HOUSE BUDGET COMMITTEE

Democratic Caucus

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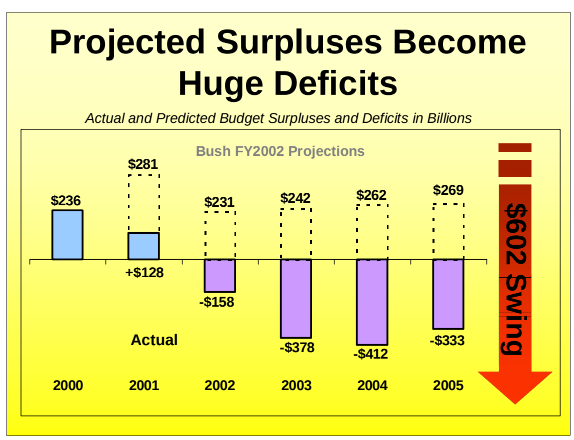
OMB's Mid-Session Review: Third Largest Deficit in History Is Little Reason to Cheer

The Administration today updated its projected deficit for 2005 to $333 billion – the third largest deficit in history. Excluding the Social Security trust fund surplus, the deficit is $505 billion. This deficit continues the most dramatic fiscal deterioration in our nation's history, with the $5.6 trillion ten-year projected surplus that President Bush inherited in 2001 now gone, and replaced by triple-digit deficits for as far as the eye can see.

Some claim that today's estimates represent meaningful progress on the deficit. While today's revision is positive relative to the Administration's February forecast, the fundamentals of the troubling long-term fiscal picture that has developed as a result of current policies unfortunately are unchanged.

Latest Numbers Confirm Harmful Effects of Republican Budgets

Third Largest Deficit in History Is Hardly Success — The $333 billion deficit for 2005 is the third worst in history. In fact, the Administration in the last three years – 2003, 2004, and 2005 – has posted the three worst deficits in the history of the country. By the President's own numbers, the deficit in 2010 – the last year for which it provides deficit figures – will still be $170 billion. Even these discouraging numbers are too optimistic, because the Administration's deficit calculations omit the full costs of some of its policies.



$600 Billion Deterioration Is Not Progress — some are claiming that today's estimate of a $333 billion deficit for 2005 represents progress. And it is welcome news that, like last year, the Administration's February estimates were overly pessimistic about the deficit and that today's number therefore looks better by comparison. But this change should not obscure the larger picture of fiscal deterioration under Republican control. When this Administration took office in 2001, it claimed that, under its proposed policies, the budget would be in *surplus* by $269 billion in

2005; today's estimate thus represents a deterioration over the last four years of $602 billion for 2005 alone.

Republican Claim of Slicing Deficit in Half Overstates the Case — Some claim that today's budget numbers confirm that they are on track to cut the deficit in half by 2009 – perhaps suggesting that, by extension, the deficit will be entirely eliminated over ten years. Yet, the Administration's budget repeatedly has failed to provide any deficit numbers after the first five years. The nonpartisan Congressional Budget Office (CBO), however, provided in March a ten-year estimate of the budget under the President's stated policies showing that after 2010, the deficit does not improve; on the contrary, the annual deficit never drops below $230 billion in the second five years. Simply put, the Administration has no plan to bring the budget back to balance. The true extent of the deficit over the five- and ten-year windows is worse than shown by either the Administration's or CBO's numbers. The Administration's budget submission – and therefore CBO's numbers, as well – omit or understate the full costs of significant items such as funding for the war, repair of the Alternative Minimum Tax (AMT), and the Administration's Social Security privatization plan.

President's Policies Make the Deficit Worse, Not Better — The continuing deterioration of the budget under Republican control should not come as a surprise because the Administration and the majority in Congress continue to propose policies that make the deficit worse, not better. In fact, over the next five years alone, the Administration's budget makes the deficit $106 billion worse than what the deficit would be if we made no changes at all, even according to the Administration's own numbers.

Deficit Numbers Revised Since February to Reflect Improvement in Receipts — The 2005 deficit estimate in today's report is $94 billion more favorable than the estimate included in the Administration's February budget and $61 billion better than CBO's March estimate. The difference is due in large part to tax receipts coming into the Treasury at a level higher than was estimated earlier this year. While the news that receipts are coming in at a higher level is welcome, one should not jump to the conclusion that this spike in revenue will be a recurring event. After all, much of the increase in revenue in the area of corporate taxes is a response to the expiration of bonus depreciation at the end of 2004 and a one-time provision in last October's tax legislation that encouraged the repatriation of multinational corporations' overseas earnings. Most of the gain in individual income taxes is concentrated in non-withheld income taxes; this suggests unexpectedly high revenues from capital gains and other investment income, which are more likely to be consistent with a one-time spike.

Tax Cuts Do Not Pay for Themselves — Moreover, the evidence simply does not support the claim that the Administration's tax agenda somehow is having a net positive impact on the budget, as some suggest. The estimated level of receipts for 2005 included in today's report remains $298 billion below what the Administration predicted in its first budget, submitted in 2001, which included its first tax cuts.

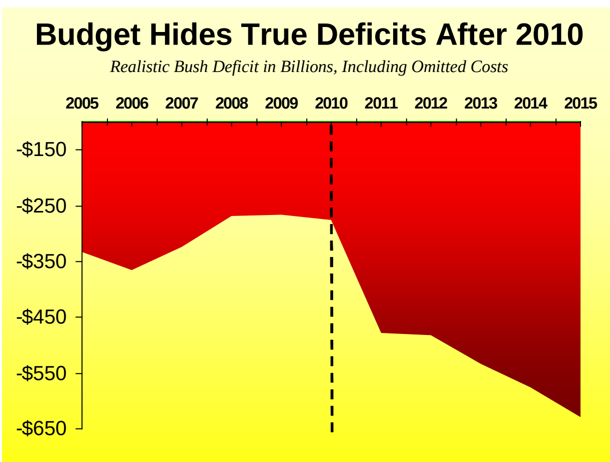
Claims That Tax Cuts Are Boosting the Economy Don't Add Up — Republicans claim that the increase in receipts demonstrates that the President's tax cuts have boosted the economy and therefore improved revenues. However, the empirical data do not support the claim that the higher receipts are linked to a surge in economic growth. In fact, for the first half of fiscal year 2005, economic growth has matched, not exceeded, the level that CBO predicted in January.

Meanwhile, despite the Administration's tax cuts, economic growth during the 13 quarters since the recession ended has been below what has occurred after other recessions since World War II. According to the Center on Budget and Policy Priorities, economic growth has averaged 3.3 percent annually during the current recovery, far less than the 4.3 percent rate averaged during the first 13 quarters after those previous recessions.

***By Contrast, Democrats Balance the Budget* —** The Clinton Administration converted record deficits into record surpluses. This year, Democrats in the House offered a budget that had smaller deficits than the majority budget and reached balance in 2012. We also support a return to the fiscally responsible budget enforcement rules of the 1990s, including requiring that any new tax cuts or entitlement spending increases be paid for. Republicans allowed the budget enforcement rules that worked in the 1990s to expire in 2002.

Deficit Outlook Is Even Worse Than Republicans Admit

***Omitted Costs Drive Deficits Even Higher* —** As troubling as they are, the deficit numbers discussed thus far do not reveal the full extent of the fiscal damage caused by Administration policies. Today's calculations omit or understate the full costs of the Administration's Social Security privatization plan, the long-term repair of the Alternative Minimum Tax (AMT), and realistic future funding for operations in Iraq and Afghanistan. When reasonable estimates of the costs for these items are factored in, along with the interest costs associated with borrowing this money, annual deficits under the Administration's policies never drop below $267 billion in any year over the next decade. By 2015, the deficit is more than $600 billion.



- ***Administration Budget Understates True Cost of Social Security Privatization* —** The President's plan for privatizing Social Security would simultaneously weaken Social Security and also make the deficit situation considerably worse. The deficit numbers in the Mid-Session Review reflect $78 billion for the first two years of this policy, but this amount understates the true magnitude of the President's plan because the accounts are phased in over several years. The costs of Social Security privatization balloon to a total of $754 billion through 2015, according to outside experts, and costs reach a total of $4.9 trillion over 20 years (2009-28).

- ***Administration Budget Omits Cost of Repair of Alternative Minimum Tax (AMT)* —** The President's budget provides no funding at all to address the growing problem of the AMT, which otherwise will affect increasing numbers of middle-income taxpayers in the years ahead. The likely ten-year cost for AMT repair is $642 billion, assuming that the President's tax cuts are extended, and $774 billion if the cost of additional interest on the debt is included.

- ***Administration Projection Omits Cost of War in Iraq and Afghanistan After 2006 —*** Based on a CBO analysis, costs for military operations in Iraq and Afghanistan could be as much as $334 billion more than the Administration projects over the next ten years. The Administration's spending projections underestimate the cost of these operations next year by assuming funding of only $50 billion and providing no funding for these efforts beyond 2006.

Deficits Weaken America

Administration Budget Continues to Use 100 Percent of Social Security Surplus — Since 2002, the Administration's budgets have used every penny of the Social Security trust fund's annual surplus – $637 billion in all – to help pay for its tax cuts and finance its deficits. The Administration's current budget continues this practice, spending another $1.1 trillion from the Social Security surplus (including interest income) over 2006-2010. Last month, House and Senate Republicans announced separate versions of a plan to spend 100 percent of Social Security's annual cash surpluses on private accounts that are designed to replace a portion of Social Security. This Congressional plan increases the publicly held debt by more than $1 trillion over the next ten years.

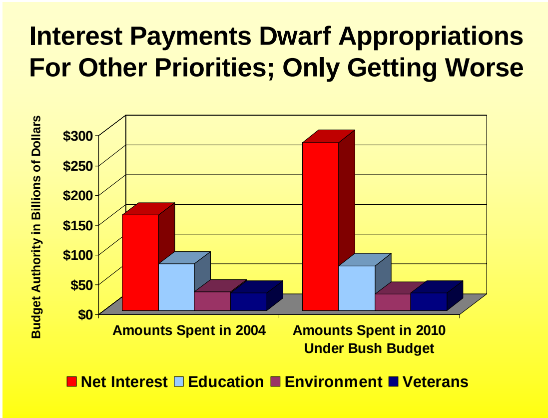
Policies Create A Mountain of Debt — These large deficits are producing a mountain of debt that is growing faster than our economy. In 2004, debt held by the public as a percentage of GDP was 37.2 percent. With a $333 billion deficit in 2005, this figure rises to 37.6 percent. Since President Bush took office, his policies already have required three increases in the statutory debt limit, most recently a November 2004 increase that took the debt limit to $8.2 trillion. The amount of these increases over just three years – $2.2 trillion, in total – is more than twice the amount of debt the that had built up from the founding of the United States more than 200 years ago to President Reagan taking office in 1981. The Administration's current budget will require yet another increase in the debt limit next year. Congressional action has acknowledged this reality, with the House already passing a $781 billion debt limit increase, which now awaits action by the Senate.

Republicans Increase the Debt Limit by $3.0 Trillion

Debt Limit Increases, Billions of Dollars

2002	**$450**
2003	**$984**
2004	**$800**
2005 Passed by House, Awaiting Senate Approval	**$781**
Total Increases	**$3,015**

Large Deficits Mean Resources Wasted Paying Interest on Debt — The growing burden of debt created under Administration policies means that the federal government is wasting resources paying interest on the debt, rather than using these resources to provide critical services and make important investments. In 2004, interest payments on the debt held by public investors consumed $160 billion, almost triple all appropriations for education, and more than five times the amount spent on either the environment or veterans' health care. That was $439 million per day wasted on interest payments on our publicly held debt. Under the President's budget, by 2010, these interest payments will rise to $282 billion, even by the Administration's own numbers. Including the cost of items omitted from the President's budget, the actual figure is likely to be even higher.



Deficits Weaken Our Economic Position — The large, long-term budget deficits that have accrued since President Bush took office undermine the long-term strength of our economy by crowding out private investment and risking upward pressure on interest rates. Meanwhile, the growing deficits have led to increased debt owed to foreign investors, which increases our vulnerability to economic instability from abroad.