.6 percent of all loans guaranteed will default, whereas CBO assumes a default of 21.8 percent (with a net of 70 percent charged off), which is more consistent with historical trends.

In addition, the Administration's February budget estimates assume that an additional $35 million in 1982 and $110 million in 1983 (and each year thereafter) will be collected as a result of an improved debt collection program. The SBA will concentrate on improving liquidation efforts by retraining staff and legal counsel, updating information regarding data collection, and reassigning some existing personnel to this function. Nonetheless, given the state of the economy (and particularly of small businesses), CBO assumes that SBA receipts will be somewhat lower. It seems unlikely that the agency will be able to increase its collection efforts by over 35 percent without additional resources allocated specifically for this purpose.

Payments to Copyright Owners. Receipts from cable television stations and juke-box licenses are disbursed to copyright owners through this appropriation. The February budget estimates incorrectly assume that all collections to date will be disbursed in 1982. The distributions of 1978 and 1979 cable TV collections remain unresolved in the courts, and hearings on 1980 and 1981 distributions have not even begun and are likely to take more than a year to resolve. Consequently, CBO estimates that $18 million rather than $80 million will be spent for this purpose in 1982.

CFTC. While the Administration has proposed user fees to recover the cost of the regulatory activities of the Commodity Futures Trading Commission (CFTC), no estimate was included in its budget request. Consistent with the intent of the Administration, CBO has included these offsetting receipts as estimated in Major Themes and Additional Budget Details.

FUNCTION 400: TRANSPORTATION

(Outlays in millions of dollars)

	1982	1983	1984	1985
President's February Budget	21,228	19,628	18,752	19,418
Preliminary CBO Reestimates				
Different economic assumptions	---	---	---	---
Technical reestimates				
Rail programs	-1	-47	65	49
Urban mass transportation	23	-247	134	109
Other	84	---	---	---
Total Reestimates	105	-294	199	158
President's Budget Reestimated	21,333	19,335	18,951	19,576

EXPLANATION OF PRELIMINARY CBO REESTIMATES

Different Economic Assumptions

This function has no reestimates resulting from different economic assumptions.

Technical Reestimates

Rail Programs. Excepting Amtrak, the major rail programs involve heavy construction that requires several years from commitment of funds through design stages to project completion. The major estimating differences between CBO and the Administration are explained by differing assumptions about the time required between the appropriation of funds and project completion. The Administration is generally overly optimistic about construction schedules, assuming a shorter spend-out period. This has been the case most clearly in the Northeast Corridor project, for which OMB has overrestimated annual outlays by as much as 230 percent over the past few years. CBO's estimates have been consistently more accurate. By assuming slower obligation rates and construction schedules consistent with actual experience, CBO's 1982 and 1983 outlay estimates are below OMB's figures by a total of $62 million. These estimating differences are much less than in the past, as OMB has moved closer to CBO's assumptions.

For the rail rehabilitation program, CBO estimates that outlays will be $21 million higher than OMB in 1982 and $29 million lower in 1983. OMB has apparently used conflicting assumptions about how quickly various years' appropriations will be spent. While it uses an unusually slow spending rate for earlier appropriations, it assumes that most of the new 1982 funds will be spent within two years. The program's history indicates that four or more years is required for commitment of funds and completion of rail rehabilitation projects. CBO has applied this spending rate to both the balance of funds from previous years and to the 1982 appropriations.

Other notable estimating differences come in the Amtrak and the rail service assistance accounts. For Amtrak, CBO assumes a slightly slower delivery of capital equipment, based on an historical record of equipment delivery delays. The OMB projection of rail service assistance outlays does not, for an unknown reason, include approximately $40 million in funds that have been, or are expected to be, obligated by the end of 1983. This explains CBO's higher outlay estimate for 1984.

Urban Mass Transportation. The CBO reestimates of outlays for urban mass transportation grants result from the use of different assumptions about how quickly appropriated funds will spend. CBO expects that spending will not depart significantly from historical patterns in 1982 and 1983, but thereafter will change as a result of a shift in program mix and direction proposed by the Administration.

At the end of January 1982, the urban mass transportation fund had a total balance of approximately $870 million of unobligated funds and $7,791 million of obligated funds. The obligated funds were for capital construction projects and the purchase of rolling stock (light and heavy rail cars and buses). CBO expects these obligated funds to spend at historical rates that are slightly faster than assumed by the Administration. CBO assumes that spending of new funds starting in 1984 will be faster than recent experience. The Administration proposes to direct capital assistance grants to modernization and rehabilitation of existing systems and to provide increased funding for buses; these have quicker disbursements than the current program mix. In addition, out of the total program level, funds are set aside for the Washington, D.C., Metro system, an ongoing construction program. The older established systems have generally spent federal funding faster than the smaller systems or totally new systems. Another reason (though on a much smaller scale) that new funds will spend faster is that; in the research and development area, the Administration plans to direct efforts on short-term solutions to immediate problems rather than on long-term research.

Other. In fiscal year 1982, CBO estimates that outlays for other programs included in this function will be $84 million higher than the Administration estimate. The CBO estimate is higher primarily in two areas--federal-aid highways, where CBO is $41 million higher than the Administration, and Federal Aviation Administration operations, where CBO is $30 million higher. Both of the higher estimates are based on CBO's spending assumptions, which reflect recent historical outlay experience. In each case, the outlay difference is small (0.5 percent and 1.4 percent) compared with the program's total outlays.

FUNCTION 450: COMMUNITY AND REGIONAL DEVELOPMENT

(Outlays in millions of dollars)

	1982	1983	1984	1985
President's February Budget	8,366	7,263	6,663	6,856
Preliminary CBO Reestimates				
Different economic assumptions	---	---	---	---
Technical reestimates				
Disaster relief	44	42	78	76
Flood insurance	25	29	76	100
Disaster loans	50	201	317	428
Other	-18	-5	10	1
Total Reestimates	101	277	481	605
President's Budget Reestimated	8,467	7,540	7,144	7,461

EXPLANATION OF PRELIMINARY CBO REESTIMATES

Different Economic Assumptions

This function has no reestimates resulting from different economic assumptions.

Technical Reestimates

The Administration has requested or projected the need for approximately $1.2 billion in 1983, 1984, and 1985 for the federal flood insurance, disaster loan, and disaster relief grant programs. This is approximately $1.1 billion below the CBO baseline projection for these programs over the period. In general, the Administration has assumed optimistic levels for these programs below the average experience in recent years, has not taken into account the impact of inflation on program resources, and has made optimistic assumptions about the annual performance of each program. Although the Administration has the authority to raise insurance premiums, to refuse to declare disasters, and to seek loan repayments aggressively, CBO does not expect the net impact of these changes to be as large as projected by the Administration.

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Disaster Relief. The Administration's budget estimate for the disaster relief program administered by the Federal Emergency Management Agency assumes that the program will accrue and retain large obligated balances in 1982 and 1983. In addition, the Administration projects extremely optimistic program levels for 1984 and 1985. The CBO estimate reflects the assumption that obligated balances will be withdrawn faster than assumed by the Administration and that inadequate program funding in 1984 and beyond will result in a faster than normal drawdown of new obligations by state recipients of program funds.

Flood Insurance. The Administration's estimate for this program includes estimates for losses and adjustments that are optimistic compared with the history of the program. Although the Administration has taken several measures to reduce the cost of the program, CBO assumes that average annual losses and total insurance in force will grow faster than premiums can be adjusted for the forseeable future.

Disaster Loans. The Administration's estimates for the Small Business Administration's disaster loan program assume a sharp reduction in the demand for disaster loans, which will result in significant net receipts over the 1982-1985 period. The CBO estimate assumes the Administration's requested loan limitation in 1983, but notes that the proposed lending level of $440 million could be $100 to $300 million below demand depending upon the incidence of disasters and the public's response to 1981 program changes. In 1982 to 1985, CBO has assumed that demand for loans will result in the obligation and outlay of all available resources of the fund.

FUNCTION 500: EDUCATION, TRAINING, EMPLOYMENT, AND SOCIAL SERVICES

(Outlays in millions of dollars)

	1982	1983	1984	1985
President's February Budget	27,770	21,552	19,266	17,791
Preliminary CBO Reestimates				
Different economic assumptions				
Guaranteed student loans	29	301	602	440
Technical reestimates				
Elementary and secondary education	-320	121	64	---
Student financial assistance	9	-124	59	---
Guaranteed student loans	139	503	552	225
Employment service	211	283	---	---
Total Reestimates	68	1,084	1,277	665
President's Budget Reestimated	27,839	22,636	20,543	18,456

EXPLANATION OF PRELIMINARY CBO REESTIMATES

Different Economic Assumptions

The economic factor affecting outlays for the Guaranteed Student Loan (GSL) program is the short-term interest rate. The table below shows the assumptions of the Administration and CBO for the 91-day Treasury bill rates by fiscal year. A one-percentage-point increase in the average Treasury bill rate would add over $200 million to program obligations in 1982 and almost $300 million in 1985. Since outlays lag behind obligations, the resulting outlay increases are spread over two years.

91-Day Treasury Bills (In percent, fiscal year average)

	1982	1983	1984	1985
Administration	11.6	11.1	9.6	8.9
CBO	11.8	13.0	12.2	9.9

Technical Reestimates

Elementary and Secondary Education. The February budget estimates 1982 outlays for the education for the handicapped programs at a higher level than actual spending to date would indicate. CBO has reestimated outlays for this program in 1982 downward by $174 million. In addition, the February budget uses a spending rate in 1982 for the vocational and adult education programs similar to the new spending rate associated with the 1983 block grant proposal. Since 1982 funds are not consolidated, CBO has assumed the historical spending rates will still apply. This results in $146 million lower outlays in 1982, $121 million higher outlays in 1983, and $64 million higher outlays in 1984.

Student Financial Assistance. The Administration has used a higher spending rate for the aggregate of all student assistance programs in 1983, including Pell grants, than recent experience would indicate. CBO has adjusted outlays for the student assistance programs to incorporate historical spending patterns.

Guaranteed Student Loans. CBO's estimate of outlays for the President's request for the GSL program exceeds the Administration's estimates each year in the 1982-1985 period. In 1982, CBO's estimate is $139 million higher than the Administration's. About $60 million of this difference relates to assumptions about when the President's legislative proposals will be implemented. Administration estimates assume implementation of all loan proposals in April 1982. Consistent with the 1981 experience, CBO has assumed that the President's proposals will be enacted in July 1982. This enactment schedule would permit the increase in the origination fee to be implemented in the final quarter of fiscal year 1982. All other programmatic changes would become effective in October 1982. The remainder of the outlay difference in 1982, approximately $70 million, relates to the relationship between obligations and outlays in the final quarter of the fiscal year. Historically, obligations in the final quarter of the year outlay in the next fiscal year. This implies that program savings in the last quarter of the year will not produce outlay savings until the next year. CBO's estimates assume a continuation of this historical relationship. The Administration's estimates do not reflect fully the lag between program obligations and outlays.

In 1983, CBO shows outlays for the President's request approximately $500 million above Administration estimates. Approximately $200 million of this difference is explained by the assumed delay in the implementation of the President's legislative proposals, as discussed above. An additional $100 million of the difference relates to assumed differences in loan volume. CBO generally expects lower loan volume than the Administration. Lower volumes result in smaller savings as a result of increasing the origination fee and the insurance premiums. Finally, approximately $200 million of the difference relates to estimates of the distribution of the loan volume. The federal government pays interest subsidies on the guaranteed loans while students are in school and during a short grace period after graduation. Thereafter, the student is responsible for interest payments and the costs to the government fall; a smaller government subsidy continues until the loan is repaid. CBO anticipates a higher proportion of total loan volume in the in-school status than does the Administration. CBO uses a cohort analysis to track the amount of loan volume receiving the higher subsidies. The Administration apparently uses a more aggregative technique.

CBO also estimates a larger proportion of total volume in the in-school status in the outyears than does the Administration. This appears to be a significant factor in explaining the higher CBO estimates in 1984 and 1985.

Employment Service. The February budget does not include a 1982 supplemental appropriation of $211 million for the Employment Service requested by the Administration, nor a recently submitted amendment requesting an additional $283 million for the Employment Service in 1983. The CBO technical reestimates correct the February budget estimates for these changes.

FUNCTION 550: HEALTH

(Outlays in millions of dollars)

	1982	1983	1984	1985
President's February Budget	73,437	78,105	84,917	93,539
Preliminary CBO Reestimates				
Different economic assumptions				
Hospital insurance	---	34	400	828
Medicaid	---	78	420	923
Technical reestimates				
Hospital insurance	---	230	551	225
Supplementary medical insurance	---	137	405	812
Medicaid	-193	20	-182	-647
Total Reestimates	-193	499	1,594	2,141
Unevaluated Administration Estimates	(---)	(362)	(2,355)	(4,560)
President's Budget Reestimated	73,245	78,604	86,511	95,680

EXPLANATION OF PRELIMINARY CBO REESTIMATES

Different Economic Assumptions

Hospital Insurance. The hospital insurance program's costs reflect hospitals' costs of providing care. As hospitals pay more for food, fuel, equipment, and other supplies, the cost of the hospital insurance program rises. For each 1 percent increase in the price of these nonlabor inputs, which constitute about 35 percent of hospitals' costs, program spending grows roughly $100 million annually. Since the CBO economic assumptions include higher rates of inflation than the assumptions underlying the President's budget estimates, the CBO estimates of outlays for hospital insurance are higher than the Administration's in 1983-1985.

Medicaid. The costs of the Medicaid program are sensitive to both the rate of inflation and the unemployment rate. As prices rise, the cost of medical services increases, including the cost of physician services, hospitalization, and nursing home care. As the unemployment rate rises, more people become eligible for Medicaid assistance, thereby increasing the costs of the program.

In 1983, the economic differences are small because the Administration's and CBO's economic assumptions regarding the CPI and unemployment are similar. In 1984 and 1985, however, CBO has projected higher increases in prices than the Administration. In addition, the small difference between CBO's and the Administration's assumed unemployment rate widens in 1985, thus increasing the estimated economic differences even further. The higher inflation rates projected by CBO account for over 80 percent of the reestimates due to differences in economic assumptions.

Technical Reestimates

Hospital Insurance. The CBO technical reestimate for the hospital insurance component of Medicare results from different projections of hospital utilization rates, costs per day of hospitalization, and administrative costs for contractors who process claims for reimbursement under the program. The first two factors account for the bulk of the CBO reestimates.

The CBO baseline projections for hospital insurance embody higher rates of hospitalization for enrollees than assumed by the Administration for its February budget estimates, as shown in the table below. CBO's projections assume that hospital utilization will increase at the average annual rate experienced from 1973 to 1978, a rate well below the unexpectedly large increases of the last two years.

Annual Hospital Days per Aged Enrollee

	Actual	Projections			
	1981	1982	1983	1984	1985
Administration	4.187	4.163	4.190	4.194	4.216
CBO	4.187	4.223	4.258	4.295	4.331

In addition, the CBO technical reestimates reflect a different pattern of increases in the cost of a day of hospital care. As displayed below, CBO projects diminishing increases in daily hospital costs, partly because of the declining inflation rate forecast by the Administration. The Administration's projected increases fall initially, but turn up again in 1985. This reversal, coupled with CBO's continued higher utilization rate, largely explains the drop in CBO's technical reestimate from 1984 to 1985.

Change in Hospital Cost per Day under the Administration's Economic Assumptions (Percent change)

	Average Annual Increase 1977-1981	Projections			
		1982	1983	1984	1985
Administration	13.2	14.3	12.9	11.8	12.4
CBO	13.2	14.6	13.1	11.6	11.3

CBO's technical reestimates also assume continued increases in the costs of administering this program. The President's budget, on the other hand, assumes a slight decline. In spite of productivity gains, administrative costs have risen over 17 percent annually since 1977, as shown in the table below. Because CBO has not yet been able to evaluate the budgetary impact of the reductions in the federal work force assumed in the President's budget, CBO's projections assume increases only in the budget for Medicare's contractors. The estimates reflect continued increases in the contractor budget at the 8.3 percent average annual rate experienced since 1977.

Medicare Administrative Costs (In millions of dollars)

	1977	1978	1979	1980	1981	Average Annual Increase (percent)
Hospital Insurance	301	451	452	494	566	17.1
Supplementary Medical Insurance	475	504	555	593	668	8.9
Contractor Costs	(505)	(536)	(576)	(642)	(694)	8.3

Both the Administration and CBO underestimated spending in the hospital insurance program in 1981. Generally, however, CBO's estimates were closer to the mark. For example, CBO's January 1981 estimate of 1981 outlays was more than $400 million higher than the Administration's figure, but almost $1.2 billion below actual spending for the year. As recently as the September budget, the Administration underestimated outlays by $600 million, while CBO's comparable estimate fell short by $200 million.

Supplementary Medical Insurance. The CBO technical reestimates for the second component of Medicare, supplementary medical insurance, result from different projections of the use of physicians' services by the eligible population and of administrative costs. Administration and CBO assumptions about physicians' fees are similar.

The Administration's February budget estimates assume slower growth in the use of physicians' services than assumed by CBO in its baseline projections. As shown in the table below, CBO assumes a relatively slow decline in the use of these services from the high rate currently observed to a rate consistent with earlier program experience.

Projected Increases in Use of Physicians' Services (Percent change)

	Estimated Average Annual Increase 1977-1981	Projections			
		1982	1983	1984	1985
Administration a/	5.2	8.2	5.4	4.6	4.4
CBO	5.2	8.2	6.5	6.0	5.2

a/ The figures shown as the Administration's projections are weighted averages of separate projections for aged and for disabled enrollees provided by the Administration.

CBO's technical reestimates also assume that the cost of administering this program will continue to rise through 1985. The President's budget, on the contrary, assumes a slight decline. As shown in an earlier table, however, administrative costs rose 8.9 percent annually from 1977 to 1981 despite substantial productivity gains during that period. CBO's estimates of administrative costs assume continued increases in the contractor budget at the 8.3 percent average annual rate experienced since 1977.

Medicaid. The CBO technical reestimates for Medicaid flow from CBO's smaller projected growth rate of Medicaid expenditures in 1982, different levels of projected savings resulting from the 1981 reconciliation act, and lower projected savings for the Administration's proposed legislation included in the February budget.

CBO Technical Reestimates for Medicaid (In millions of dollars)

	1982	1983	1984	1985
Existing Law	-159	58	-461	-1,011
Proposed Legislation	-34	-38	279	364
Total	-193	20	-182	-647

CBO projects a smaller growth rate for the Medicaid program in 1982 than the Administration. This smaller rate is consistent with the current fiscal year's spending pattern. The Treasury statements for the first quarter of fiscal year 1982 show only $4,113 million in outlays for the Medicaid program, indicating that increases in Medicaid spending are slowing down. This represents a growth rate of one percentage point less than the previous year's growth rate for the first quarter of the fiscal year. In addition, discussions with state officials indicate that they are making efforts to restrain Medicaid spending because of current fiscal conditions. California is attempting to contain costs through changes in eligibility, benefits, and rates. New York has already made several program changes this year in an effort to hold down costs.

CBO also estimates different levels of projected savings for program changes made in the 1981 reconciliation act. One of the provisions of this act established a reduction in federal Medicaid payments to each state. However, a state is entitled to receive a supplemental adjustment to this reduction if total federal Medicaid funding of the state's program in a year falls below a specified target level. The supplemental adjustment for the 1982 reduction will be awarded in 1983, so that awards will lag one year behind the reduction. CBO's projected lower growth rate in 1982 results in more states falling below the specified target level. Thus, CBO's estimate of the supplemental adjustment payments to be awarded in 1983 is higher than the Administration's estimate.

Once a state exceeds the target level, however, it would be very difficult not to continue to exceed the target in subsequent years, because target rates are cumulative from year to year. A state would have to decrease spending in subsequent years to compensate for previous years' growth. This would be quite difficult and therefore the supplemental adjustment payments should decrease over time as fewer states will be able to qualify for these payments. The Administration shows an increase in these payments over time.

In addition, the Administration shows no savings as a result of the flexibilities given to the states in the 1981 reconciliation act. The flexibilities were established to provide states with greater latitude in operating their programs. For example, the flexibilities allow states to determine hospital reimbursement rates and to purchase laboratory services competitively for their Medicaid recipients. The states must submit waiver requests for many of the flexibilities. At present, 42 states have submitted waiver requests relating to specific provisions of the 1981 reconciliation act. Furthermore, discussions with state officials indicate that efforts are being made to achieve savings in this area, and in 1983 and beyond such savings should be realized.

CBO estimates lower savings for the proposed legislation in the budget than the Administration. A small portion of this reestimate in the Medicaid program is the result of CBO's reestimate of the savings in the Aid to Families with Dependent Children (AFDC) program. CBO shows no estimated savings from the Administration's legislative proposals in the AFDC program in 1982 and slightly reduced savings in 1983. Therefore, the estimated impact of these AFDC proposals on the Medicaid program is eliminated in 1982 and adjusted in 1983.

CBO also reestimated the impact of proposed legislation on the level of supplemental adjustment payments. The proposed legislation will substantially slow program growth to a point at which more states are estimated to qualify for these payments. This would increase projected program costs in 1983 and 1984 by $279 million and $364 million.

Finally, CBO has made no further reestimates of the Administration's legislation proposals or regulatory changes in the Medicaid program, because there is no legislative or regulatory language available at this time. As such language becomes available, CBO will examine the proposals more closely.

UNEVALUATED ADMINISTRATION SAVINGS

The President's budget includes substantial savings in Medicare from both administrative and legislative proposals that are undeveloped at this time. Because the details of the proposals are not available, CBO has been unable to evaluate the savings from them assumed in the budget.

President's Budget Savings in Medicare from Undeveloped Proposals (In millions of dollars)

	1982	1983	1984	1985
Reform Health Care Financing (Future Legislation)	---	---	-1,950	-4,100
Improve Contractor Utilization Review Activities (Administrative Savings)	---	-362	-405	-460
Total	---	-362	-2,355	-4,560

The health care financing reforms to be proposed are intended to strengthen market forces in health care. The Administration's March 1981 budget included savings from similar future legislation known as the competition proposal. Savings included from that proposal were $0.5 billion in 1983, $1.6 billion in 1984, and $3.7 billion in 1985. Thus, in the current budget, savings have grown by $0.4 billion in both 1984 and 1985, although implementation of the proposal has been delayed. Moreover, the savings in the current budget are in addition to savings of $850 million in 1984 and $950 million in 1985 from a proposed 2 percent reduction in reimbursements to hospitals, itself billed as an interim measure until the financing reforms are enacted. Together these assumed savings represent reductions of 4.3 percent and 6.7 percent from projected Medicare spending under existing law in 1984 and 1985, respectively. To achieve savings of such magnitude as early as assumed in the budget, the strengthening of market forces would have to include some combination of large benefit reductions and shifts of costs to beneficiaries or providers.

The Administration attributes the savings from the utilization reduction initiative to two activities: intensified efforts by Medicare's contractors to reduce waste in the provision and use of health services (that is, stepped-up medical and reasonable charge review), and what the Administration describes as "a similar effort in the private sector recently announced by a coalition of health providers, health insurers, business, and labor." CBO has not been able to obtain from the Administration details about either activity nor any substantiation of the estimated savings included in the President's budget. Based on discussions to date, however, it would appear that the estimated savings from this proposed initiative are optimistic.

FUNCTION 600: INCOME SECURITY

(Outlays in millions of dollars)

	1982	1983	1984	1985
President's February Budget	250,870	261,736	274,808	290,122
Preliminary CBO Reestimates				
Different economic assumptions				
Social Security and SSI	---	---	1,237	5,920
Unemployment compensation	---	736	1,498	3,445
Food stamps and AFDC	---	105	293	1,054
Technical reestimates				
Social Security (OASDI)	954	920	1,178	-210
Civil Service Retirement	225	332	448	612
Unemployment compensation	-239	-27	311	463
Food stamps	245	298	-255	-395
Child nutrition	245	130	115	---
Supplemental Security Income	-122	-180	-134	-165
Assistance payments (AFDC)	---	243	179	328
Energy assistance	123	---	---	---
Total Reestimates	1,430	2,557	4,870	11,052
President's Budget Reestimated	252,300	264,293	279,678	301,174

EXPLANATION OF PRELIMINARY CBO REESTIMATES

Different Economic Assumptions

Outlays in income security programs are sensitive to changes in economic conditions, most notably increases in prices and changes in unemployment levels. Both CBO and the Administration show improving economic conditions over the forecast period. However, the economic recovery reflected in CBO's economic assumptions is not as rapid as that in the Administration's assumptions. CBO assumes higher cost-of-living adjustments (COLAs) in indexed programs beginning in 1984 and higher rates of unemployment beginning in 1983.

Social Security and SSI. Social Security and Supplemental Security Income (SSI) benefits are automatically adjusted each year for increases in the cost of living as measured by the Consumer Price Index. The 1982 and

1983 COLAs assumed by CBO for these programs are the same as those of the Administration. CBO's assumed COLAs exceed the Administration's by 2.4 percentage points in 1984 and by 1.7 percentage points in 1985, resulting in the upward reestimate of outlays.

The Old Age and Survivors Insurance (OASI) program accounts for most of the reestimate, as shown in the table below. The Disability Insurance (DI) and Supplemental Security Income programs also contribute to the reestimate.

Effects on OASDI and SSI of Different COLAs (Outlays in millions of dollars)

	1982	1983	1984	1985
Old Age and Survivors Insurance	---	---	1,050	5,056
Disability Insurance	---	---	146	641
Supplemental Security Income	---	---	41	223

Although the program is currently indexed to the CPI, no economic reestimate is shown for Civil Service Retirement because the President's budget proposes to limit future COLAs to the lesser of the change in the CPI or the general schedule pay increase for federal employees. Under CBO's baseline economic assumptions, the projected COLAs will exceed the federal pay raise in each year.

Unemployment Compensation. CBO's projection of the rate of unemployment exceeds the Administration's by 0.2 percentage points in fiscal years 1983 and 1984 and by 0.6 percentage points in fiscal year 1985. Unemployment compensation is very sensitive to differences in assumed unemployment rates. By 1985, CBO's estimate of unemployment compensation is above the Administration's by $3,445 million. A small part of this difference is explained by CBO's higher assumed rates of inflation.

Food Stamps and Aid to Families with Dependent Children (AFDC). The food stamp and AFDC programs are sensitive to changes in both unemployment rates and rates of inflation. When unemployment rates rise, participation increases in both programs, especially in food stamps. When rates of inflation rise, average payments per recipient rise: in food stamps because allotments are automatically indexed to the Department of Agriculture Thrifty Food Plan and in AFDC because some states are mandated or choose to increase payments as prices rise.

Because of the differences in economic assumptions, CBO's estimates of food stamp outlays are $50 million higher than the Administration's in fiscal year 1983 and $719 million higher in 1985, as shown in the table below. CBO's higher assumed unemployment rate explains all of the reestimate in 1983 and 40 percent of the reestimate in 1985. Higher prices explain the remaining 60 percent in 1985. In AFDC, CBO's estimated outlays are $55 million higher than the Administration's in 1983 and $335 million higher in 1985. Higher prices explain about 60 percent of the difference in 1983 and 70 percent in 1985.

Effects on Food Stamps and AFDC of Different Economic Assumptions (Outlays in millions of dollars)

	1982	1983	1984	1985
Food Stamps	---	50	134	719
AFDC	---	55	159	335
Total Economic Reestimate	---	105	293	1,054

Technical Reestimates

Social Security. The Old Age and Survivors Insurance (OASI) and Disability Insurance (DI) programs are very large, with combined outlays in 1981 totaling $139.6 billion. Consequently, even a minor difference in technical reestimates can cause a large difference in outlays in absolute terms. Many of the technical reestimates in Social Security discussed below are minor.

The CBO technical reestimate of OASI shows slightly higher outlays throughout the 1982-1985 period, as presented in the table below. This reestimate is only 0.6 percent of total OASI outlays. The DI technical reestimate is proportionately somewhat larger, but it is still less than 2 percent of program outlays. Sources of the technical reestimates of OASI and DI are discussed, in turn, below.

CBO Technical Reestimate of OASI and DI (Outlays in millions of dollars)

	1982	1983	1984	1985
Old Age and Survivors Insurance	858	440	799	275
Disability Insurance	96	482	379	-485
Total Technical Reestimate	954	922	1,178	-210

In OASI, CBO's technical reestimate of the President's budget reflects primarily a slightly higher estimate of the number of beneficiaries. CBO is projecting approximately 100,000 to 125,000 more retired workers on average over the course of fiscal year 1982 than is the Administration. This difference represents less than 0.5 percent of all retired workers. In 1983 and 1984, CBO's estimated number of recipients averages about 150,000 more than the Administration's estimate. By 1985, these differences have narrowed with the sustained improvement in the economy.

CBO's method of forecasting recipients differs from the Administration's in several technical respects. Most importantly, it takes into account the effect of the economy on retirement decisions. Some individuals may find retirement an acceptable alternative to worsening labor market conditions, resulting in a greater number of retirements than if labor market conditions were better.

A rise in outlays above what the Administration is estimating for 1982 is substantiated by recent data on benefit payments. Benefit payments typically rise from month to month over the course of the fiscal year. For example, the monthly increase averaged $40 million in 1981, based on Treasury data. Recent Social Security Administration (SSA) data show monthly increases of $40-60 million for the first five months of 1982. Yet the Administration's 1982 estimates indicate little, if any, monthly rise in benefit payments during the remainder of 1982. In contrast, CBO's estimates assume a $20 million average monthly increase over the remainder of the year. (The $20 million monthly increase is low by historical standards because of the effects of the 1981 reconciliation act.)

In DI, a technical reestimate has brought the Administration's numbers in line with CBO's published baseline budget projections. It is difficult to identify all of the technical factors contributing to the difference in outlays between CBO and the Administration. Several important factors can be identified: differences in savings from management initiatives and differences in numbers of beneficiaries.

In its 1982 budget, the Administration proposed to tighten the management of the DI program by searching for and terminating all disability beneficiaries who do not meet the program's current disability criteria. These continuing disability investigations are being maintained as a management initiative in the 1983 budget. They are to be in addition to those mandated in the 1980 Disability Amendments, as well as those planned under current law. Sorting out these effects is difficult, but CBO estimates that this proposal can save $110 million in fiscal year 1982 and $833 million in 1985 in benefit payments from the DI trust fund, as compared with the Administration's estimated savings of $370 million in 1982 and $1,210 million in 1985. Thus, CBO's estimates of savings are lower by about $250 million to $375 million, respectively.

CBO is assuming a much lower number of terminations than the Administration as the result of the continuing disability investigations. Based on an error rate of 15 percent (determined by the General Accounting Office) and recent reversal rates in denied cases, CBO estimates that ultimately 115,000 additional beneficiaries will be terminated and kept off the rolls to obtain these savings. The Administration assumes that the number terminated will be approximately twice this level.

As to the number of beneficiaries, CBO's projections show somewhat higher numbers in fiscal years 1982-1984 and a lower number in 1985. Projections of beneficiaries are subject to considerable uncertainty. In the last year, the number of DI beneficiaries has declined sharply for reasons that are not clear. However, 1982 data from the Monthly Treasury Statements for the fiscal year to date show a flow of cash benefit payments that appears to be consistent with the CBO reestimate.

CBO's methodology assumes that, as labor market conditions deteriorate, many disabled workers will find DI benefits an attractive alternative to diminishing labor market prospects. Although the impact of labor market conditions acts to increase the estimated number of beneficiaries relative to the Administration's estimates, this increase is partially offset by effects of the 1977 and 1980 Social Security legislation, the 1981 reconciliation act, and other administrative actions. These effects are not available on a disaggregated basis from SSA.

By 1985, however, CBO's projected number of beneficiaries is below the Administration's. This reflects, in part, shifts in demographics: the number of people in the age groups most likely to become disabled is projected to decline over the next few years. The number of people aged 50 to 64 is projected to decline after 1982, while the rate of increase of those aged 60 to 64 is projected to slow dramatically beginning in 1984.

Civil Service Retirement. CBO projects Civil Service Retirement outlays above the President's budget throughout the 1982-1985 period. The higher outlays reflect higher refunds paid to separated government employees and higher annuity payments, as shown in the table below.

Components of CBO's Technical Reestimate for Civil Service Retirement (Outlays in millions of dollars)

	1982	1983	1984	1985
Refunds	130	104	158	217
Annuities	95	228	290	395
Total Technical Reestimate	225	332	448	612

Refunds paid to separated government employees have averaged $74 million per month so far in fiscal year 1982. The Administration's annual estimate averages $41 million each month. CBO's incorporation of later data on refund payments results in $130 million of the higher 1982 outlays in Civil Service Retirement.

In 1983 to 1985, about one-third of CBO's higher outlays reflects higher projected refund payments. CBO's projection of refunds reflects the historical growth in these payments. As illustrated in the table below, the President's budget shows no growth in projected refund payments in these years. In fact, the Administration's estimate of $428 million a year in refunds for 1983 to 1985 represents a slight decrease from actual 1981 payments. With the Administration's proposal to reduce federal employment, refunds to separated government employees are not likely to decline from 1981 to 1983.

In addition to higher refund payments, CBO also projects higher outlays for annuities in all years. CBO's projections are based on outlays through the first quarter of fiscal year 1982, cash disbursements for annuity payments, and the Administration's most recent actuarial estimates for the growth in the program. Relying upon the Administration's most recent growth assumptions for annuities and actual benefits to date, CBO's annuitant outlays exceed the President's budget by $95 million in 1982 and by $395 million in 1985.

Refunds to Separated Government Employees from the Civil Service Retirement Fund (In millions of dollars)

	Average Annual Percentage Growth, 1977-1981	1982	1983	1984	1985
Administration	12.7	493	428	428	428
CBO	12.7	623 a/	532	586	645

a/ CBO's 1982 estimate incorporates actual refunds to date.

Unemployment Compensation. The technical reestimate of unemployment trust fund outlays can be analyzed in terms of differences in the projected number of weeks of unemployment compensation being paid and in the expected increase in the average weekly benefit amount. The table below compares the Administration's and CBO's estimates of weeks of unemployment compensated and of average weekly benefits. Both sets of estimates are based upon the Administration's economic assumptions.

Unemployment Compensation: Weeks Compensated and Average Benefits

	1982	1983	1984	1985
Weeks Compensated (in millions)				
Administration	211.62	181.74	151.32	132.47
CBO	202.87	175.99	148.34	129.14
Average Weekly Benefits (in dollars)				
Administration	107.36	113.48	118.79	122.92
CBO	110.64	116.86	123.32	129.69

NOTE: Based on the Administration's economic assumptions.

Because of the flow of unemployment insurance claimants into and out of employment, it is more useful to speak of weeks of compensated unemployment rather than numbers of beneficiaries. For reasons that are not completely understood, the insured unemployment rate has been diverging from the total unemployment rate for the past year. The insured unemployment rate is the number of persons currently claiming state unemployment compensation benefits divided by the level of covered employment in a recent historical period. This phenomenon has resulted in fewer persons actually drawing weeks of compensation than would be expected from past experience during periods of high unemployment. Because of this, CBO projects fewer weeks of compensation being paid than does the Administration even at the same unemployment rate.

On the other hand, the Administration's estimates assume a rate of increase in average weekly benefits below recent experience, even after taking into account the lower wage and price increases it expects. The fiscal year 1982 average benefit amount projected by the Administration is at approximately the same level as the actual average for the first quarter. In recent years, the first quarter's average benefit has been lower than that for the following three quarters by about $5.00.

The first of these two conflicting differences is stronger in 1982 and 1983 and results in technical reestimates that lower the level of outlays. The second is more influential in 1984 and 1985; as a consequence, it reinforces the economic differences and increases outlays.

The Administration is proposing legislation that would further dramatically diminish the size of two auxilliary unemployment compensation programs: trade adjustment assistance (TAA) and unemployment compensation for ex-service members (UCX). All TAA beneficiaries who are not enrolled in approved training as of July 1, 1982, would be eliminated from cash benefit assistance. As a result, the income transfer component of this program would be eliminated by 1984. CBO estimates $16 million more will be spent in 1982, primarily based upon the pattern of expenditures thus far in the fiscal year. The UCX legislation would eliminate from program eligibility those future potential beneficiaries who are barred from reenlistment rights. Based upon Defense Department enlisted personnel separation data, CBO believes that the number of claimants the Administration is projecting is too low in 1982 and 1983. Thus, CBO estimates the Administration's UCX outlays upward by $20 million and $17 million in these years.

Food Stamps. Technical reestimates of food stamp outlays result from differences between CBO and the Administration in estimates of the current policy baseline and in estimated effects of proposed legislation on program cost. The following table shows these components of the technical reestimate.

Components of CBO's Technical Reestimate of the Food Stamp Program (Outlays in millions of dollars)

	1982	1983	1984	1985
Current Policy Baseline	0	-162	-130	-267
Proposed Legislation	245	460	-125	-128
Total Technical Reestimate	245	298	-255	-395

The downward technical reestimate of the current policy baseline in 1983 through 1985 results primarily from differences in projection methods. The Administration's forecast includes less of a decrease in program participation in response to economic recovery than does the CBO forecast. By 1985, the Administration's current policy projection of participation exceeds CBO's by 5 percent, or nearly one million people. The Administration includes a factor in its projection method that acts like a time trend and contributes to increases in participation levels through time. This is one of several reasons that the Administration's current policy baseline exceeds CBO's estimate. Sufficient detail on the Administration's forecasting techniques is not available to make a complete analysis of the differences.

A reestimate of savings from proposed legislation explains much of the difference between the CBO and the Administration estimates. The entire 1982 technical reestimate of $245 million reflects a reestimate of proposed legislative savings. The Administration has assumed that four of the major proposals requiring legislation would be effective on July 1, 1982. It has not made clear how much time will be needed to issue regulations, to allow states to prepare to make the changes, and to implement the changes. For these four proposals, implementation requires the review of over 7 million case files. Previous experience indicates that a period of at least four to five months is required following enactment of legislation to allow for full implementation. Enactment of the Administration's latest legislative proposals is not likely to occur in time to realize savings during fiscal year 1982.

CBO also does not include full savings during the first months of fiscal year 1983 to allow time for full implementation of the proposed changes. This accounts for $70 million of the $460 million technical reestimate of proposed legislation. The remainder is a \$390 million reestimate of savings in the Administration's legislative proposals, for two reasons. The first is that the Administration has not subtracted the costs of the food stamp program in territories other than Puerto Rico in its budget estimates. The proposal to replace the food stamp program and other nutrition programs in these areas with a block grant starting in 1983 would reduce food stamp outlays by about \$45 million. The second involves the Administration's proposal on "erroneous payments." In this proposal, the federal government will no longer have responsibility for erroneous benefits in excess of 3 percent in fiscal year 1983, 2 percent in 1984, and 1 percent in 1985. CBO's estimate of the effects of this proposal differs from the Administration's with respect to when the savings would be realized. The Administration has assumed that error rates will be at the target levels in each year. If this were to occur, savings would be realized during the current year rather than during the year following when actual error rates are known and states are assessed for erroneous benefits in excess of the target levels. CBO feels that dramatic improvements in rates of error due to overpayment or ineligible participation such as assumed by the Administration are not possible and that much of the outlay savings, especially in the first few years following enactment, will result from state assessments rather than actual reductions in errors. This difference in assumed timing of savings accounts for all but a small portion of the remaining 1983 technical reestimate.

The 1984 and 1985 differences due to reestimates of proposed legislation of -\$125 million and -\$128 million result, in part, from including projected current policy outlays from the food stamp program in the territories in the estimate of savings due to proposed legislation. Also, the redistribution of erroneous payments from earlier years adds to 1984 and 1985 savings.

Child Nutrition. The technical reestimate of \$245 million in fiscal year 1982 results from differences in projected numbers and types of meals served in the school breakfast and national school lunch programs and differences in assumed spending patterns from current year budget authority.

In the school breakfast program, CBO has projected 600 million meals during fiscal year 1982, a decline from the 1981 level of 652 million, while the Administration forecasts an increase to 675 million meals. Early participation data from this school year indicate nearly a 10 percent decline in program participation from the same period last year. CBO believes that this drop in breakfasts served will be maintained throughout the year. This difference accounts for a downward reestimate of the President's budget of \$35 million.

In the school lunch program, CBO and the Administration project similar numbers of total lunches but a different mix of meals among reimbursement categories. The Administration assumes that about 39 percent of lunches will be served to needy children in the highest reimbursement rate category. CBO projects that about 42 percent of lunches will be served in this category, a proportion that is consistent with early program data. This difference causes an upward reestimate of $85 million.

The remainder of the reestimate ($195 million) is due to differences in the assumed rate of spending of current year budget authority. The Administration assumes that 84 percent of budget authority will be spent during the current year, while CBO assumes a 91 percent rate. Actual spending patterns during the past several years show that more than 90 percent of budget authority has been spent during the current year. Reestimates in 1983 and beyond are based only on these differences in assumed spending patterns. The Administration has included a proposal in the budget that will cause the Child Nutrition account to be no longer considered an entitlement.

Supplemental Security Income. The technical reestimate for SSI results from differences between CBO and the Administration in the current policy baseline and in estimated effects of proposed legislation. The following table shows these components of the technical reestimate.

Components of CBO's Technical Reestimate of SSI (Outlays in millions of dollars)

	1982	1983	1984	1985
Current Policy Baseline	-122	-217	-200	-262
Proposed Legislation	---	38	66	97
Total Technical Reestimate	-122	-179	-134	-165

The current policy baseline of CBO is lower than the Administration's because of lower projected recipient levels. CBO projects about 0.1 million fewer recipients than the Administration in fiscal year 1983 and 0.2 million fewer in fiscal year 1985 (see the table below). Applications for SSI dropped

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sharply and unexpectedly during the last half of 1981. Demographic factors explain some of this drop. The cohorts now aged 50-59 and 60-64, those most at risk of disability, have declined recently or are expected to exhibit reduced rates of growth over the next few years. Persons in these cohorts were born in the period spanning World War I and the depression. CBO has incorporated this drop in applications in its projections, while the Administration has not yet done so.

Projections of the Number of SSI Recipients (Average monthly number in millions)

	1981 a/	1982	1983	1984	1985
Administration	3.7	3.7	3.6	3.6	3.6
CBO	3.7	3.6	3.5	3.5	3.4

a/ Actual.

The President's budget includes eight proposals estimated to save $286 million in 1983 and $708 million by 1985. CBO has reduced these savings to reflect the lower projected application and recipient levels discussed above. CBO's estimated savings are $97 million below the Administration's by fiscal year 1985.

Assistance Payments. Assistance payments include AFDC, child support enforcement, and the AFDC portion of the combined welfare administration proposal. In assistance payments, the technical reestimate reflects differences with the Administration in both the current policy baseline and in savings from proposed legislation. These differences are shown in the table below.

Technical differences between CBO and the Administration in the current policy baseline result from differences in numbers of recipients, average payments per recipient, and savings from the 1981 reconciliation act. As shown in the table below, these differences are partially offsetting.

Components of CBO's Technical Reestimate of Assistance Payments (Outlays in millions of dollars)

	1982	1983	1984	1985
Current Policy Baseline				
Number of recipients a/	-325	-175	-250	-250
Average payment b/	35	33	86	222
1981 reconciliation act	89	342	343	356
Subtotal	-201	200	179	328
Proposed Legislation	201	43	---	---
Total Technical Reestimate	---	243	179	328

a/ Estimated.

b/ The difference in average payment per recipient is estimated; Administration estimates are not available. Other unexplained differences in the current policy baseline are included here.

The models that CBO and the Administration use to project AFDC recipients differ in a number of technical respects. For example, they differ in the lag structure relating recipient levels to changes in unemployment rates and in the inclusion of other factors that might offset unemployment rate effects. Differences in projected recipient levels are shown in the table below. In fiscal year 1982, CBO projections show recipient levels well below the Administration's. Excluding the effects of the 1981 reconciliation act on recipient levels, CBO shows fewer recipients throughout the period. Much of this difference is because the Administration assumes a larger current increase in recipients from a given rise in the unemployment rate. Recipients in the most recent month for which data are available (November 1981) were 10.7 million, below CBO's estimate of 10.8 million for the fiscal year. Unemployment would have to cause an unusually sharp rise in recipients in the remainder of the year to more than offset the large declines in recipients in and after January 1982 that will result from the implementation of the 1981 reconciliation act provisions.

Projections of the Number of AFDC Recipients (Average monthly number in millions)

	1981 a/	1982	1983	1984	1985
Administration	11.1	11.0	10.6	10.4 b/	10.3 b/
CBO	11.1	10.8	10.7	10.4	10.2
Difference	0	-0.3	+0.1	*	-0.1

* Less than 50,000.

a/ Actual.

b/ Estimates provided by the Social Security Administration.

Projections by CBO and the Administration of average payments also differ. Before the last few years, average payments per recipient increased at a rate similar to the rate of increase in the CPI during the preceding year. However, rates of increase in average payments have recently fallen well below rates of increase in the preceding year's CPI. In fiscal year 1981, for example, the increase was about one-half that of the CPI. At the same time, the annual rate of increase in average payments has not fallen below 5 1/2 percent during the last five years. CBO's projection ranges from 5.0 to 6.1 percent a year, following recent experience. The Administration's projection is below CBO's by around two percentage points; this reflects only in part the Administration's lower CPI increases.

CBO shows lower savings from the 1981 reconciliation act throughout the period. In fiscal year 1982, CBO shows savings of about $650 million as compared with the Administration's $750 million; the Administration has recently lowered its estimated 1982 savings by more than $300 million. Beyond 1982, CBO shows savings of about $850-900 million a year. The Administration's savings are about $350 million a year higher. The major reason for CBO's lower savings is its assumption that the reconciliation act reductions in earnings disregards will reduce the work effort of recipients.

Lower savings are also shown for the Administration's proposed legislation. Proposed cuts in AFDC (and child support enforcement) are again sizable, totaling $1.3 billion in 1983. Because these proposals are extensive and not yet fully specified, CBO's only reestimate at this time is the deletion of $201 million in 1982 savings and a reduction of $43 million in 1983 savings as a result of expected implementation delays. A recent survey of states by the American Public Welfare Association found that at least 21 states applied for full or partial waivers of the 1981 reconciliation act's October 1 implementation date because of the need for legislative action to remove state law impediments, lawsuits, and/or administrative complications. An assumed July enactment date for the proposed legislation again makes implementation before October improbable, and is likely to delay implementation in 1983 in some states.

Energy Assistance. The CBO technical reestimates include the recently passed 1982 supplemental appropriation of $123 million for energy assistance, which was not requested by the Administration nor included in the February budget.

FUNCTION 700: VETERANS' BENEFITS AND SERVICES

(Outlays in millions of dollars)

	1982	1983	1984	1985
President's February Budget	24,155	24,383	25,584	26,948
Preliminary CBO Reestimates				
Different economic assumptions				
Compensation and Pensions	---	---	18	333
Technical reestimates				
Compensation	-35	21	84	164
Pensions	-305	-505	-576	-631
National Service Life Insurance	---	-31	-73	-74
Readjustment benefits	17	-145	-192	-218
Medical care	-73	73	---	---
Total Reestimates	-396	-587	-739	-426
President's Budget Reestimated	23,760	23,796	24,845	26,522

EXPLANATION OF PRELIMINARY CBO REESTIMATES

Different Economic Assumptions

Compensation and Pensions. The veterans' pension program established by Public Law 95-588 is indexed for inflation in the same manner as Social Security. While the compensation program is not indexed by law, it has historically received legislated cost-of-living increases each year, effective October 1 and usually equal to the percentage increase in pension benefits the previous June. The Administration's February budget assumes that annual cost-of-living increases will be provided for compensation benefits based on projected increases in the Consumer Price Index. Under CBO's economic assumptions, cost-of-living adjustments for these two programs in 1984 and 1985 would be somewhat higher than projected by the Administration.

Technical Reestimates

Compensation. Although the CBO estimate of compensation outlays is $35 million below the Administration's estimate for 1982, CBO estimates exceed those of the Administration by increasing amounts in 1983-1985.

The differences result from small and partially offsetting variances in the estimates of average benefits to veteran and survivor recipients. CBO assumes that the average compensation benefit to veterans will increase faster than estimated by the Veterans Administration (VA). This is expected to occur because of the worsening of the disabilities of these veterans as their average age increases. The effects of this phenomenon are partially offset by CBO's projection of slower growth in average benefits payable to survivor cases than assumed by the VA. The total number of dependent surviving children is falling, as many of them become too old to qualify as dependents. The number of new cases with dependent children is not sufficient to replace the age-related terminations, since the number of service-connected deaths during peacetime is low. This depresses the average number of dependents per case and, thus, the average benefit level. The differences in the estimates, however, are quite small; in 1985 the technical reestimate represents only slightly more than 1 percent of total anticipated program costs.

The President's 1983 budget also contains a legislative proposal to eliminate unemployability benefits to compensation recipients who also receive other federal disability or retirement benefits. The VA's estimate of the savings from this proposal, $282.5 million in 1984, is considerably lower than CBO would expect, based on the description of the proposal in the budget. CBO will be unable to develop an alternative estimate, however, until legislative language is available for the proposed amendment.

Pensions. The large technical reestimate in pension outlays results primarily from the substantially slower growth rate in the CBO projection of average benefits to Public Law 95-588 pension recipients than the growth rate reflected in the Administration's projection.

Projections of Average Benefit Levels For Public Law 95-588 Pension (In dollars)

	1982	1983	1984	1985
Administration Projection				
Veterans	4,736	4,854	4,946	5,032
Survivors	3,254	3,286	3,330	3,366
CBO Projection				
Veterans	4,076	4,104	4,127	4,190
Survivors	2,899	3,009	3,139	3,304

Few data are available on the components of the Administration's estimates, particularly in the outyears. However, the disparity in the projections of average benefit amounts is believed to result from different assumptions about the types of cases that will be added to the Public Law 95-588 rolls in future years and about the impact these cases will have on overall benefit levels.

CBO expects average benefit levels in current dollars to increase very slowly because of a decline in real average benefits resulting from a recent change in the mix of Public Law 95-588 pension accessions. Before 1981, the majority of added cases were those transferring their entitlement from the Public Law 86-211 pension. Transfer cases have generally had very low non-pension incomes and, therefore, have received relatively high benefits under the new pension program. In 1981, the balance tipped and the largest number of cases added to the rolls were new cases who had never before received a VA pension. These new cases tend to have higher nonpension incomes and, thus, receive lower than average pension benefits. Since the Public Law 95-588 pension is a fairly new program with a rapidly growing caseload, the impact on real average benefit levels (calculated in constant 1980 dollars) of the cases added to the rolls in any year is quite significant, as can be seen in the following table.

Cases and Real Average Monthly Benefits Under Public Law 95-588 Pension (Number in thousands, benefits in dollars)

	Cases in Current Payment Status at Start of Year		Cases Added During Year: Cases Transferring From P.L. 86-211		Cases Added During Year: Cases Not Previously Receiving Pension	
	Number	Average Monthly Benefits	Number	Average Monthly Benefits	Number	Average Monthly Benefits
1980	230	282	143	264	90	217
1981	427	265	66	275	102	218
1982 est.	525	270	47	255	125	216
1983 est.	598	253	18	240	163	214
1984 est.	659	241	10	228	185	211
1985 est.	714	234	7	215	203	207

NOTE: The effects of cost-of-living increases have been removed from actual and projected average benefit levels to show more clearly the trend in real average benefits.

The effect of this phenomenon is obvious in a comparison of actual average benefit levels in 1980 and 1981. Despite a 14.3 percent cost-of-living adjustment in June 1980 and an 11.2 percent adjustment in June 1981, the average benefit of Public Law 95-588 survivors increased by only 2.4 percent and the level for veterans by a mere 0.2 percent. The impact of new cases on the average benefit will diminish in the future as each year's new cases become a smaller proportion of the total caseload. However, the impact is unlikely to decline as fast as VA estimates would indicate.

National Service Life Insurance (NSLI). The CBO technical reestimate results from a lower CBO projection of outlays for new policy loans, as shown in the following table.

Outlays for NSLI Policy Loans (In millions of dollars)

	1982	1983	1984	1985
Administration	96.4	124.2	163.3	161.9
CBO	96.4	93.5	90.7	88.0

The Administration's estimate of outlays for policy loans reflects an increasing level of loan activity, despite the fact that the number of policies in force is expected to decline from 3,378,000 in 1982 to 3,101,000 in 1985. In addition, the decline in interest rates projected by both the Administration and CBO should exert further downward pressure on the loan level. As interest rates drop, the cost of borrowing elsewhere decreases relative to the loss of insurance coverage that results from borrowing against the policy.

Readjustment Benefits. The CBO estimate of outlays for these benefits is slightly higher than the Administration's estimate in 1982 but lower by a growing margin in 1983-1985. This is largely attributable to different projections of the number of veterans training under the G.I. Bill.

The number of veterans in training increased unexpectedly by 75,000 in the fall of 1981. This increase is believed to have resulted from the impact of the previous year's 10 percent increase in benefit rates, exaggerated by the sharp rise in the unemployment rate. Since no future increases are proposed by the President for education benefits, and since both CBO and the Administration are forecasting a steady decline in the unemployment rate, the CBO projection of outlays for readjustment benefits reflects a reemergence of the normal downward program trend after 1982. The Administration's projection, however, shows a lasting decrease in the rate of program decline, which would be inconsistent with historical experience.

Medical Care. The CBO technical reestimate of medical care outlays results from different assumptions regarding the speed with which appropriated funds will be spent. CBO expects a somewhat slower expenditure of the 1982 appropriation for this account consistent with historical experience. The CBO reestimate, therefore, lowers 1982 outlays and raises 1983 outlays by the same amount.

FUNCTION 750: ADMINISTRATION OF JUSTICE

(Outlays in millions of dollars)

	1982	1983	1984	1985
President's February Budget	4,521	4,592	4,571	4,500
Preliminary CBO Reestimates				
Different economic assumptions	---	---	---	---
Technical reestimates	-29	8	---	---
Total Reestimates	-29	8	---	---
President's Budget Reestimated	4,492	4,600	4,600	4,500

EXPLANATION OF PRELIMINARY CBO REESTIMATES

Different Economic Assumptions

This function has no reestimates resulting from different economic assumptions.

Technical Reestimates

CBO has a number of relatively minor technical reestimates in this function that result primarily from the use of different assumptions about spending rates, especially spending from obligated balances. The net effect of these reestimates is quite small.

FUNCTION 800: GENERAL GOVERNMENT

(Outlays in millions of dollars)

	1982	1983	1984	1985
President's February Budget	5,146	5,008	5,210	4,886
Preliminary CBO Reestimates				
Different economic assumptions	---	---	---	---
Technical reestimates				
Legislative Branch	-47	---	---	---
Federal Buildings Fund	-107	42	51	88
Other	-7	---	---	---
Total Reestimates	-161	42	51	88
President's Budget Reestimated	4,985	5,050	5,261	4,974

EXPLANATION OF PRELIMINARY CBO REESTIMATES

Different Economic Assumptions

This function has no reestimates resulting from different economic assumptions.

Technical Reestimates

Legislative Branch. The CBO 1982 outlay estimate for the Legislative Branch is nearly $50 million below the estimate contained in the Administration's budget. This difference is the result of different assumptions about how quickly funds appropriated in 1982 will be disbursed and the level of 1982 outlays from previous years' appropriations. CBO expects somewhat slower spending based on recent actual experience with these appropriations. Estimating differences are negligible in 1983 through 1985.

Federal Buildings Fund. The CBO outlay estimates for this revolving fund are based on the fund's past spending patterns. In 1982, the Administration estimates positive outlays of $2.8 million; CBO's estimate is for negative outlays of -$104 million. Over the past several years, this fund has never shown positive outlays at the end of the fiscal year and CBO does not expect this spending pattern to change.

An examination of previous estimates for this account reveals the difficulty the Administration has experienced in developing outlay estimates. In each year but one between 1976 and 1981, net outlays were lower than initially estimated in the President's January budget submission for that year. In all but two years, actual outlays were also significantly lower than revised estimates contained in the President's budget submission released in January of the current year. The following table compares actual outlays with the Administration's original estimate for each year contained in the President's annual budget submission and the revised estimate contained in the budget submission of the following January. The final two lines show the difference between actual outlays and the estimates of the two relevant January budget submissions.

Federal Buildings Fund: Differences Between Administration Budget Estimates and Actual Outlays, 1976-1981 (In millions of dollars)

	1976	1977	1978	1979	1980	1981
Original Estimate	-98	-10	17	-5	-138	-14
Revised Estimate	35	6	1	-127	-146	-12
Actual Outlays	-105	-122	-165	-56	-54	-154
Difference A (actual outlays minus original estimate)	-7	-112	-182	-51	84	-140
Difference B (actual outlays minus revised estimate)	-140	-128	-166	71	92	-142

For 1983-1985, CBO estimates that net outlays from this fund will continue to be negative, but less so than projected in the President's February budget. Receipts and reimbursements received by the fund are expected to increase significantly as a result of planned increases in standard user charges beginning in 1983, but CBO expects that service costs will rise somewhat faster than projected by the Administration.

FUNCTION 850: GENERAL PURPOSE FISCAL ASSISTANCE

(Outlays in millions of dollars)

	1982	1983	1984	1985
President's February Budget	6,417	6,686	6,788	7,090
Preliminary CBO Reestimates				
Different economic assumptions	---	---	---	---
Technical reestimates				
BLM, Misc. Perm. Approp.	-123	-228	-224	-356
Forest Service, Perm. Approp.	---	-48	-123	-163
Other	-17	---	---	---
Total Reestimates	-140	-275	-347	-519
President's Budget Reestimated	6,277	6,410	6,441	6,571

EXPLANATION OF PRELIMINARY CBO REESTIMATES

Different Economic Assumptions

This function has no reestimates resulting from different economic assumptions.

Technical Reestimates

Bureau of Land Management, Miscellaneous Permanent Appropriations. Payments are made to state and local units of government based on percentages of the federal government's receipts from revenue-producing activities on certain federal lands. More than 80 percent of the payments made through this account are for federal receipts from bonuses, royalties, and rentals under the Mineral Leasing Act. Under the provisions of this act, Alaska receives 90 percent of federal receipts from minerals activity on public lands in that state; the other states receive 50 percent. The balance of federal receipts for these activities are deposited in the Land and Water Resources Reclamation Fund and the miscellaneous receipts of the Treasury.

Approximately 20 percent of the payments made through this account are payments to counties in Oregon and California. These payments represent 50 percent reimbursement for federal receipts resulting from the sale of timber on grant lands located in the counties.

The CBO 1982 estimate of mineral leasing receipts is nearly $200 million lower than the Administration's latest estimate. These receipts are recorded as offsetting outlays in function 300. In later years, CBO's estimates for mineral leasing receipts generally reflect a more moderate increase than that estimated for the February budget. The CBO estimates of mineral leasing payments to localities reflect the lower receipt estimates discussed in function 300. The 1982 estimate is approximately 35 percent lower than the President's.

The CBO estimates for the sale of timber are also lower than those of the Administration. CBO's estimated increases in timber prices in function 300 are more moderate in 1982 and 1983 than OMB's estimates. In 1984 through 1985, CBO's estimated rate of increase in timber receipts remains fairly constant, but OMB's diminishes. Therefore, the size of the difference between OMB and CBO receipt estimates, and the corresponding estimates for payments to counties, are smaller in 1984 and 1985, partially offsetting the larger differences for mineral leasing payments.

The balance of this account represents smaller payments to state and local governments for a variety of activities on federal lands within those jurisdictions. Overall, CBO estimates 1985 payments to state and local governments as increasing by more than 50 percent above the 1981 level. The Administration estimates a 235 percent increase.

Forest Service, Permanent Appropriations. Payments are made to state and local entities for reimbursement of revenues received by the federal government for activities on property owned by the Department of Agriculture that lies within the local jurisdiction. An annual payment is also made to the state of Minnesota for distribution to certain counties. This payment is equal to 0.75 percent of the appraised value of Superior National Forest lands located in those counties. Most of the payments, however, represent 25 percent of funds received from national forests for timber sales. Because the 1982 payment is based on actual 1981 receipts, CBO and OMB have the same estimates for this account in 1982. The CBO estimates for 1983 through 1985 are lower than those of the Administration. This is because CBO's timber receipt estimates in function 300 are lower than the Administration's as a result of different assumptions about the price and volume of timber sales. The estimate of payments to the states for Forest Service lands reflects CBO's assumptions regarding timber receipts, with a one-year lag.

FUNCTION 900: INTEREST

(Outlays in millions of dollars)

	1982	1983	1984	1985
President's February Budget	99,095	112,536	116,185	119,726
Preliminary CBO Reestimates				
Different economic assumptions				
Interest on the public debt	1,143	1,749	9,418	6,543
IRS refunds	---	---	270	373
Interest from off-budget agencies	-50	-44	-63	-142
Tax and loan accounts	-141	-239	-281	-197
Technical reestimates				
Interest on the public debt	1,064	4,292	5,791	6,652
Interest from off-budget agencies	7	-208	662	555
Effects of higher deficits				
Different economic assumptions	287	928	2,530	4,661
Technical reestimates	439	2,833	6,197	9,864
Total Reestimates	2,750	9,311	24,524	28,309
President's Budget Reestimated	101,845	121,847	140,709	148,035

EXPLANATION OF PRELIMINARY CBO REESTIMATES

Different Economic Assumptions

Interest on the Public Debt. CBO interest rate assumptions are higher than those of the Administration in all fiscal years. Higher rates cause higher interest outlays both for financing current deficits and for refinancing existing debt. Average interest rates can be estimated by making certain assumptions about the composition of new financing and refinancing among various marketable Treasury issues (bills, notes, and bonds). Assuming no difference in the composition of new financing, average rates for the Administration and CBO assumptions are shown in the table below.

Interest Rates on Net New Financing (Fiscal year averages)

	1982	1983	1984	1985
Administration	12.4	12.4	10.6	9.9
CBO	12.7	12.7	12.1	10.1

CBO isolates the impact of higher interest rates by incorporating Administration projections of the total public debt level. The CBO reestimate for interest on the public debt is highest in fiscal year 1984, when the difference between interest rates is most pronounced. Higher interest rates in one year also carry over into future years, since the government must continue to pay interest on longer-term securities issued during previous years.

IRS Refunds. CBO's assumed higher interest rates also lead to higher outlays for interest on IRS refunds. The statutory interest rate for accruals in a particular calendar year is equal to the average prime rate charged by commercial banks during the preceding September, rounded to the nearest whole percent. Interest payments are a function of the statutory rates for the current year and previous years. The Administration and CBO forecasts for September 1982 are sufficiently close that the rounded interest rates for calendar year 1983 are equal. By September 1983, the forecasts differ sufficiently to produce different statutory rates and different estimates of interest costs beginning in fiscal year 1984. The Administration projects the statutory rate to be 12 percent in calendar year 1985, while CBO projects it to be 14 percent. The outlay differences in 1984 are smaller than those in 1985, since the 1984 refunds accrue interest at the same statutory rates for a longer period than do the 1985 refunds.

Interest from Off-Budget Agencies. The higher interest rates assumed by CBO reduce outlays (increase offsetting receipts) for interest from off-budget agencies. This interest consists almost entirely of that received from the Federal Financing Bank (FFB). FFB borrowing from the Treasury primarily includes long-term notes and bonds. While the FFB has over $100 billion of borrowings from the Treasury, most of the portfolio's interest rates were determined in past years. Differences in interest receipts because of different interest rate assumptions result only from net new borrowing from the Treasury and borrowing to refinance expiring securities.

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CBO's average long-term rates are higher over the projection period, resulting in higher receipts from the FFB. The difference in estimated receipts increases in later years, as more net new borrowing and refinancing occur at CBO's assumed interest rates. In 1982, CBO projects $50 million more in receipts, and this difference increases to $142 million in 1985.

Tax and Loan Accounts. CBO's projected higher interest rates also lead to lower outlays (higher offsetting receipts) for interest on tax and loan accounts. The major portion of the government's cash operating balance is held in the tax and loan accounts at commercial banks throughout the country. The accounts earn interest at the federal funds rate, which is subject to daily fluctuation. Both the Administration and CBO forecasts of the federal funds rate depend on the projected 91-day Treasury bill rate. With higher projected Treasury bill rates, CBO estimates higher interest receipts from the tax and loan accounts.

Interest Rates on Tax and Loan Accounts (Fiscal year averages)

	1982	1983	1984	1985
Administration a/	11.4	11.1	9.6	8.8
CBO b/	13.5	14.8	14.0	11.7

a/ 91-day Treasury bill rate.

b/ Estimated federal funds rate based on 91-day Treasury bill rate.

Technical Reestimates

Interest on the Public Debt. Part of this technical reestimate results from making outlays for interest on the public debt consistent with the Administration's published unified budget deficit figures. The deficits assumed by the Administration in estimating interest costs were lower than those ultimately incorporated in the budget.

The other part of CBO's technical reestimate reflects a higher level of interest payments to trust funds that hold government securities. CBO's estimating methodology is based on an examination of historical patterns of redemption of securities held by these trust funds. CBO assumes less refinancing of the long-term securities held by these trust funds, thus giving greater weight to current high interest rates and less weight to projected lower rates. Since this outlay is almost entirely an intragovernmental transaction, this portion of CBO's technical reestimate in function 900 is offset in subfunction 952 (interest received by certain trust funds).

Interest from Off-Budget Agencies. The Administration's interest calculation uses levels of lending and repayment activity that do not correspond to its published figures for off-budget accounts. The CBO reestimate corrects for this by using the published data. The reestimate also reflects consistency with CBO reestimates of FFB lending and repayment activity.

Effects of Higher Deficits

New financing requirements are projected to be higher because of CBO economic and technical reestimates of revenues and of other outlays (both on- and off-budget). This causes higher budget deficits and, therefore, higher outlays for interest on the public debt. The deficits resulting from the CBO reestimates (excluding the induced interest costs) exceed the Administration's estimates by about \$11.6 billion in 1982, \$24.6 billion in 1983, \$37.3 billion in 1984, and \$53.1 billion in 1985. The interest outlays resulting from these higher levels of deficit financing rise from about \$0.4 billion in 1982 to \$9.9 billion by 1985, as shown in the table presented at the start of this function.

FUNCTION 920: ALLOWANCES

(Outlays in millions of dollars)

	1982	1983	1984	1985
President's February Budget	-624	-1,257	-191	-369
Preliminary CBO Reestimates				
Different economic assumptions	---	---	---	---
Technical reestimates				
Civilian agency pay raises	---	71	556	564
Total Reestimates	---	71	556	564
Unevaluated Administration Estimates				
Fraud, waste, and abuse	(1,000)	(1,000)	(1,000)	(1,000)
Debt collection	(---)	(1,000)	(1,000)	(2,000)
President's Budget Reestimated	-624	-1,186	365	195

EXPLANATION OF PRELIMINARY CBO REESTIMATES

Different Economic Assumptions

This function has no reestimates resulting from different economic assumptions.

Technical Reestimates

Civilian Agency Pay Raises. The Administration's February budget estimates assume pay raises of 5 percent for all federal white- and blue-collar employees in each of the next three years. The estimates also assume a reduction in the federal civilian agency work force of approximately 75,000 full-time equivalent positions over the 1982-1984 period.

The pay raise cost figures provided by the Administration do not reflect the full cost of the anticipated pay adjustments for fiscal years 1983 through 1985. As can be seen in the table below, the Administration's estimate falls significantly short of CBO's full cost estimate, raising the possibility that the Administration is assuming partial absorption of pay raise costs, or that the payroll savings associated with proposed work force reductions are being placed in function 920. If, in fact, the latter is true, the saving would be double counted, since it is already contained in various accounts throughout the budget. For the sake of comparison, the table also provides CBO pay raise cost estimates assuming absorption rates of 70 percent (the level proposed by the Administration for 1982) and 40 percent (the average of the absorption rates actually adopted by the Congress over the last 10 years). The CBO reestimate of the Administration's budget is based on the assumption of 40 percent absorption in 1983-1987. While CBO's work force and pay rate adjustment assumptions are consistent with those used by the Administration, its 1982 payroll figure is approximately $2 billion higher than the Administration's. This results in an upward adjustment in the pay raise cost estimates of approximately $60 million in 1983, $160 million in 1984, and $240 million in 1985.

A Comparison of Administration and CBO Pay Raise Cost Estimates (In millions of dollars)

Fiscal Year	Administration	CBO at Full Cost	CBO with 70 Percent Absorption	CBO with 40 Percent Absorption
1983	743	1,405	371	814
1984	1,809	2,986	1,899	2,365
1985	3,331	4,645	3,508	3,895

UNEVALUATED ADMINISTRATION ESTIMATES

Fraud, Waste, and Abuse

The Administration's allowance estimates for the 1982-1985 period also contain $1 billion in annual savings from the elimination of fraud, waste, and abuse. According to the President's budget, these savings are expected to result from the vigorous program of the Inspectors General to uncover wrongdoing and inefficiency in various government activities. The Administration claims that savings will also result from increased cooperation between the Inspectors General and agency Assistant Secretaries for Management.

CBO has not reestimated the Administration's projections of the savings assumed to result from the reduction of fraud, waste, and abuse, but believes they are optimistic for two reasons. First, while the Administration asserts that an additional savings of $1 billion a year can be achieved through a more vigorous program of auditing and oversight, in most cases it has not provided for the additional personnel necessary to handle the increased workload. This can be seen in the following table, which provides a comparison of 1982 and 1983 staffing levels for a number of major Inspectors General offices. In each case, the Administration projects little or no change in the office's level of staffing for 1983. This raises serious doubts about the ability of the Inspectors General to perform the job asked of them by the Administration.

Offices of Inspectors General--Full-Time Staffing Levels

Department or Agency	1982	1983
Department of Agriculture	889	889
Department of Education (proposed Foundation for Educational Assistance)	292	292
Department of Health and Human Services	1,024	1,026
General Services Administration	509	499

A second reason CBO believes the allowance target is optimistic is that the Administration is already claiming savings from the elimination of fraud, waste, and abuse in various spending accounts throughout the budget--assistance payments, health care services, and Pell grants being notable examples. Since the budget estimates for these programs already reflect savings expected to result from the elimination of fraud, waste, and abuse, CBO believes that the additional savings estimated in function 920 will be difficult to achieve.

Debt Collection

The Administration has estimated savings of $13 billion (excluding tax receipts) in the period 1983-1987 as a result of improved debt collection procedures. Of this amount, $5 billion has been distributed to agency accounts within several functions of the budget. The undistributed balance is reflected in function 920.

The improved debt collection is to be achieved through both administrative and legislative initiatives. The administrative remedies planned by the Administration include examination and improved effectiveness of loan origination and servicing, better training for collections officials, faster and more effective litigation, and utilization of new tools and techniques--one of which is the contracting of certain debt collection functions to the private sector. Legislative proposals outlined in the Administration's budget include contracting for use of private-sector debt collection agencies, assessment of interest, penalties, and administrative charges on nontax debts, granting authority to refer credit information on delinquent debtors to credit bureaus, and requiring credit applicants to furnish their Social Security numbers to the government.

Both the General Accounting Office (GAO) and the Justice Department issued regulations in the Federal Claims Collection Standards in April 1979, which were soon followed by Treasury Department regulations, requiring agencies to charge interest and penalties on delinquent debt. According to the January 1981 report of the OMB Debt Collection Project, few agencies have adhered to these regulations. It is clear that the federal government has been lax in its debt collection efforts in the past.

The following table compares several debt collection estimates. The first column shows delinquent debt owed to the government as of September 30, 1981. The second column is CBO's estimate of the portion of that debt that was over 90 days delinquent on that date. The next column presents the Administration's 1983 estimates for those savings that have been distributed to agency accounts. (It does not include the additional $1 billion in undistributed allowances that the Administration allocates to function 920.) Finally, the table shows GAO's estimates of savings that could be achieved over several years (generally covering at least a four-year period).

The Administration's 1983 and 1984 estimates are the same for each agency except those for the Department of Housing and Urban Development, which increase to $150 million in 1984. The Administration estimate of $5,050 million in collections over five years appears optimistic but feasible when compared with the GAO collection estimates. The GAO paper on debt collection stresses, however, the need for maximum availability of resources and management tools, and states that current resources are insufficient. If resources are diverted from other activities, as suggested by the Administration, agencies will incur opportunity costs as effort in other programs is diminished. CBO's cost estimate of S. 1249, the Debt Collections Act of 1981, estimated that collection costs of $0.7 billion would be associated with the collection of $1.9 billion in delinquent debt. Under the bill's provisions, this would result in a net savings of $1.2 billion over a period of four and one-half years.

Debt Collection Estimates (In millions of dollars)

Department or Agency	Delinquent Debt a/	CBO Estimate of Delinquencies Aged 90 Days b/	Administration Estimate of Fiscal Year 1983 Savings	GAO Estimate of Savings Over Several Years c/
Department of Agriculture	1,976	1,646	250	675-1,150
Department of Commerce	244	237	30	N/A
Department of Defense	226	93	35	105-129
Department of Education	2,976	2,553	225	800-1,800
Department of Energy	115	60	35	N/A
Department of Health and Human Services	2,000	2,000	155	170-540
Department of Housing and Urban Development	1,293	1,293	125	362-633
Department of the Interior	59	43	25	N/A
Department of Labor	305	272	75	466-559
Department of State	12	12	5	N/A
Department of Transportation	141	138	5	N/A
National Aeronautics and Space Administration	*	*	25	N/A
Veterans Administration	1,042	913	150	340-640
Agency for International Development	77	53	35	N/A
Small Business Administration	1,698	1,499	175	900-1,300
All Other d/	255	193	---	N/A
Total	12,419	11,005	1,350	3,918-6,751

*Less than $500 million.

N/A = Not available.

a/ As of September 30, 1981. Supplied by the Office of Management and Budget.

b/ This estimate is based on the percentage of each agency's debt that was over 90 days delinquent on September 30, 1979. Actual 1981 data are not yet available.

c/ Derived from Enclosure IV of a Memorandum prepared by the Office of the Comptroller General, General Accounting Office, to Chairman James R. Jones, House Committee on the Budget, "Improved Administrative Practices Can Result in Further Budget Reductions (PAD-81-69)," (March 1981). These estimates were based on September 30, 1979, delinquency levels, which totaled approximately $10.9 billion for all departments and agencies other than the Department of the Treasury.

d/ Debts owed to the Treasury Department have been excluded because more than 90 percent of Treasury Department delinquencies are owed to the Internal Revenue Service, which has its own unique debt collection activities and programs.

Based on both the GAO and CBO estimates of debt collection activities, CBO believes that the Administration may be able to achieve the savings allocated to agencies, but that the additional $4 billion in undistributed savings estimated by the Administration over the 1983-1985 period appears to be optimistic. Moreover, unless significant new resources are allocated to the debt collection effort, it is doubtful that agencies will be able to realize the savings estimated by the Administration.

FUNCTION 950: UNDISTRIBUTED OFFSETTING RECEIPTS

(Outlays in millions of dollars)

	1982	1983	1984	1985
President's February Budget	-31,502	-43,474	-48,245	-50,043
Preliminary CBO Reestimates				
Different economic assumptions				
Interest rates	-56	-372	-57	-466
Technical reestimates				
Employer's share, employee retirement	390	253	-57	-291
Interest received by certain trust funds	-637	-3,233	-4,446	-3,578
Outer Continental Shelf receipts	900	5,200	4,800	3,200
Total Reestimates	597	1,847	240	-1,135
Unevaluated Administration Estimates				
Federal surplus property disposition	(---)	(1,000)	(4,000)	(4,000)
President's Budget Reestimated	-30,904	-41,627	-48,005	-51,178

EXPLANATION OF PRELIMINARY CBO REESTIMATES

Different Economic Assumptions

Interest Rates. Subfunction 952 consists of interest received on securities held by certain federal government trust funds. CBO projects higher interest rates than the Administration and, hence, larger offsetting receipts by these trust funds. The trust funds invest almost entirely in special issues of long-term securities, whose interest rates are typically linked to average rates on some defined portion of outstanding marketable long-term debt. These portfolios are largely fixed, but their composition changes over time as the trust funds purchase new securities and refinance expiring debt. Changes in trust fund interest receipts resulting from different interest rate assumptions occur with a lag of about one year, as the new purchases (and refinancing) gradually constitute a larger share of the portfolio. Different long-term interest rate assumptions in fiscal year 1982 lead to a small reestimate in that year and a larger reestimate in fiscal year 1983. The Administration's and CBO's long-term interest rate assumptions are similar in fiscal year 1983, leading to only a small reestimate in 1984. Long-term interest rate assumptions for fiscal year 1984 and beyond diverge more widely, producing $466 million in higher interest receipts for fiscal year 1985.

Technical Reestimates

Employer's Share, Employee Retirement. The employer's share of employee retirement is the federal government's contribution to its retirement plans. About 70 percent of the payments are made to the Civil Service Retirement fund. The remaining payments are mostly to Social Security trust funds. In 1983, the Administration has proposed legislation to cover federal employees under Medicare. The estimated employer contributions for this proposal are $619 million in 1983, $844 million in 1984, and $933 million in 1985.

CBO estimates lower receipts than the Administration in 1982 and 1983 for the employer's share of employee retirement. Based on recent information from the Postal Service and receipts to date, CBO estimates Postal Service contributions to the Civil Service Retirement fund of $1.8 billion in fiscal year 1982. In contrast, the Administration estimates 1982 payments of $2.2 billion--a 42 percent increase over the 1981 level.

Postal Service Contributions to Civil Service Retirement Fund (In millions of dollars)

	Actual		Estimate	
	1980	1981	1982	1983
Administration	1,489	1,537	2,188	2,192
CBO	1,489	1,537	1,751	1,792

From 1980 to 1981, Postal Service contributions increased by about 3 percent. The CBO estimate of a 14 percent increase from 1981 to 1982 reflects recent Postal Service pay raises. CBO estimated 1981 Postal Service contributions of $1.5 billion, while the Administration's estimate of $1.7 billion exceeded actual 1981 payments by about $200 million.

From 1983 to 1985, CBO's estimates of lower Postal Service payments are offset by increased receipts resulting from the federal pay raise. While CBO includes the additional receipts from the Administration's 5 percent federal pay raise assumption each year, the Administration includes receipts only in 1982. Because of these additional receipts from the federal pay raise, CBO estimates higher receipts than the Administration in 1984 and 1985.

Interest Received by Certain Trust Funds. This technical reestimate is the counterpart of another technical reestimate discussed in function 900. As noted in that earlier discussion, CBO assumes, based on historical data, a somewhat slower pattern of redemptions of securities held by the trust funds. This procedure accords greater weight to the relatively high interest rates in current portfolios, and less weight to future purchases at declining interest rates. The two reestimates are largely offsetting.

Outer Continental Shelf Receipts. CBO estimates that receipts from leasing activities on the Outer Continental Shelf will be substantially lower than the Administration estimates in fiscal years 1982-1985. CBO's technical reestimates result largely from different projections of bonus receipts from new lease sales and royalties received from leased lands. The Administration and CBO also make different assumptions about the release of bonus receipts held in escrow as a result of boundary disputes between the federal government and certain states. The following table shows the distribution of CBO's technical reestimate among these three factors.

Components of CBO's Technical Reestimate of OCS Receipts (In millions of dollars)

	1982	1983	1984	1985
Lower Bonus Receipts	1,100	4,000	3,700	1,900
Higher Rents and Royalties	-200	-300	-400	-200
No Escrow Releases	---	1,500	1,500	1,500
Total Reestimate	900	5,200	4,800	3,200

The Administration's and CBO's estimates of bonus receipts for 1982 and 1983 are based on assessments of the likely results of individual scheduled lease sales. For 1984 and beyond, the estimates are aggregate projections with no sale-by-sale detail. Three of the seven scheduled sales for 1982 have been held, and the resulting receipts are included in CBO's latest estimate. The February sale in the Gulf of Mexico was held after the preparation of the Administration's latest estimates. The Administration's and CBO's projections for bonus receipts are shown in the following table.

Projected Bonus Receipts from OCS Lease Sales (In millions of dollars)

	Actual		Projections			
	1980	1981	1982	1983	1984	1985
Administration	2.2	7.8	4.5	13.2	12.9	11.1
CBO	2.2	7.8	3.4	9.2	9.2	9.2

CBO's estimate of aggregate bonus receipts for 1982 is approximately $1.1 billion lower than the Administration's estimate of $4.5 billion as a result of different sale-by-sale bonus receipt estimates and different assumptions regarding collection of bonus payments within the fiscal year for sales occurring at the end of the year.

Both the Administration's and CBO's 1983-1985 bonus estimates are high and unprecedented. The record level to date occurred in 1981, with bonus receipts reaching $7.8 billion. The Administration's proposed accelerated schedule, however, will offer far more acreage than has been offered in the past and will include for the first time certain frontier acreage in which the industry has expressed interest.

The 1983 estimates include partial bonus payments for four sales--two held at the end of fiscal year 1982 and two at the end of 1983--and the entire payments from seven 1983 sales. Again, there are differences in the Administration's and CBO's assumptions regarding timing of end-of-year sales' bonus receipts as well as different estimates of receipts for the various sales. Included in the Administration's 1983 bonus receipt estimate are receipts for two sales of $5.6 billion and $3.2 billion (of the $6.5 billion total estimated for that end-of-the-fiscal-year sale), both in the Gulf of Mexico. Bonus receipts of this magnitude are greater than twice the record bonus receipts for any sale. (Bonuses of $2.3 billion in September 1980 and $2.4 billion in July 1981 were received for sales A62 and A66, respectively, both in the Gulf of Mexico.) CBO has estimated total receipts for those sales of $3.5 billion each. Acreage in the Gulf is generally considered attractive by industry. The last two sales in that area, however, have brought in relatively lower bonus receipts. (Sales 66 and 67 held in October 1981 and February 1982 yielded bonuses of $1.1 billion and $0.8 billion, respectively.) This might indicate an unwillingness by industry to bid large amounts for OCS leases under current economic conditions.

For 1984 and 1985, the Administration has estimated declining bonus receipts ($12.9 billion in 1983 and $11.1 billion in 1984). For purposes of estimating future OCS receipts based on the new leasing schedule, CBO has held the 1983 bonus estimate of $9.2 billion constant for 1984 and 1985.

CBO's estimate of royalty receipts is higher than the Administration's in every year, 1982 through 1985, as the net effect of higher gas (but lower oil) price estimates for those years.

CBO's estimate differs from the Administration's with regard to assumed releases of escrowed sums. Approximately $4 billion are currently in escrow accounts as a result of disputes between certain states and the federal government regarding potential resource drainage from state lands by lessees of federal OCS lands. In accordance with Section 8G of the OCS Lands Act, when the federal government leases a tract within three to six miles of the shore (an "8-G tract"), receipts must go into an escrow account until a decision has been reached in court regarding adequate compensation from federal royalties to reimburse states for lost resources. A release of $348 million to the federal government of sums that had been in escrow since 1956 will occur in 1982 as a result of a boundary dispute settlement in January 1982. The Administration estimates that $1.5 billion from sums escrowed for 8-G tracts will be released to the federal government in each year from 1983 through 1985. Because these cases have moved slowly through the courts, however, and decisions will likely be appealed once they are made, CBO has assumed no releases in any year, 1983 through 1985.

Both the Administration's and CBO's estimates for OCS receipts are subject to a wide margin of possible error. Various factors may result in lower bonus bids by industry. First, the proposed accelerated leasing schedule, which is not due to be formally in place until spring, may not be implemented exactly as introduced, or without delay. Various factors, including an October 1981 court decision regarding the existing schedule (promulgated by former Secretary of the Interior Cecil Andrus in July 1980), delayed the planned submission of a final proposed schedule by Interior Secretary James Watt from early calendar year 1982 to spring 1982. Opposition to parts of the schedule by states, environmental advocates, and other interested parties may result in further modification of the proposed schedule. Lease sale 73 off California, scheduled for January 1983 under the new leasing schedule (and for May 1983 under the old schedule), is likely to be postponed as a result of delays in tract selection because of environmental controversy. Environmental issues, long a stumbling block for lease sales off California, promise to surface with regard to certain Alaska tracts as well. Other objections have been voiced regarding Alaskan areas in which commercial fishing occurs. If lease offerings are not modified to reflect concerns of this type, industry wary of litigation may bid moderately for these controversial tracts.

Bonus bids will also respond to oil and gas prices and interest rates. Much of the area to be offered in the revised schedule is frontier acreage with little or no drilling experience to substantiate the magnitude and location of oil and gas reserves. Many of the areas are in deep water, far offshore, or in areas with harsh seasonal weather. As a result, industry will be forced to incur greater risks and exploration and drilling costs than in the past. Unless oil and gas prices are rising steadily, industry may not believe the additional risk and expense are worthwhile. In addition, interest rates--as long as they are high--will temper the size of bonus bids. Alternatively, it is possible that, as the cost of capital rises or remains high, companies will find that taking over another company is altogether a cheaper and more attractive means of replacing reserves than leasing on the OCS. Given the various factors that may result in low bonus bids by industry, CBO believes its more conservative estimate of bonus bids to be more realistic than the Administration's.

UNEVALUATED ADMINISTRATION ESTIMATES

Federal Surplus Property Disposition

The Administration's February budget estimates include anticipated receipts of $1 billion in fiscal year 1983 and $4 billion in both 1984 and 1985 through the sale of surplus property. This proposal is in addition to significant increases in estimated receipts included in function 800 for the disposal of excess real property controlled by the General Services Administration (GSA).

The most important aspect of this proposal is the Administration's plan to establish a Real Property Review Board to oversee federal property acquisition, utilization, and disposal practices. This board would identify unnecessary and underutilized federal property and encourage its disposal. The Administration's receipt estimates for this activity include $1 billion in receipts from GSA surplus property in 1983. In fiscal years 1984 and 1985, $2 billion each year is attributed to GSA and $2 billion to the Army Corps of Engineers and the Departments of Agriculture and the Interior. Under current procedures, it takes GSA an average of 18 months to dispose of surplus property. GSA's estimated annual receipts from this activity, which are recorded in function 800, already have been estimated to increase from $18 million in fiscal year 1981 to more than $250 million in 1983 and future years. Based on past experience, estimates of additional receipts of $5 billion over the 1983-1985 period from GSA disposal activities would appear to be very optimistic.

Because of the time involved in identifying and declaring property surplus, and because the Corps of Engineers and the Departments of Agriculture and the Interior do not have programs in place to facilitate this volume of property disposal, CBO believes that an estimate of significant receipts from surplus property disposition activity in those departments is also very optimistic.

OUTLAYS OF OFF-BUDGET FEDERAL ENTITIES

(Outlays in millions of dollars)

	1982	1983	1984	1985
President's February Budget	19,689	15,701	14,285	10,950
Preliminary CBO Reestimates				
Different economic assumptions	---	---	---	---
Technical reestimates				
Federal Financing Bank	552	776	931	1,082
Total Reestimates	552	776	931	1,082
President's Budget Reestimated	20,241	16,477	15,216	12,032

EXPLANATION OF PRELIMINARY CBO REESTIMATES

Different Economic Assumptions

There are no reestimates for off-budget entities resulting from different economic assumptions.

Technical Reestimates

The CBO reestimate of net outlays for the Federal Financing Bank (FFB) is the result of the reestimate to the Agricultural Credit Insurance Fund (Function 350). CBO assumes that net lending from the ACIF in the disaster loan program will result in additional loan asset sales to the FFB. This increase in sales will require additional borrowing from the Treasury and will result in additional net FFB outlays.

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CHAPTER V. THE ADMINISTRATION'S DEFENSE BUDGET

The President's 1983 budget projects rapid real growth in defense spending over the next five years. As a consequence, the defense share of the federal budget would climb steadily. Defense spending relative to the size of the economy would also grow, but would still remain below past levels of peacetime spending.

The Administration's defense budget proposes close to a doubling of annual appropriations over the next five years. New budget authority for national defense is projected to increase from $263 billion in 1983 to $408 billion in 1987, for a five-year total of approximately $1.7 trillion. In real terms, measured in constant 1983 dollars, this represents an average annual real growth of 7.4 percent using Administration assumptions about future rates of inflation.

Despite the fact that the Administration has requested a significant increase in resources for national defense, the Administration may in fact have underestimated projected funding for its program. Two major elements of this risk are the possibilities of higher inflation and of higher real cost growth than the Administration has assumed. For example, on the basis of CBO economic assumptions, maintaining the real growth assumed by the Administration for 1983-1987 would require additional budget authority of about $61 billion. Moreover, defense purchases have experienced significant cost growth in real terms in recent years. Recent Department of Defense (DoD) data suggest that real cost growth since 1975 for major weapons systems alone has averaged 3.5 percent per year. If such cost growth continues, the Administration's 1983-1987 funding estimates just to procure major weapons systems would have to be increased by a total of about $48 billion. Together, these items would increase aggregate 1983-1987 outlays for national defense by $62 billion.

This chapter discusses defense budget trends, proposed force structure changes, and the risks of underpricing. To illustrate the point that initial outlay effects of defense budget authority reductions can be relatively small and that realizing the total outlay savings typically requires several years, the last section of the chapter briefly examines the structure of 1983 defense outlays.

DEFENSE BUDGET GROWTH IN PERSPECTIVE

The Administration's defense budget for 1983-1987 is summarized in Table 28. The President has requested 1983 defense appropriations of $263 billion, a $44 billion or 20 percent increase over the 1982 estimated level. The February budget also includes a $2.6 billion supplemental appropriation for defense programs for fiscal year 1982.

Further large increases in defense appropriations are projected for 1984-1987. New budget authority to be provided through annual appropriations would rise to $291 billion in 1984, $338 billion in 1985, $375 billion in 1986, and $408 billion in 1987. Together with the requested 1983 appropriations, this represents close to a $1.7 trillion defense program over the next five years. This is almost $900 billion more for national defense funding than was provided by the Congress during the past five years (1978-1982). In real terms, this represents a 50 percent increase in defense appropriations over the next five years (1983-1987) in comparison to the past five years. Figure 11 portrays graphically the proposed rapid real growth in future Department of Defense appropriations.

Over the 1983-1987 period, Administration estimates of defense outlays would total $1.5 trillion. This represents a real increase of over 44 percent over total 1978-1982 outlays. In dollar terms, this is the largest peacetime five-year increase in defense outlays since World War II.

Relative to the total economy, Administration data indicate that the national defense function would increase from 6.1 percent of GNP in 1982 to 7.3 percent in 1986 and 1987. Figure 12 shows the post-World War II trends for defense outlays as a share of GNP and of total federal outlays. Over the 1983-1987 period, the Administration's proposed defense outlays would average 6.9 percent of GNP. This is higher than the average for the preceding five years, 1978-1982, during which the average defense share of GNP was 5.4 percent. It is lower, however, than the 10 percent average for several years following the Korean War.

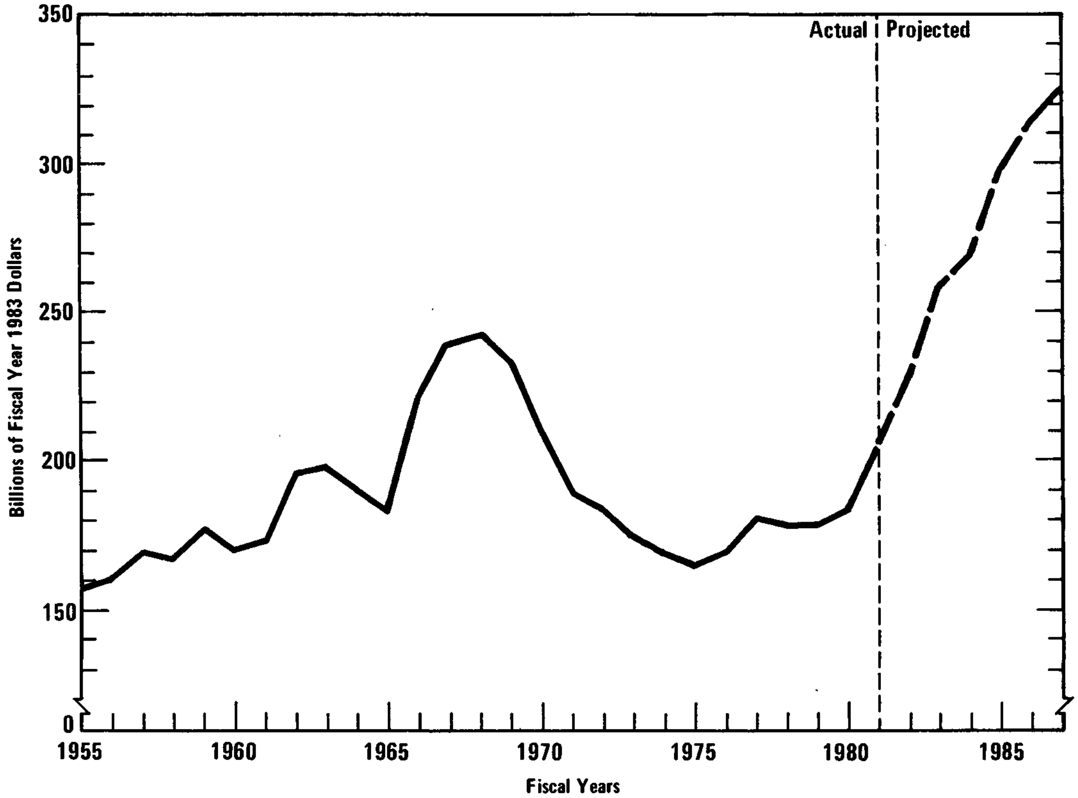
Relative to total federal unified budget outlays, national defense outlays from 1978 to 1982 were about 25 percent--the lowest share since World War II. The Administration's 1983 budget indicates that this share would increase to about 37 percent by 1987--a level last reached in 1971. In the post-World War II period, national defense as a percent of unified budget outlays exceeded 37 percent each peacetime year from 1954 to 1970.

TABLE 28. THE ADMINISTRATION'S DEFENSE BUDGET (By fiscal year, in billions of dollars)

	Actual 1981	Administration Estimates 1982	1983	1984	1985	1986	1987
				Budget Authority			
Department of Defense-Military							
Operations	58.2	62.7	70.3	73.8	83.1	92.4	101.0
Procurement	48.0	65.7	89.5	101.9	125.5	142.8	155.1
Other	72.2	85.7	97.7	109.0	122.3	131.6	143.8
Subtotal, DoD	178.4	214.1	257.5	284.7	330.9	366.8	399.9
Other National Defense	4.0	4.8	5.6	6.4	7.1	8.0	8.5
Total	182.4	218.9	263.0	291.0	338.0	374.9	408.4
				Outlays			
Department of Defense-Military							
Operations	52.0	60.5	67.2	72.4	80.5	89.8	98.5
Procurement	35.2	41.3	55.1	70.0	88.3	106.9	119.4
Other	68.9	81.0	93.6	104.6	116.7	127.3	138.1
Subtotal, DoD	156.1	182.8	215.9	247.0	285.5	324.0	356.0
Other National Defense	3.7	4.7	5.2	6.0	6.6	7.7	8.2
Total	159.8	187.5	221.1	253.0	292.1	331.7	364.2

Source: Office of Management and Budget.

Figure 11.
Budget Authority for the Department of Defense



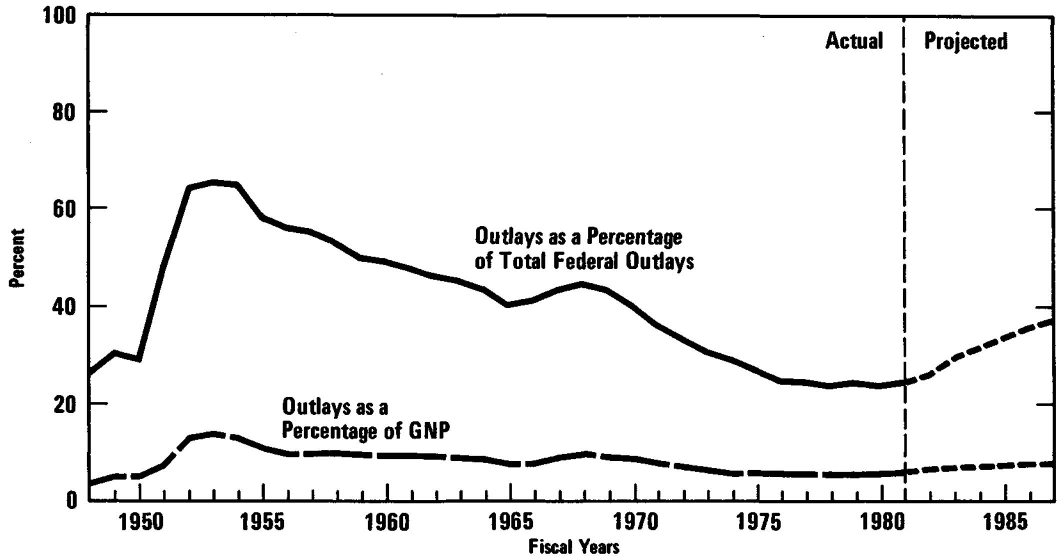
SOURCE: CBO calculations based on data from the Department of Defense.

GROWTH IN FORCES, MAJOR PURCHASES, AND DEVELOPMENT

In the short term, major changes are slated for the strategic nuclear forces and for general-purpose naval forces. Major strategic force changes for 1983 are the retirement of three squadrons of B-52D strategic bombers and eight Titan II intercontinental ballistic missile launchers, to be offset by delivery of one Trident submarine and deployment of 50 Minuteman III missiles in place of 50 Minuteman II missiles. In naval forces, there is to be a substantial increase in ships in 1983, with the planned delivery of the first reactivated battleship, plus increases in cruisers, destroyers, frigates, and nuclear attack submarines. In the longer term, major planned increases in force structure are consistent with the Administration goal of expanding Navy resources from the current 514 ships to over 600 ships by 1992.

Figure 12.

National Defense Outlays as a Percentage of Total Outlays and of GNP



SOURCES: For historical data, Department of Defense; for projections, *Budget of the United States Government, Fiscal Year 1983.*

The procurement budget for 1983 would rise over the 1982 level of $65.7 billion in budget authority by $24 billion--54 percent of the total $44 billion proposed defense increase in budget authority. The Administration's $89.5 billion program for 1983 contains 26.4 percent real growth over 1982 and is more than double the level of $43.6 billion projected by the previous Administration for 1983. Similarly, proposed 1983 research and development budget authority would increase by $4.2 billion over 1982 levels. This represents a real increase of 14.6 percent according to the Administration's economic assumptions and 12.8 percent using CBO's economic assumptions.

The Administration's 1983 budget stresses investment in major weapons systems, with 43 percent of the total budget allocated for the development and production of weapons systems, compared to 39 percent in 1982. The percentage is projected to increase each year, reaching 47 percent in 1987. Funding for Navy shipbuilding has real growth of 89 percent, with orders for two nuclear-powered aircraft carriers, two Trident submarines, and 21 other ships. The 1983 shipbuilding budget is the first installment of a five-year, 149-ship acquisition plan costing $85 billion, leading to a 600-ship Navy. A total of 654 aircraft would be procured in 1983, 33 more than 1982 and 48 percent more than planned for 1983 by the previous Administration. Major programs just getting under way include the second-year order of seven B-1 bombers, part of a $29 billion, 100-aircraft program, and the initial order of 50 C-5N cargo aircraft, part of a $4.6 billion program. The Administration has chosen to follow a "two strategic bomber" concept and is developing the so-called "Stealth" bomber to be operational in the early 1990s. In 1983, the Administration plans to procure 852 strategic and theater nuclear missiles. Table 29 summarizes major force, manpower, and procurement levels for 1982 and 1983.

TABLE 29. SUMMARY OF MAJOR FORCES, MANPOWER, AND PROCUREMENT LEVELS (By fiscal year, in units)

	1982	1983
Forces		
Strategic bomber squadrons	25	22
Land-based intercontinental ballistic missiles	1,052	1,044
Sea-based intercontinental ballistic missiles	544	568
Active divisions	19	19
Major warships	369	385
Tactical airwings	41	42
Manpower		
Active duty endstrength (personnel in thousands)	2,110	2,148
Civilian endstrength (personnel in thousands)	1,033	1,035
Procurement		
Navy ships	24	25
Aircraft	621	654
Strategic and theater nuclear missiles	675	852
Tactical missiles	27,699	53,984
Armored vehicles	1,509	3,000

SOURCE: Compiled by CBO from data supplied by the Department of Defense.

Ships

The Administration has developed an ambitious shipbuilding and conversion program. As Table 30 shows, this plan calls for 149 ships to be constructed, converted, modified, or leased between 1983 and 1987. The CBO estimates that more than $85 billion in Shipbuilding and Conversion (SCN) funds will be needed over the next five years to finance this plan. At an annual average of $17 billion, this is roughly double the level of SCN funds of recent years. At least a similar level of SCN funds will be needed in 1988 to ensure that the required 600-plus ships are available in the early 1990s.

A decision to fund two nuclear carriers in 1983 implies a commitment to 15 carrier battle groups and over 600 deployable ships. Beyond the large financial commitments this implies, it could also limit future operational decisions, because less money might be available to fund other forces before 1989 or 1990.

TABLE 30. ADMINISTRATION'S NAVY SHIPBUILDING PROGRAM FOR 1983-1987 (By fiscal year, in units procured)

	1983	1984	1985	1986	1987	Total
Trident Submarines	2	1	1	1	1	6
Nuclear Carrier Ships	2	--	--	--	--	2
Other Major Warships a/	7	7	10	10	14	48
Amphibious Ships	1	2	2	2	3	10
Frigates	2	2	2	3	3	12
Mine Warfare	4	5	5	5	5	24
Auxiliaries	7	6	9	12	13	47
Total	25	23	29	33	39	149

SOURCE: Compiled by CBO from data supplied by the Department of Defense.

a/ Includes Service Life Extension Program for one conventional carrier in 1983, 1985, and 1987.

Supporting and defending each carrier battle group require additional ships, aircraft, and weapons. The CBO estimates that the acquisition cost of one carrier battle group is over $13 billion in 1983 budget authority. Of all carrier battle group components, the production of carriers requires the longest lead time; supporting ships and aircraft require less lead time. The additional costs of some of these elements are reflected in the 1983-1987 program. Additional funding will be required after 1987.

Aircraft

The Carter Administration's January 1981 plan for aircraft orders for 1982 and 1983 contained 780 aircraft. As a result of modifications to the 1982 budget, plus expanded order levels in 1983, total aircraft orders for the two years are now projected at 1,275. The largest single recipients of these increases are the Navy and Marine Corps, whose orders increase 94 percent. Air Force orders rise 65 percent. Overall, this increase of 495 aircraft for the two years is 63 percent higher than the level planned in January 1981, but it is a reduction of 96 aircraft from this Administration's first plans of March 1981. Table 31 shows the aircraft acquisition plan of the previous Administration (January 1981) as compared with the plans submitted by the current Administration.

TABLE 31. COMPARISON OF CARTER AND REAGAN ADMINISTRATION AIRCRAFT ACQUISITION PLANS, BY SERVICE (By fiscal year, in units procured)

	President's Program for 1982			President's Program for 1983		
	January 1981 Budget (Carter)	March 1981 Revisions (Reagan)	February 1982 Budget (Reagan)	January 1981 Budget (Carter)	March 1981 Revisions (Reagan)	February 1982 Budget (Reagan)
Army	86	110	127	145	179	156
Navy/Marine Corps	121	283	287	175	339	288
Air Force	130	254	207	123	206	210
Total	337	647	621	443	724	654

SOURCE: Compiled by CBO from data supplied by the Department of Defense.

Aside from the number of aircraft ordered, the start of two major new aircraft procurement programs distinguishes this Administration's plan markedly from that of the previous Administration.

- o The first eight orders in 1982-1983 for 100 B-1B strategic nuclear bombers, with an initial operational capability of 1986, at a total cost estimated by the Administration at more than $29 billion. The major strategic bomber decision is to acquire the B-1B now and to develop the so-called "Stealth" bomber (also called the Advanced Technology Bomber, or ATB) for deployment in the early 1990s.

- o The first two orders of 50 C-5N transport aircraft at a total cost of at least $4.6 billion. The major airlift decision is to abandon the CX(C-17) aircraft now, in favor of the C-5N.

In addition to these two new programs, the Administration has decided to increase significantly the total purchases, or "buys," of several other aircraft. For example, the F-15 fighter aircraft buy is increased by 610, the F-16 buy is increased by 937, and the KC-10 tanker buy is increased by 44. The impact of these increased buys will be felt both in the near and outyear periods, as the size of the annual orders rises and as production extends for several years.

The Administration's decision to acquire 44 additional new KC-10 tanker aircraft, while continuing to re-engine 300 KC-135 tanker aircraft, will yield a significant improvement in aerial tanker support capability plus some increase in airlift capability.

Missiles

Long range missile programs are greater than 1982 levels and equal to or greater than the levels projected by the previous Administration. An exception is the Army's Pershing II missile, for which the current Administration proposes to slow production in both 1982 and 1983 (see Table 32).

The MX missile is the only major new program in this area, with $4.5 billion in 1983 to continue development and initial production of nine missiles. Late in 1986, the first 40 of 100 MX missiles are to be initially deployed in existing Minuteman silos. Research will proceed on the long-term basing options, which include deep underground basing, continuous patrol aircraft, and ballistic missile defense. Since the indecision on long-term basing creates great uncertainty about the ultimate cost of the program, total basing costs may not be fully reflected in the Administration program.

TABLE 32. COMPARISON OF CARTER AND REAGAN ADMINISTRATION PLANS TO ACQUIRE STRATEGIC AND THEATER NUCLEAR MISSILES, BY SERVICE (By fiscal year, in units procured)

	President's Program for 1982			President's Program for 1983		
	January 1981 Budget (Carter)	March 1981 Revisions (Reagan)	February 1982 Budget (Reagan)	January 1981 Budget (Carter)	March 1981 Revisions (Reagan)	February 1982 Budget (Reagan)
Army	39	39	21	134	134	91
Navy	120	160	160	135	165	192
Air Force	494	494	494	569	569	569
Total	653	693	675	838	868	852

SOURCE: Compiled by CBO from data supplied by the Department of Defense.

Unlike its plans for other weapons programs, the current Administration's 1983 program to purchase tactical missiles is not significantly different from that projected by the previous Administration. The proposed 1983 procurement plan for both the Air Force and the Navy is substantially lower than the 1983 program projected in January 1981 by the previous Administration, while that for the Army and Marine Corps is higher (see Table 33).

Armored Vehicles

Armored combat vehicles include tanks, fighting vehicles, light armored personnel carriers, and ancillary armored recovery vehicles. The Administration's armored combat vehicle program emphasizes acquisition of two "families" of vehicles:

- o Heavy combat vehicles dedicated for use by Army forces in Europe commited to NATO; and

TABLE 33. COMPARISON OF CARTER AND REAGAN ADMINISTRATION PLANS TO ACQUIRE TACTICAL MISSILES, BY SERVICE (By fiscal year, in units procured)

	President's Program for 1982			President's Program for 1983		
	January 1981 Budget (Carter)	March 1981 Revisions (Reagan)	February 1982 Budget (Reagan)	January 1981 Budget (Carter)	March 1981 Revisions (Reagan)	February 1982 Budget (Reagan)
Army	17,102	19,274	17,896	41,970	46,350	42,243
Navy	2,622	3,456	2,810	3,733	3,898	2,982
Marine Corps	561	3,806	3,542	370	370	2,773
Air Force	2,030	3,986	3,451	7,296	7,796	5,986
Total	22,315	30,522	27,699	53,369	58,414	53,984

SOURCE: Compiled by CBO from data supplied by the Department of Defense.

- Light armored vehicles for both the Army and the Marine Corps to strengthen the Rapid Deployment Force, primarily for deployment in the Middle East.

The major 1982 change with respect to heavy combat vehicles is the continued buildup in production levels of the new M-1 tank and its companion fighting vehicle (notwithstanding steadily escalating unit cost estimates and criticism about the technical performance of the vehicles). The fiscal year 1983 budget contains the first Army order of 258 light armored vehicles, plus second-year Marine Corps orders for 134 vehicles. The highly transportable light armored vehicle is a joint Army-Marine Corps effort to select an "off-the-shelf" vehicle for rapid delivery. As shown in Table 34, the Administration plans significant growth in armored vehicle procurement, compared with 1982 and previous plans for 1983.

Readiness Procurement

Readiness procurement programs include the spare parts, support equipment, and munitions necessary in peacetime to keep military forces

TABLE 34. COMPARISON OF CARTER AND REAGAN ADMINISTRATION PLANS TO ACQUIRE ARMORED COMBAT VEHICLES, BY SERVICE (By fiscal year, in units procured)

	President's Program for 1982			President's Program for 1983		
	January 1981 Budget (Carter)	March 1981 Revisions (Reagan)	February 1982 Budget (Reagan)	January 1981 Budget (Carter)	March 1981 Revisions (Reagan)	February 1982 Budget (Reagan)
Army	1,033	1,500	1,415	1,054	1,582	2,698
Marine Corps	102	102	94	226	226	302
Total	1,135	1,602	1,509	1,280	1,808	3,000

SOURCE: Compiled by CBO from data supplied by the Department of Defense.

ready for combat and to sustain their operation once combat begins. In past years, funding for readiness has often been traded off for aircraft, tanks, and ships. Both the current and previous Administrations made a commitment to raise funding levels for readiness.

As shown in Table 35, the funding level for readiness, when compared to the growth in funding for high-priced items, suggests that, the Air Force may have reduced readiness funding in favor of major new weapons--notably aircraft and strategic missiles. Although the Air Force has experienced significant improvements in spare parts and support equipment between 1981 and 1982, data reflect a real decline of 15 percent for these items between 1982 and 1983. The Air Force also will experience a 24.8 percent decline in munitions funding in these years. The growth in Army and Navy spare parts and support equipment is primarily the result of increased funding for aircraft parts and equipment. The increase in Navy/Marine Corps ammunition reflects 100 percent nominal growth in funding for Marine Corps ammunition, which may be the result of a one-time investment in prepositioned ammunition.

TABLE 35. PROPOSED FUNDING AND PERCENT OF REAL GROWTH FOR READINESS ITEMS, BY SERVICE (By fiscal year, in billions of dollars, and in percents)

	1982	1983	Percent of Real Growth
Spare Parts and Support Equipment			
Army	0.7	1.0	39.3
Navy/Marine Corps	3.2	3.8	12.1
Air Force	6.1	5.7	-15.0
Subtotal	10.0	10.6	-2.8
Munitions			
Army	2.3	2.6	0.3
Navy/Marine Corps	1.1	1.4	14.9
Air Force	1.1	0.9	-24.8
Subtotal	4.5	4.9	-1.8
Total	14.5	15.5	-2.5

SOURCE: Compiled by CBO from data supplied by the Department of Defense.

RISKS OF UNDERPRICING

Despite the fact that the Administration has requested significant increases in national defense funding, there is some risk that it may have underestimated the future costs of its program. The possibilities of higher inflation and higher real cost growth are the two main components of this risk. These two elements are discussed in this section. A third risk is that there may be significant additional expenditures needed to carry out the Administration's program. This factor is not discussed here because it is not quantifiable. The earlier MX discussion provided an example, however, in noting that the basing costs of the MX are probably not fully reflected in the Administration's program.

Potential Underestimation of Inflation

Under CBO's baseline economic assumptions, inflation rates would not subside as much as assumed for the February budget estimates. Higher than anticipated inflation could cause a scaling back of defense purchases to stay within available funds. Alternatively, additional funds would be needed to complete the Administration's plans for weapons procurement and other purchases. Using CBO's inflation assumptions for defense purchases requires increases of about $1.5 billion in budget authority in 1983 and a total of $61 billion more by 1987. About 65 percent of this increase would be allocated to investment programs; the remainder would affect operations. The difference between the Administration and CBO inflation assumptions for defense purchases varies from roughly 1.1 percent to 1.9 percent over the projection period (see Table 36). The annual distribution of the $61 billion figure is shown in Table 39 at the end of the chapter.

TABLE 36. COMPARISON OF CBO AND ADMINISTRATION INFLATION ASSUMPTIONS FOR DEFENSE PURCHASES (By fiscal year, budget authority deflators in percents)

	1983	1984	1985	1986	1987
CBO Assumptions	7.2	7.7	7.3	6.9	6.9
Administration's Assumptions	6.1	5.8	5.5	5.4	5.2

SOURCES: Congressional Budget Office and Department of Defense.

Real Cost Growth in Weapon Systems

Defense purchases have experienced significant real cost growth in recent years. This has occurred for a variety of reasons, including program changes (such as new specifications or revised production schedules) and underestimates of real resources (such as manufacturing hours and material costs). Although sufficient data are not available to estimate the full extent of this risk, it is possible to illustrate the effects on proposed major defense procurement funding. Recent DoD data indicate that real cost growth since 1975 in major weapons systems alone has averaged 3.5 percent per year (see Table 37). If the Administration's attempts to curb this cost growth fail and current trends continue, the Administration's estimates for major weapons systems procurement from 1983 to 1987 would have to be increased by a total of about $48 billion. Together, a $61 billion increase in budget authority under CBO inflation assumptions and this $48 billion increase in budget authority for potential real cost growth in major weapons procurement would increase national defense 1983-1987 budget authority by $109 billion and outlays by $62 billion.

TABLE 37. MAJOR WEAPONS SYSTEMS COST GROWTH PER UNIT (In percents)

Dates of Reports		Annual Growth Rate	Dates of Reports		Annual Growth Rate
March	1975	3.7	March	1979	3.4
March	1976	3.0	December	1979	3.6
December	1977	3.3	September	1980	3.7
December	1978	3.6	December	1980	3.9

SOURCES: Milton A. Margolis, "Improving Cost Estimating in the Department of Defense," Concepts, vol. 4, no. 2 (Spring 1981), p. 8 (data are derived from DoD Selected Acquisition Reports); and Stephen Gross, "Program Cost Growth in the Department of Defense as of December 31, 1980," (paper prepared by the Air Force Data Services Center, undated).

NOTE: These rates are adjusted to exclude the impact of quantity changes and inflation.

Recognizing the cost growth problem in major weapons systems, the Administration has undertaken a number of initiatives to restrain it. So far, these actions seem to have had little effect. The evidence presented below shows that real cost growth persisted at substantial levels during the first year of this Administration.

Table 38 provides cost growth data on 48 weapons systems by comparing costs as initially projected by the Administration in March 1981 against estimates contained in the 1983 budget. The table shows the approximate amount of real cost growth in major systems and notes that the defense program has absorbed a net amount of about $2.7 billion of cost growth since last year.

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TABLE 38. MAJOR WEAPONS SYSTEMS COST GROWTH IN THE 1983 PROGRAM (In millions of dollars and in percents)

Weapons System	Procurement Unit Cost March 1981	Procurement Unit Cost February 1982	Percent Increase	Cost Impact on 1983 Budget
HARM Missile, Air Force	0.31	0.78	152	97
Pershing II Missile	2.49	5.48	120	272
Phoenix Missile	1.13	2.31	104	127
AH-64 Helicopter	9.94	17.18	73	347
TR-1 Aircraft	25.18	38.85	54	55
Sparrow Missile, Navy	0.14	0.20	42	40
AV-8B Aircraft	28.34	39.67	40	204
HARM Missile, Navy	0.61	0.85	39	50
E-2C Aircraft	40.33	56.13	39	95
Patriot Missile	1.58	2.14	35	211
A-6E Aircraft	24.15	31.88	32	62
Standard Missile (RIM 66C)	0.62	0.82	32	30
SH-2F Helicopter	7.99	10.51	32	45
P-3C Aircraft	42.83	55.83	30	78
Standard Missile (RIM 67B)	0.63	0.81	29	67
CH-53E Helicopter	18.30	23.46	28	57
Sparrow Missile, Air Force	0.12	0.15	25	39
Cost Impact of 18 Other Systems Showing Unit Price Increases				1,554
Cost Impact of 13 Other Systems Showing Unit Price Decreases				-704
Total Impact of 48 Systems				2,725

SOURCE: Compiled by CBO from data supplied by the Department of Defense.

Another measure of cost growth is the number of weapon systems reported in the DoD Selected Acquisition Report (SAR) that have reached the cost ceilings imposed by the Nunn Amendment to the fiscal year 1982 Defense Authorization bill. The Nunn Amendment requires special reports to the Congress when the total unit costs of a SAR weapons system exceed by more than 15 percent the unit cost reported in the March 1981 SAR. The following 13 systems reflect total system unit cost increases of more than 25 percent over the past 10 months: SSN-688 nuclear attack submarine, F-14, Sparrow missile (Navy and Air Force versions), Trident I missile, five-inch guided projectile (SAL), F-15, F-16, Defense Satellite Communications System, Roland missile system, Patriot missile, Pershing II missile, and AH-64 helicopter. Three systems reflect total system unit cost increases of greater than 15 percent but less than 25 percent: FFG-7 guided missile frigate, Phoenix missile, and Maverick missile.

POTENTIAL REDUCTIONS

Much of the initial debate about the Administration's budget request has focused on the issue of reducing proposed national defense outlays. The variety of defense programs affords a wide range of potential options for spending reductions. Typically, many options produce initial outlay savings equal to only a fraction of the program cost reduction in the long run. The following classification of the source of defense outlays helps to illustrate this problem.

- o 32 percent ($72 billion) of national defense outlays for 1983 result from budget authority for 1982 (including proposed supplementals) and earlier years.

- o 62 percent ($138 billion) of 1983 outlays relate to proposed 1983 budget authority to pay active duty and retired military and civilian defense personnel; to support defense activities at 1982 levels; and to continue ongoing modernization, development, and construction programs.

- o 6 percent ($13 billion) of 1983 outlays result from 1983 budget authority for new activities, including new modernization programs and higher pay for defense personnel.

Excepting 1982 supplementals, to make any reduction in the $72 billion of 1983 outlays from prior-year budget authority requires cancellation, delay, or termination of programs already approved and, in many cases, already under contract. The preponderance of programs in this category represent fully funded investments that expend appropriations over several years. This characteristic, plus the fact that penalty costs are often incurred when the Administration has to cancel or modify existing contracts, means that 1983 outlay savings would be only a fraction of the ultimate outlay reductions from cutting such programs.

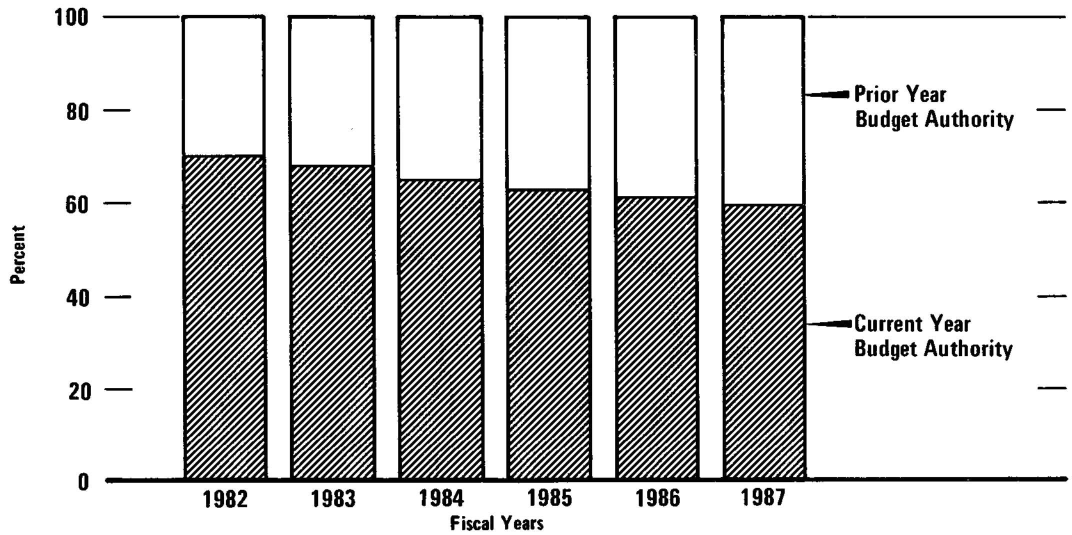
Similar problems affect the other two categories. For example, if none of the $89.5 billion budget authority requested for weapons systems procurement were appropriated in 1983, outlays in that year would decline by less than $11 billion, because so much of the budget authority will be spent after 1983, when most production occurs (see Function 050, Chapter IV). In general, to achieve a high proportion of 1983 outlay savings from cutting the Administration's 1983 request would usually require trimming personnel levels, pay increases (such as the proposed allowance for an October 1, 1982 federal pay raise), and relatively short lead time purchases such as fuel, ammunition, and maintenance-related items that affect readiness rather than modernization.

This condition will worsen in the future if the Administration program is enacted. The share of outlays from prior-years' funding in each years' projected outlays would rise steadily from 30 percent in 1982 to 41 percent in 1987 (see Figure 13). Thus, by approving programs with a larger modernization component, the Congress risks an outyear dilemma characterized by intensified competition for resources between modernization and readiness needs. If future defense budgets fall short of the real growth targets assumed here, the increasing share of the outlays required to finance previous years' programs will only further limit Congress's flexibility to establish or readjust priorities in defense programs.

To illustrate the outlay savings from average funding reductions, Table 39 provides calculations of savings from reduced real growth levels. The lower-growth options begin with a 1982 base that includes Congressional actions to date, plus supplementals for pay raises and military retired pay. Excluding all but the retired pay portion of the program supplemental saves $0.8 billion in 1983 alone. The Administration's estimates include annual real growth for budget authority as high as 12.3 percent (1982 to 1983) and as low as 2.3 percent (1986 to 1987), for an annual average of 6.1 percent (1982 to 1987). Compared to the Administration proposal, providing a steady 7 percent in annual real growth in budget authority would achieve savings between 1983 and 1987, because cumulatively, the program would be reduced and some outlays that occur earlier, when more real growth is concentrated in 1983, would be pushed beyond 1987. Greater outlay savings would accrue from holding annual real growth to 3 percent--$10 billion in 1983 and $157 billion for the 1983-1987 period (see Table 39). To achieve more than $10 billion savings in 1983 could mean little or no real growth in budget authority. For example, cutting the 1982 defense supplementals and the entire increase in national defense budget authority above the 1982 enacted level would save $8 billion and $55 billion in 1982 and 1983 budget authority, respectively, and about $21 billion in 1983 outlays. Denying military and civilian pay raises would increase 1983 outlay savings to $24 billion.

Figure 13.

Percentage of Defense Outlays Resulting from Current and Prior Year Budget Authority



SOURCE: Congressional Budget Office.

The outlay savings shown in Table 39 assume proportional reductions in all spending categories other than pay. The first-year savings rate--37 cents for every dollar of budget authority--reflects reductions in operations and investment that save about 75 cents and 12 cents, respectively, for every budget authority dollar; reducing personnel and pay raises would increase 1983 savings.

TABLE 39. COMPARISON OF THE PRESIDENT'S DEFENSE BUDGET WITH ALTERNATIVE BUDGET PROJECTIONS (In billions of dollars)

	1982		1983		1984		1985	
	BA	O	BA	O	BA	O	BA	O
President's Budget with CBO Technical Reestimates a/	218.2	190.8	263.2	222.9	290.8	254.6	337.7	293.5
Options (President's request with CBO inflation assumptions) b/	218.2	190.8	264.7	223.1	296.1	257.2	349.0	300.3
7 % real growth c/	216.0	190.2	247.1	216.3	283.1	246.1	323.9	282.8
5 % real growth c/	216.0	190.2	242.4	214.6	272.6	240.7	306.0	272.0
3 % real growth c/	216.0	190.2	237.8	212.9	262.4	235.5	288.9	261.6
Differences from the President's Request								
President's Request with CBO Inflation Assumptions	---	---	1.5	0.2	5.3	2.6	11.3	6.8
7 % real growth	-2.2	-0.6	-16.1	-6.6	-7.7	-8.5	-13.8	-10.7
5 % real growth	-2.2	-0.6	-20.8	-8.3	-18.2	-13.9	-31.7	-21.5
3 % real growth	-2.2	-0.6	-25.4	-10.0	-28.4	-19.1	-48.8	-31.9

(Continued)

SOURCE: Congressional Budget Office

a/ These estimates are based on the President's request with adjustments for CBO technical reestimates to budget authority (BA) and outlays (O); they are based on the Administration's economic assumptions. Budget authority differs from Administration estimates mainly because CBO anticipates lower growth in the military retiree population; secondly, Congressional scorekeeping conventions require that CBO count the $343 million shipbuilding reappropriation contained in the 1982 supplemental act as 1983 budget authority instead of 1982.

TABLE 39. (Continued)

	1986		1987		1983-1987 Total	
	BA	O	BA	O	BA	O
President's Budget with CBO Technical Reestimates a/	374.5	334.5	408.1	372.3	1,674.3	1,477.8
Options (President's request with CBO inflation assumptions) b/	392.4	346.7	433.5	390.7	1,735.7	1,518.0
7 % real growth c/	369.0	325.5	420.5	371.5	1,643.6	1,442.2
5 % real growth c/	342.2	307.6	382.7	344.8	1,545.9	1,379.7
3 % real growth c/	316.9	290.6	347.6	319.8	1,453.6	1,320.4
Differences from the President's Request						
President's Request with CBO Inflation Assumptions	17.9	12.2	25.4	18.4	61.4	40.2
7 % real growth	-5.5	-9.0	12.4	-0.8	-30.7	-35.6
5 % real growth	-32.3	-26.9	-25.4	-27.5	-128.4	-98.1
3 % real growth	-57.6	-43.9	-60.5	-52.5	-220.7	-157.4

b/ These estimates include additions to the President's program consistent with CBO's less optimistic inflation assumptions and more extensive application of specialized defense inflation estimates.

c/ These estimates assume that the reductions from the President's program will come mainly from the nonpay parts of the budget; assuming personnel or pay reductions would increase the outlay savings, but relatively little growth in the President's program occurs in these areas.

APPENDIX

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